

South Shore Health System, Inc. and Subsidiaries

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

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
South Shore Health System, Inc.
South Weymouth, Massachusetts

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

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

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

Emphasis of Matter

As discussed in Note 1 to the consolidated financial statements, in 2019 the Corporation adopted new accounting guidance related to the presentation of financial statements for not-for-profit entities, revenue recognition, and goodwill and other intangibles. Our opinion is not modified with respect to this matter.

Report on Supplemental Consolidating Schedules

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplemental consolidating schedules listed in the table of contents are presented for the purpose of additional analysis of the consolidated financial statements rather than to present the financial position, and results of operations of the individual companies, and are not a required part of the consolidated financial statements. These supplemental consolidating schedules are the responsibility of the Corporation's management and were derived from and relate directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such supplemental consolidating schedules have been subjected to the auditing procedures applied in our audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such supplemental consolidating schedules directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such supplemental consolidating schedules are fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Deloitte + Touche LLP

December 20, 2019

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS AS OF SEPTEMBER 30, 2019 AND 2018

	2019	2018		2019	2018
ASSETS			LIABILITIES		
CURRENT ASSETS:			CURRENT LIABILITIES:		
Cash and cash equivalents	\$ 47,153,204	\$ 54,171,280	Current portion of long-term debt	\$ 11,935,119	\$ 9,452,500
Short-term investments	51,825,346	56,453,064	Current portion of capital lease obligations	1,191,079	1,074,383
Current portion of assets whose use is limited	6,394,057	8,384,859	Accounts payable and accrued liabilities	112,582,171	88,001,833
Patient accounts receivable—less allowance for uncollectible accounts of \$14,751,000 in 2018	70,997,442	75,364,384	Current portion of estimated settlements with third-party payors	<u>9,118,335</u>	<u>18,521,742</u>
Inventories	8,497,464	8,960,417	Total current liabilities	134,826,704	117,050,458
Prepaid and other current assets	<u>25,240,044</u>	<u>21,244,435</u>	LONG-TERM DEBT—Net of current portion	256,905,679	236,685,848
Total current assets	<u>210,107,557</u>	<u>224,578,439</u>	CAPITAL LEASE OBLIGATIONS—Net of current portion	10,135,014	11,111,818
ASSETS WHOSE USE IS LIMITED OR RESTRICTED:			ESTIMATED SETTLEMENTS WITH THIRD-PARTY PAYORS—Net of current portion	16,766,408	36,220,278
Internally designated investments	217,841,753	209,220,561	MALPRACTICE LIABILITY	7,888,404	7,615,765
Donor-restricted investments	27,836,056	16,704,013	OTHER LONG-TERM LIABILITIES	<u>30,004,956</u>	<u>27,621,423</u>
Other investments	33,254,089	11,274,887	Total liabilities	<u>456,527,165</u>	<u>436,305,590</u>
Unexpended bond proceeds	<u>4,894,737</u>	<u>4,894,737</u>	COMMITMENTS AND CONTINGENCIES (Note 10)		
Total assets whose use is limited or restricted—net of current portion	<u>278,931,898</u>	<u>242,094,198</u>	NET ASSETS:		
PROPERTY AND EQUIPMENT—Net	316,136,600	309,691,618	Without donor restrictions	376,811,873	357,141,837
PENSION ASSET	7,831,231	8,386,051	With donor restrictions	<u>34,296,304</u>	<u>24,091,165</u>
GOODWILL—Net	24,120,112		Total net assets	<u>411,108,177</u>	<u>381,233,002</u>
INTANGIBLE ASSET	3,744,000		TOTAL	<u>\$ 867,635,342</u>	<u>\$ 817,538,592</u>
OTHER ASSETS	<u>26,763,944</u>	<u>32,788,286</u>			
TOTAL	<u>\$ 867,635,342</u>	<u>\$ 817,538,592</u>			

See notes to consolidated financial statements.

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

	2019	2018
NET ASSETS WITHOUT DONOR RESTRICTIONS:		
Deficiency of revenue over expenses	\$ (3,604,810)	\$ (2,394,265)
Change in net unrealized gains and losses on investments	4,758,924	10,922,492
Pension-related adjustments	499,680	14,492,877
Gain on interest rate swap agreement	67,340	67,341
Net assets released from restrictions used for purchase of property and equipment	<u>1,052,376</u>	<u>873,430</u>
Increase in net assets without donor restrictions	<u>2,773,510</u>	<u>23,961,875</u>
NET ASSETS WITH DONOR RESTRICTIONS:		
Contributions	13,387,000	6,620,520
Investment income	164,672	108,457
Change in net unrealized gains and losses on investments	(30,516)	77,984
Net assets released from restrictions for operations	(2,263,641)	(3,368,229)
Net assets released from restrictions for purchase of property and equipment	<u>(1,052,376)</u>	<u>(873,430)</u>
Increase in net assets with donor restrictions	<u>10,205,139</u>	<u>2,565,302</u>
INCREASE IN NET ASSETS	<u>12,978,649</u>	26,527,177
NET ASSETS—End of prior period	381,233,002	
Cumulative effect of adoption of ASU No. 2014-09 (Note 1)	<u>16,896,526</u>	
NET ASSETS—Beginning of year	<u>398,129,528</u>	<u>354,705,825</u>
NET ASSETS—End of year	<u>\$ 411,108,177</u>	<u>\$ 381,233,002</u>

See notes to consolidated financial statements.

(Concluded)

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES:		
Increase in net assets	\$ 29,875,175	\$ 26,527,177
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	33,710,616	30,150,488
Net unrealized and realized gains on investments, other than trading	(9,591,407)	(12,274,699)
Impairment of investments		114,606
Loss (gain) on interest rate swap agreement	3,300,815	(3,581,205)
Provision for bad debts		15,701,557
Pension-related adjustments	(499,680)	(14,492,877)
Amortization of deferred financing costs, premium, and discount	(487,694)	(508,389)
Restricted contributions and restricted investment income received	(13,551,672)	(6,728,977)
Increase (decrease) in cash resulting from a change in:		
Patient accounts receivable	5,508,814	(12,945,668)
Inventories	641,013	(1,343,353)
Prepaid expenses and other current assets	(4,210,796)	(2,586,244)
Trading securities	664,961	102,025
Other assets	6,017,358	(5,060,333)
Accounts payable and accrued liabilities	20,148,708	(3,557,834)
Pension asset	1,054,500	(3,942,376)
Estimated settlements with third-party payors—net	(28,646,529)	9,486,864
Malpractice liability	272,639	380,925
Other long-term liabilities	<u>3,463,540</u>	<u>2,734,924</u>
Net cash provided by operating activities	<u>47,670,361</u>	<u>18,176,611</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(36,053,201)	(36,787,686)
Cash paid in acquisition of Health Express net of cash received	(23,100,000)	
Purchases of investments	(51,349,386)	(39,118,011)
Proceeds from sale of investments	<u>30,056,653</u>	<u>55,248,011</u>
Net cash used in investing activities	<u>(80,445,934)</u>	<u>(20,657,686)</u>

(Continued)

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

	2019	2018
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from restricted contributions and restricted investment income	\$ 13,551,672	\$ 6,728,977
Payments on long-term debt	(9,452,500)	(9,504,167)
Payments on capital lease obligations	(1,084,318)	(906,034)
Proceeds from new debt obligations	23,100,000	
Increase in debt issue costs	<u>(357,357)</u>	<u> </u>
Net cash provided by (used in) financing activities	<u>25,757,497</u>	<u>(3,681,224)</u>
DECREASE IN CASH AND CASH EQUIVALENTS	(7,018,076)	(6,162,299)
CASH AND CASH EQUIVALENTS—Beginning of year	<u>54,171,280</u>	<u>60,333,579</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 47,153,204</u>	<u>\$ 54,171,280</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest	<u>\$ 12,011,378</u>	<u>\$ 11,382,574</u>
Equipment acquired through capital leases	<u>\$ 224,211</u>	<u>\$ 767,711</u>
Acquisitions funded through liabilities	<u>\$ 9,900,000</u>	<u>\$ -</u>
See notes to consolidated financial statements.		(Concluded)

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED SEPTEMBER 30, 2019 AND 2018

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General—The accompanying consolidated financial statements include the accounts of South Shore Health System, Inc. and subsidiaries (the “Corporation”). The assets of any one of the members of the consolidated group may not be available to meet the obligations of other entities in the group. Intercompany balances and transactions are eliminated in consolidation.

The Corporation’s operating subsidiaries include South Shore Hospital, Inc. (the “Hospital”), an acute-care hospital providing inpatient, outpatient, home care, and emergency care services; South Shore Property, Inc. (SSP); Coastal Medical Associates, Inc. (CMA), which includes South Shore Medical Center, Inc. (SSMC); Connected Care of Southeastern Massachusetts, Inc. (CCSM); South Shore Health Express, Inc. (SSHE), previously named Health Provider Services Organization (HPSO); MetroSouth Obstetrics & Gynecology, Inc. (MSOG); and Atlantic Women’s Health (AWH). MSOG and AWH are consolidated with the Hospital.

Basis of Presentation—The accompanying consolidated financial statements have been presented in conformity with accounting principles generally accepted in the United States of America (GAAP) consistent with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 954, *Health Care Entities*, and other pronouncements applicable to health care organizations.

Use of Estimates—The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The primary estimates relate to net patient service revenue, which includes explicit and implicit price concessions, allowance for uncollectible accounts, the valuation of investments in common collective trusts, valuation of interest rate swaps, goodwill, intangible assets, estimated settlements with third-party payors, postretirement benefits, liabilities and estimated insurance recoveries for malpractice, workers’ compensation, and employee health claims.

Cash and Cash Equivalents—Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less. The Corporation routinely invests its surplus operating funds in money market mutual funds. These funds generally invest in highly liquid US government and agency obligations. Temporary cash investments included in the Corporation’s investment accounts are reported as assets whose use is limited. The carrying amounts reported in the consolidated balance sheets approximate their fair value.

Patient Accounts Receivable—Patient accounts receivable are stated at estimated net realizable amounts from patients, third-party payors, and other insurers to which the Corporation expects to be entitled in exchange for providing patient care. Management

periodically reviews the adequacy of explicit and implicit price concessions (during 2019) or the allowance for uncollectible accounts (during 2018) based on historical experience, trends in health care coverage, and other collection indicators.

The Corporation's mission is to provide exceptional health care services to all persons regardless of their ability to pay. After all payments, discounts, and reasonable collection efforts have been exhausted, the Corporation follows established guidelines for placing certain past-due patient balances with collection agencies, subject to the terms of certain restrictions on collection efforts as determined by the Corporation. Accounts placed with collection agencies are written off and excluded from patient accounts receivable.

Inventories—Inventories are stated at the lower of cost, determined on the first-in, first-out method or net realizable value.

Assets Whose Use is Limited—Assets whose use is limited include donor-restricted investments, assets set aside by the board of directors (the "Board"), assets held for deferred compensation arrangements, assets held for purchase of property and equipment, and assets held by trustees under debt agreements. Internally designated assets may subsequently be used for other purposes at the Board's discretion.

Property and Equipment—Property and equipment are stated at cost, less accumulated depreciation. Gifts of long-lived assets, such as land, buildings, or equipment, are reported as unrestricted support and are excluded from the excess (deficiency) of revenue over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. In the absence of explicit donor stipulations about how long those assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service. Liabilities for the purchase of property and equipment aggregating approximately \$2,373,000 and \$2,731,000 remained in accounts payable and accrued liabilities at September 30, 2019 and 2018, respectively.

Depreciation is computed using the straight-line method over the estimated useful lives of depreciable assets. Equipment under capitalized leases is amortized using the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment as recommended by the American Hospital Association's guide, *Estimated Useful Lives of Depreciable Hospital Assets*. Such amortization is included with depreciation expense.

Impairment of Long-Lived Assets—Long-lived assets to be held and used are reviewed for impairment whenever circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value, less cost to sell. There were no impairments during the years ended September 30, 2019 and 2018.

Software Costs—Capitalized computer software costs include internally developed software. Costs incurred in developing and installing internal use software are expensed or capitalized depending on whether they are incurred in the preliminary project stage, application development stage, or postimplementation stage. Capitalized software costs and related accumulated amortization expenses are included in property and equipment.

Accounting for Postretirement Benefit Plans—The Corporation recognizes the overfunded or underfunded status of its defined benefit plan as an asset or liability in its consolidated balance sheets. Changes in the funded status of the defined benefit plan are reported as a change in unrestricted net assets presented below the excess of revenue over expenses in its consolidated statements of operations and changes in net assets in the year in which the changes occur.

Goodwill—Goodwill represents the future economic benefits arising from assets acquired in business combinations that are not individually identified and separately recognized. Goodwill is amortized on a straight-line basis over 10 years or less than 10 years if the Corporation determines that a shorter useful life is more appropriate. Goodwill is tested for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Fair value of a reporting unit is estimated using a combination of income-based and market-based valuation methodologies. An impairment is recorded if the carrying value of the goodwill exceeds its implied fair value. There were no impairments identified during 2019 or 2018.

Intangible Assets—Intangible assets include a tradename in connection with the acquisition of SSHE (see Note 4). Intangible assets with a definite life are amortized on a straight-line basis, with estimated useful lives of 10 years. Amortization of intangible assets is included in depreciation and amortization expense. The Corporation reviews the carrying value of its amortizable intangible assets only when impairment indicators are present. The Corporation evaluates intangible assets for impairment by comparing the estimates of undiscounted future cash flows to the carrying values of the related assets. Indefinite-lived intangible assets are evaluated for possible impairment at least annually or whenever events or changes in circumstances indicate the asset might be impaired. The intangible asset at September 30, 2019, is an indefinite-lived intangible asset. There were no impairments identified during 2019 or 2018.

Other Assets—Other assets as of September 30, 2019 and 2018, consisted of the following:

	2019	2018
Life insurance policies	\$ 15,770,358	\$ 15,826,065
Pledges receivable—net of current portion	4,403,641	5,358,008
Insurance recoveries	5,191,260	4,734,044
ACO risk sharing		5,235,500
Investment in joint ventures	798,751	726,061
Long-term portion of loans		125,267
Swap termination	89,051	96,035
Security deposits and other	<u>510,883</u>	<u>687,306</u>
Total other assets	<u>\$ 26,763,944</u>	<u>\$ 32,788,286</u>

The Corporation accounts for its interest in life insurance policies at the lower of the policies' cash surrender value or the discounted value of expected cash flows.

Accounts Payable and Accrued Liabilities—Accounts payable and accrued liabilities as of September 30, 2019 and 2018, consisted of the following:

	2019	2018
Accrued salaries, wages, and employee benefits	\$ 48,910,749	\$ 45,967,569
Accounts payable	53,362,232	33,356,327
Accrued workers compensation, current portion	2,440,000	2,360,000
Accrued interest	2,745,334	1,980,256
Accrued other	<u>5,123,856</u>	<u>4,337,681</u>
 Total	 <u>\$ 112,582,171</u>	 <u>\$ 88,001,833</u>

Estimated Third-Party Payor Receivable and Payable Settlements—The Corporation has agreements with payors that provide for payments at amounts different from established charges. The basis for payment under these agreements includes prospectively determined rates, cost reimbursement, and negotiated discounts from established charges. These estimated amounts are subject to further adjustments upon review by third-party payors (see Note 2).

Estimated Malpractice and Workers' Compensation Liabilities—The liabilities for estimated medical malpractice and workers' compensation claims include estimates of the ultimate cost for both reported claims and claims incurred but not reported.

Derivative Instruments—The Corporation manages a portion of its interest rate risk by entering into an interest rate swap agreement. This financial instrument is recorded at estimated fair value. The Corporation has not designated this contract as a hedging instrument and, accordingly, changes in its fair value are reported within the excess (deficiency) of revenue over expenses.

Other Long-Term Liabilities—Other long-term liabilities as of September 30, 2019 and 2018, consisted of the following:

	2019	2018
Workers' compensation liability	\$ 3,855,554	\$ 4,455,993
Executive and physician benefits payable	10,396,250	10,622,007
Interest rate swap contract	8,582,517	5,356,027
Community health initiative payable	1,236,667	1,969,280
Other	<u>5,933,968</u>	<u>5,218,116</u>
 Total other liabilities	 <u>\$ 30,004,956</u>	 <u>\$ 27,621,423</u>

The community health initiative payable is a result of an agreement between the Corporation and the Commonwealth of Massachusetts Department of Health and Human Services. The Corporation has agreed to pay certain amounts to support various community health initiatives. In addition to the amounts noted above, \$566,667 and \$402,520 at September 30, 2019 and 2018, respectively, is included in accounts payable and accrued liabilities in the accompanying consolidated balance sheets.

Net Assets without Donor Restrictions—Net assets without donor restrictions are available for use in general operations and are not subject to donor restrictions.

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

Revenue—As further discussed in Note 1, under recently adopted accounting pronouncements, Accounting Standard Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* was issued to clarify the principles for recognizing revenue, to remove inconsistencies and weaknesses in revenue recognition requirements, and to provide a more robust framework for addressing revenue issues. The Corporation adopted ASU No. 2014-09 using a modified retrospective method of application, and the Corporation's accounting policies related to revenues were revised accordingly effective October 1, 2018.

The Corporation recognizes revenues in the period in which the Corporation satisfies its performance obligations under contracts by transferring services to customers. Net operating revenues are recognized in the amounts to which the Corporation expects to be entitled, which are the transaction prices allocated to the distinct services.

Net Patient Service Revenue—The Corporation's main source of revenue is net patient service revenue principally for patients covered by Medicare, Medicaid, managed care, and other health plans, as well as certain uninsured patients. The Corporation's performance obligations are to provide health care services to the patients.

Allowance for Uncollectible Accounts—During the year ended September 30, 2018, patient accounts receivable were reduced by an allowance for uncollectible accounts. In evaluating the collectibility of accounts receivable, the Corporation analyzed its past history and identified trends for each of its major payor sources of revenue to estimate the appropriate allowance for uncollectible accounts and provision for bad debts. Management regularly reviewed data about these major payor sources of revenue in evaluating the sufficiency of the allowance for uncollectible accounts. For receivables associated with services provided to patients who have third-party coverage, the Corporation analyzed contractually due amounts and provided an allowance for uncollectible accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Corporation recorded a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted was charged off against the allowance for uncollectible accounts. For patient accounts receivable subsequent to the adoption of ASU No. 2014-09 on October 1, 2018, the estimated uncollectible amounts are generally

considered implicit price concessions that are a direct reduction to patient accounts receivable and revenue rather than an allowance for doubtful accounts.

Third-Party Payment Agreements—The Corporation has entered into payment agreements with Medicare, BlueCross BlueShield of Massachusetts (“BlueCross”), Medicaid, various commercial insurance carriers, HMOs, and preferred provider organizations. The basis for payment under these agreements varies and includes prospectively determined rates per discharge and per visit, discounts from established charges, cost (subject to limits), fee screens, and prospectively determined daily rates.

The Corporation formed CCSM on December 4, 2017, to operate an accountable care organization (ACO). During the year ended September 30, 2018, and through December 31, 2018, CCSM’s activity was in connection with its participation in the Medicare Next Generation ACO Participation Agreement (NGACO). The NGACO contract commenced on January 1, 2018, and ended on December 31, 2018. The contract terms required a settlement at the end of each contract year. At September 30, 2019 and 2018, the Corporation has included \$3,537,225 and \$10,471,000, respectively, in estimated settlements due to third-party payors, in the accompanying consolidated balance sheets, in connection with the 2018 estimated settlement related to the NGACO contract. In addition, at September 30, 2019 and 2018, the Corporation included \$0 and \$5,235,500, respectively, in other assets as an amount due from a third-party service provider in connection with the NGACO administration. The NGACO contract was replaced with the Medicare Shared Savings Program Basic Track E contract (Medicare Shared Savings contract), an advanced alternative payment model under CMS’ Pathways to Success. The Medicare Shared Savings Contract is effective July 1, 2019, through December 31, 2024. At September 30, 2019, the Corporation has included \$651,000 related to the Medicare Shared Savings contract in settlements due to third-party payors. Such amounts are estimated by management based on the information available as of the date of these consolidated financial statements. Actual amounts could differ from these estimates.

Other Operating Revenue—Other operating revenue includes, nonpatient service revenue, including leased employees, dining room revenue, joint venture income, certain legal settlements, certain interest income, and other nonpatient-related point of service revenues. For other revenue related to contracts with customers, the Corporation recognizes revenue in the period in which performance obligations under contracts are satisfied by transferring goods or services to our customers, in the amounts to which the Corporation expects to be entitled, which are the transaction prices allocated to the distinct services.

Capitalized Interest—Interest costs incurred on borrowed funds during the period of construction of capital assets, net of investment income earned on borrowed funds held by trustees, are capitalized as a component of the cost of acquiring capital assets. Interest on borrowed funds capitalized during the years ended September 30, 2019 and 2018, was \$434,683 and \$421,563, respectively.

Costs of Borrowing—Deferred financing costs and original issue discounts are amortized over the period that the related obligations are outstanding. Amortization of such costs during the periods of construction of capital assets is capitalized as a component of the cost of acquiring such assets.

Investments and Investment Income—Investments are stated at fair value. The Corporation reviews its investments to identify those for which market value is below cost. The Corporation then makes a determination as to whether the investments should be

considered other-than-temporarily impaired. For the years ended September 30, 2019 and 2018, the Corporation recognized \$0 and \$114,607, respectively, in losses related to declines in value that were determined by management to be other than temporary in nature.

Investment income and gains on proceeds of borrowings that are held by a trustee, to the extent not capitalized, and income and gains and losses from certain investments classified as trading securities are reported as other revenue. Such investment income totaled \$1,000,917 and \$1,469,791 in 2019 and 2018, respectively. Other investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in nonoperating gains and losses, unless the income or loss is restricted by donor or law.

Unrealized gains and losses on investments (other than those classified as trading securities) are excluded from the excess of revenue over expenses and reported as an increase or decrease in net assets, except that declines in fair value that are determined by management to be other than temporary are reported as realized losses.

Investments, in general, are exposed to various risks, such as interest rate, credit risk, and overall market volatility. As such, it is reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the consolidated balance sheets and consolidated statements of operations and changes in net assets.

Contributions—Unconditional promises to give cash and other assets to the Corporation are recognized at their fair value at the time of receipt. For financial reporting purposes, the Corporation distinguishes between contributions that are without donor restrictions and those that have restrictions placed on their use by the donors. Contributions restricted for additions to property and equipment are recorded as net assets with donor restrictions. When the restrictions have been met, these restricted contributions are recorded as net assets released from restrictions for property acquisitions. Contributions restricted for other purposes are reported as increases in net assets with donor restrictions if the restrictions are not met in the same reporting period. When such donor-imposed restrictions are met in subsequent reporting periods, they are reported as net assets released from restrictions and an increase to net assets without donor restrictions. Contributions for which donors have not stipulated restrictions are reported as other revenue.

Endowment assets include donor-restricted funds that the Corporation must hold in perpetuity or for a donor-specified period. The Corporation preserves the fair value of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor stipulations to the contrary. The Corporation retains in perpetuity (a) the original value of initial and subsequent gift amounts donated to the endowment and (b) any accumulations to the endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added. Donor-restricted amounts not retained in perpetuity are classified as net assets with donor restrictions until those amounts are appropriated for expenditure by the entity that received the donation. The Corporation considers the following factors in making determinations to appropriate or accumulate donor-restricted endowment funds:

- a. State law.
- b. The duration and preservation of the fund.

- c. The purposes of the donor-restricted endowment funds and how they relate to the Corporation's priorities for carrying out its mission within the communities it serves.
- d. General economic conditions.
- e. The possible effects of inflation and deflation.
- f. The expected total return from income and the appreciation of investments.
- g. Other resources available to the entity and its beneficiary, if applicable.
- h. The investment policies of the entity.

Consolidated Statements of Operations and Changes in Net Assets—For purposes of display, transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as revenue and expenses. Peripheral or incidental transactions are reported as nonoperating gains and losses.

Excess (Deficiency) of Revenue over Expenses—The consolidated statements of operations and changes in net assets include excess (deficiency) of revenue over expenses. Changes in net assets without donor restrictions, which are excluded from excess (deficiency) of revenue over expenses, consistent with industry practice, include changes in unrealized gains and losses on investments (other than those classified as trading securities and those on which other-than-temporary losses are recognized), contributions of long-lived assets (including assets acquired using pledges which, by donor restriction, were to be used for the purposes of acquiring such assets), and certain pension-related adjustments.

Income Tax Status—The Internal Revenue Service has previously determined that the Corporation and its subsidiaries are organizations as described in Section 501(c)(3) of the Internal Revenue Code (IRC) and are exempt from federal income taxes on related income pursuant to Section 501(a) of the IRC. Accordingly, no provision for income taxes has been made in the accompanying consolidated financial statements.

The Corporation follows the provisions of FASB ASC 740, *Income Taxes*, relating to accounting for uncertainty in income taxes. ASC 740 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements. It prescribes an uncertainty threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return.

The Corporation and its subsidiaries are subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

Recently Adopted Accounting Pronouncements—On October 1, 2018, the Corporation adopted ASU No. 2014-09, using a modified retrospective method of application to all contracts existing on October 1, 2018. The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

Adoption of ASU No. 2014-09 resulted in changes to the Corporation's presentation and disclosure of revenue primarily related to uninsured or underinsured patients. Prior to the adoption of ASU No. 2014-09, a significant portion of the Corporation's provision for bad

debts included within net patient service revenues related to self-pay patients, as well as copays, coinsurance amounts, and deductibles owed to the Corporation by patients with insurance. Under ASU No. 2014-09, the estimated uncollectible amounts due from these patients are generally considered implicit price concessions that are a direct reduction to net patient service revenue and not reflected separately as a provision for bad debts. For the year ended September 30, 2019, the Corporation recorded \$17,316,235 of implicit price concessions as a direct reduction of net patient service revenue that would have been recorded as provision for bad debts prior to the adoption of ASU No. 2014-09.

Under the new standard, subsequent changes in estimate of collectibility due to a change in the financial status of a payor, for example, a bankruptcy, will be recognized as bad debt expense in operating expenses under supplies and other in the consolidated statements of operations and changes in net assets. Additionally, upon adoption of ASU No. 2014-09 the allowance for uncollectible accounts of \$12,285,993 as of October 1, 2018, was reclassified as a component of patient accounts receivable. The adoption of ASU No. 2014-09 also resulted in a reduction of \$16,896,526 in estimated settlements with third-party payors, which has been reported as a cumulative effect adjustment in the statement of operations and changes in net assets for the year ended September 30, 2019. Other than these changes in presentation in the consolidated statement of operations and changes in net assets and the consolidated balance sheet, the adoption of ASU No. 2014-09 did not have a material impact on the consolidated results of operations and changes in net assets for the year ended September 30, 2019, and the Corporation does not expect it to have a material impact on its consolidated results of operations or changes in net assets on a prospective basis.

As part of the adoption of ASU No. 2014-09, the Corporation elected two of the available practical expedients provided for in the standard. First, the Corporation does not adjust the transaction price for any financing components as those were deemed to be insignificant. Additionally, the Corporation expenses all incremental customer contract acquisition costs as incurred because such costs are not material and would be amortized over a period less than one year. The ASU also requires an entity to disclose sufficient information to enable the financial statement users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.

Effective in the reporting period ended September 30, 2019, the Corporation adopted ASU No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*, to improve the financial reporting of not-for-profit entities. The guidance requires two categories of net assets instead of the previous three and enhances disclosures. The Corporation adopted the ASU retrospectively and has adjusted the presentation of its consolidated financial statements accordingly, except for the enhanced disclosures related to functional expenses and liquidity. Those disclosures have been omitted for the year ended September 30, 2018, the period presented prior to the period of adoption as permitted in the transition guidance. Although the adoption of ASU No. 2016-14 affected the presentation of the net asset sections in the consolidated financial statements, it had no impact on the total amount of net assets or deficiency of revenues over expenses shown in the consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-08, *Not-For-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which clarifies whether a transfer of assets is a contribution or an exchange transaction. This guidance is effective for the Corporation beginning October 1, 2018. The adoption of ASU No. 2018-08 did not have a significant impact to the consolidated financial statements.

Effective October 1, 2018, the Corporation adopted ASU No. 2019-06, *Intangibles—Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958)*, which extends the private company accounting alternatives on goodwill and certain identifiable intangible assets to not-for-profit entities. ASU No. 2019-06 allows a not-for-profit entity to amortize goodwill on a straight-line basis over 10 years, and test goodwill for impairment when a triggering event occurs that indicates that the fair value of the entity may be below its carrying amount. The ASU also allows the entity to subsume into goodwill and amortize customer-related intangible assets that are not capable of being sold or licensed independently from the other assets of a business and all noncompetition agreements acquired. As a result of the adoption of Topics 350 and 805, in connection with the acquisition of Health Express, Inc., the Corporation recorded \$26,433,000 in goodwill, which is being amortized over 10 years (see Note 9).

Upcoming Accounting Pronouncements—In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This guidance revises accounting related to (a) the classification and measurement of investments in equity securities and (b) the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments. The Corporation will adopt ASU No. 2016-01 in the reporting period ending September 30, 2020. The Corporation has not determined the impact the adoption of this standard will have on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. This guidance introduces a lessee model that brings substantially all leases into the consolidated balance sheet. In July 2018, the FASB issued ASU No. 2018-10, *Codification Improvements to Topic 842, Leases*, which clarifies some of the provisions of ASU No. 2016-02. In July 2018, the FASB issued ASU No. 2018-11, *Leases (Topic 842)—Targeted Improvements*, which provides additional transition methods when adopting ASU No. 2016-02, and also provides additional guidance to lessors with a practical expedient for separating components of a contract. This guidance is effective for the Corporation beginning October 1, 2019. The provisions of this update are to be applied using a modified retrospective approach. The Corporation plans to elect the practical expedients upon transition that will retain the lease classification and initial direct costs for any leases that exist prior to the adoption of the standard. The Corporation will not reassess whether any contracts entered into prior to adoption are leases. With the adoption of this standard, the Corporation expects to recognize material right-of-use assets and lease liabilities on the presentation of assets and liabilities, but does not expect a material impact to total net assets, or to the consolidated statements of operations and changes in net assets or cash flows.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This guidance adds or clarifies guidance on the classification of certain cash receipts and payments in the consolidated statement of cash flows. This guidance is effective for the Corporation for the annual reporting period ending September 30, 2020. The Corporation has not determined the impact the adoption of this standard will have on its consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows—Restricted Cash*, which requires that a statement of cash flows explain the change during the period in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The Corporation will adopt ASU No. 2016-18 in the reporting period beginning October 1, 2019. Upon adoption, the Corporation will include restricted cash and restricted cash equivalents with cash and cash equivalents

when reconciling the beginning-of-period and end-of-period total amounts shown in the consolidated statements of cash flows and related disclosures. Adoption will not have an impact on the consolidated balance sheets or consolidated statements of operations and changes in net assets.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*, which modifies the disclosure requirements on fair value measurements. This guidance is effective for the Corporation beginning October 1, 2020. The Corporation has not determined the impact the adoption of this standard will have on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-14, *Compensation—Retirement Benefits – Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*, which modifies the disclosure requirements for entities with defined benefit plans. This guidance is effective for the Corporation for the annual reporting period ending September 30, 2022. The Corporation has not determined the impact the adoption of this standard will have on its consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*, which helps entities evaluate the fees paid by a customer in a cloud computing arrangement by providing guidance for determining when an arrangement includes a software license. This guidance is effective for the Corporation for the annual reporting period ending September 30, 2022. The Corporation has not determined the impact the adoption of this standard will have on its consolidated financial statements.

2. NET PATIENT SERVICE REVENUE

Net patient service revenue is reported at the amount that reflects the consideration to which the Corporation expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others and includes variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, the Corporation bills patients and third-party payors several days after the services are performed or shortly after discharge. Revenues are recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services the Corporation provides. Revenues for performance obligations satisfied over time are recognized based on actual charges incurred in relation to total expected charges. The Corporation believes that this method provides a faithful depiction of the transfer of services over the term of performance obligations based on the inputs needed to satisfy the obligations. Generally, performance obligations satisfied over time relate to patients receiving inpatient acute care services. The Corporation measures performance obligations from admission to the point when there are no further services required for that patient, which is generally at the time of discharge. Revenues for performance obligations satisfied at a point in time, which generally relate to patients receiving outpatient services, are recognized when goods or services are provided and the Corporation does not believe the patient requires additional goods or services.

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

The Corporation determines the transaction price based on gross charges for goods and services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with the Corporation's policies, and implicit price concessions provided primarily to uninsured patients. The Corporation determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience using the portfolio approach. The Corporation determines its estimate of implicit price concessions based on its historical collection experience with classes of patients using a portfolio approach as a practical expedient to account for patient contracts as collective groups rather than individually. The financial statement effects of using this practical expedient are not materially different from an individual contract approach.

Agreements with third-party payors typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payors is as follows:

- **Medicare and Medicaid**—A significant portion of the Corporation's revenue is generated under agreements with Medicare and Medicaid. Payments for services covered by Medicare are based on federal regulations specific to the type of service provided. Medicare pays for most services at a prospective rate. Hospital facilities that meet certain requirements receive additional funds in partial payment for the cost of medical education and caring for the indigent. The rates for services covered by Medicaid are determined by the regulations of the state in which the beneficiary is a resident. Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount.
- **Other**—The Corporation has negotiated contracts with certain other third-party payors. Revenues under these contracts are based primarily on payment terms involving predetermined rates per diagnosis, per diem rates, discounted fee-for-service rates, and other similar contractual arrangements. The Corporation estimates the discounts for contractual allowances at the individual hospital level utilizing billing data on an individual patient basis. On a monthly basis, an estimate is made of the expected reimbursement for patients of managed care plans based on the applicable contract terms. In addition, the contracts the Corporation has with commercial payors also provide for retroactive audit and review of claims.

Settlements with third-party payors for retroactive adjustments due to audits, reviews, or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. The Corporation uses the expected value method of calculating estimated revenue, receivables, and liabilities as it

relates to third-party settlements. These settlements are estimated based on the terms of the payment agreement with the payor; correspondence from the payor; and the Corporation's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available), or as years are settled or are no longer subject to such audits, reviews, and investigations. In relation to certain government programs, primarily Medicare, this is generally referred to as the "cost report" filing and settlement process. For the years ended September 30, 2019 and 2018, net patient service revenues increased by \$4,639,110 and \$4,401,185, respectively, relating to changes in estimates for prior years' settlements from Medicare, Medicaid, and other programs.

Generally patients who are covered by third-party payors are responsible for related copays, coinsurance, and deductibles, which vary in amount. The Corporation also provides services to uninsured patients, and offers uninsured patients a discount from standard charges. The discount varies by geographical location, primarily based on the discounts negotiated with private third-party payors in that location. The total discounts provided to uninsured patients under this policy were \$2,272,745 and \$1,774,863 for the years ended September 30, 2019 and 2018, respectively. The Corporation estimates the transaction price for patients with copays, coinsurance, and deductibles, and for those who are uninsured based on historical collection experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense. Bad debt expense for the year ended September 30, 2019, was immaterial.

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

Patients who meet the Corporation's criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue.

Financing Component—The Corporation has elected the practical expedient allowed under ASC 606 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Corporation's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will generally be one year or less. However, the Corporation does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Contract costs—The Corporation has elected the practical expedient provided by ASC 340 and all incremental customer contract acquisition costs are expensed as they are incurred, as the amortization period of the asset that the Corporation otherwise would have recognized is one year or less in duration.

Revenue disclosures under ASC 606 include enhanced disclosures on the disaggregation of revenue. The composition of net patient care service revenue by payor and service line for the year ended September 30, 2019, is as follows:

		Ratio
Medicare	\$270,127,202	38 %
Medicaid	54,488,942	8
Managed care	300,204,128	43
Other third-party payors	72,221,079	10
Self-pay	<u>3,796,022</u>	<u>1</u>
Total net patient service revenue by payor	<u>\$700,837,373</u>	<u>100 %</u>
Hospital—inpatient	\$329,501,471	47
Hospital—outpatient	242,738,828	35
Physician services	78,342,851	11
Home health and hospice	37,808,567	5
Other	<u>12,445,656</u>	<u>2</u>
Total net patient service revenue by service line	<u>\$700,837,373</u>	<u>100 %</u>

Under ASC 605, the Corporation's revenue disclosure shows the sources of net patient service revenue before provision for uncollectible accounts for the year ended September 30, 2018, and is as follows:

		Ratio
Third-party payors	\$641,315,514	98 %
Self-pay	<u>10,572,213</u>	<u>2</u>
Net patient service revenue before provision for bad debts	<u>\$651,887,727</u>	<u>100 %</u>

3. CHARITY CARE

The Corporation provides care without charge or at amounts less than its established rates to patients who meet certain criteria under its charity care policy. Because the Corporation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue, except to the extent reimbursed by the Health Safety Net (HSN). The Corporation also supports the delivery of health care services to the indigent through payments to the HSN, which is operated by the Commonwealth of Massachusetts. The estimated cost of unreimbursed charity care provided by the Corporation and net payments to the HSN for charity care, provided by other institutions, aggregated to \$6,443,437 and \$6,155,922 in 2019 and 2018, respectively. The estimated cost of unreimbursed charity care provided by the Corporation is based on the ratio of its total

costs to total patient care charges applied to the amount of unreimbursed charity care charges.

4. BUSINESS ACQUISITIONS

Effective November 16, 2018 (date of acquisition), SSHE acquired Health Express LLC, ("Health Express"), an urgent care practice located in Massachusetts. The acquisition of Health Express is expected to have a positive impact on quality, access, and affordability of health care in southern Massachusetts. Consideration of \$33,000,000 was paid in connection with the acquisition in the form of \$23,100,000 in bank loans and \$9,900,000 in a promissory note due to the seller (see Note 10).

The consolidated statement of operations and changes in net assets for 2019 includes the operations of Health Express since the date of acquisition. The consolidated statement of operations and changes in net assets includes total operating revenues of approximately \$10,092,000 related to Health Express and deficiency of expenses over revenues of approximately \$(768,000).

The transaction was accounted for as an acquisition in accordance with ASU No. 2010-07, *Not for profit Entities: Mergers and Acquisitions*, which required the assets and liabilities of Health Express to be accounted for at fair value, as of the date of acquisition. The excess of the consideration paid over the fair value of the net assets at the date of acquisition of Health Express, which amounted to \$19,391,000, was recognized as goodwill. In accordance with ASU No. 2019-06 certain intangible assets have also been recorded as goodwill, including \$5,195,000 related to customer relationships and \$1,847,000 related to a noncompete agreement, resulting in total goodwill of \$26,433,000 being recorded at November 16, 2018.

The amounts assigned to the major assets and liabilities of Health Express at the date of acquisition are as follows:

Fair value of assets acquired:	
Current assets	\$ 5,060,000
Property and equipment	1,923,000
Liabilities assumed	<u>(416,000)</u>
Net assets at date of acquisition	<u>\$ 6,567,000</u>
Consideration paid	<u>\$ 33,000,000</u>
Goodwill	<u>\$ 26,433,000</u>

Costs related to the acquisition were not material and are included in supplies and other expenses in the consolidated statement of operations and changes in net assets for the years ended September 30, 2019 and 2018.

5. PLEDGES RECEIVABLE

Pledges receivable as of September 30, 2019 and 2018, consisted of the following:

	2019	2018
Amounts due in:		
Less than one year	\$ 1,942,271	\$ 1,955,204
One to five years	<u>5,329,495</u>	<u>7,019,500</u>
Unconditional promises to give before unamortized discount and allowance for uncollectible amounts	7,271,766	8,974,704
Less unamortized discount	<u>(278,968)</u>	<u>(805,153)</u>
Subtotal	6,992,798	8,169,551
Less allowance for uncollectible amounts	<u>(699,280)</u>	<u>(980,346)</u>
Net pledges receivable	<u>\$ 6,293,518</u>	<u>\$ 7,189,205</u>

Pledges receivable are reported in the consolidated balance sheets in other current assets and other assets and do not include conditional promises to give.

6. FINANCIAL ASSETS AND LIQUIDITY RESOURCES

As of September 30, 2019, financial assets and liquidity resources available within one year for general expenditure, such as operating expenses, scheduled principal payments on debt, and capital expenditures not financed with debt were as follows:

Financial assets:	
Cash and cash equivalents	\$ 47,153,204
Investments	269,667,099
Patient accounts receivable	70,997,442
Other receivables	<u>16,026,343</u>
	403,844,088
Liquidity resources—Unused line of credit	<u>20,000,000</u>
Total financial assets and liquidity resources available within one year	<u>\$ 423,844,088</u>

The Corporation considers board designated assets limited as to use to be available within one year for general expenditure.

7. INVESTMENTS AND ASSETS WHOSE USE IS LIMITED

Investments and assets whose use is limited as of September 30, 2019 and 2018, consisted of the following:

	2019	2018
Cash and money market investments	\$ 51,018,001	\$ 24,304,861
Mutual fund investments	81,287,914	80,726,982
Common collective trusts	<u>204,845,386</u>	<u>201,900,278</u>
Total investments and assets whose use is limited	<u>\$ 337,151,301</u>	<u>\$ 306,932,121</u>

Investment income and gains (losses) from investments for the years ended September 30, 2019 and 2018, consisted of the following:

	2019	2018
Investment income:		
Other revenue	\$ 1,000,917	\$ 1,469,791
Nonoperating gains and losses	2,461,397	1,504,259
Net assets with donor restriction	164,672	108,457
Gain on sales of investments—net	4,860,739	1,187,539
Impairment of investments		(114,607)
Change in net unrealized gains and losses on investments:		
Net assets without donor restriction	4,758,924	10,922,492
Net assets with donor restriction	<u>(30,516)</u>	<u>77,984</u>
Total	<u>\$ 13,216,133</u>	<u>\$ 15,155,915</u>

8. PROPERTY AND EQUIPMENT

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

	2019	2018
Land	\$ 5,728,236	\$ 5,728,236
Land improvements	4,136,152	4,124,903
Buildings	316,713,968	307,602,647
Fixed equipment	66,393,499	65,043,043
Major movable equipment	183,951,233	172,648,741
Internal use software	66,812,377	60,405,632
Construction in progress	14,223,114	6,441,346
Buildings and equipment under capital leases	18,245,647	18,021,436
Leasehold improvements	<u>20,532,068</u>	<u>19,729,099</u>
Total property and equipment	696,736,294	659,745,083
Less accumulated depreciation (including \$9,913,525 and \$8,685,692 of accumulated amortization of equipment under capital leases in 2019 and 2018, respectively)	<u>(380,599,694)</u>	<u>(350,053,465)</u>
Property and equipment—net	<u>\$ 316,136,600</u>	<u>\$ 309,691,618</u>

In November 2015, at a joint meeting of the health system boards (the "Health System Boards," consisting of the Corporation, the Hospital, CMA, and HPSO), \$236.5 million was authorized for the construction of a new critical care unit, refurbishment of the current unit into medical and surgical beds (the "Critical Care Project"), and the acquisition and implementation of electronic medical records and enterprise resource planning systems (the "IT Project"). The Health System Boards authorized \$203.4 million for the Critical Care Project, the IT Project, and other routine capital expenditures to be financed through long-term debt (see Note 10). The total amount of assets placed in service for the IT Project was \$93,571,716 as of September 30, 2019. The total amount of assets placed in service for the Critical Care Project was \$57,668,860 as of September 30, 2019.

9. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table provides information on changes in the carrying amount of goodwill and other intangible assets as of September 30, 2019 and 2018:

	2019	2018
Goodwill—net	<u>\$ 24,120,112</u>	<u>\$ -</u>
Other intangible assets—tradename	<u>\$ 3,744,000</u>	<u>\$ -</u>

The following table provides information regarding goodwill for the years ended September 30, 2019 and 2018:

	2019	2018
Amortized intangible assets—Goodwill	\$ 26,433,000	\$ -
Less accumulated amortization	<u>(2,312,888)</u>	<u> </u>
Goodwill—net	<u>\$ 24,120,112</u>	<u>\$ -</u>

The amortization period for the goodwill subject to amortization acquired during the year ended September 30, 2019, is 10 years. There are no expected residual values related to the goodwill.

Amortization expense related to goodwill was \$2,312,888 and \$0 during the years ended September 30, 2019 and 2018, respectively. The tradename is not subject to amortization and is subject to annual impairment testing.

The estimated future amortization of intangible assets with finite useful lives as of September 30, 2019, is as follows:

**Years Ending
September 30**

2020	\$ 2,643,300
2021	2,643,300
2022	2,643,300
2023	2,643,300
2024 and thereafter	13,546,913

10. LONG-TERM DEBT

Long-term debt as of September 30, 2019 and 2018, consisted of the following:

	2019	2018
South Shore Hospital, Series D	\$ 740,000	\$ 740,000
South Shore Hospital, Series 2012	56,050,833	60,291,667
South Shore Hospital, Series H	17,777,778	18,444,444
South Shore Hospital, Series I	110,005,000	112,520,000
South Shore Property, Series A	38,955,000	40,985,000
South Shore Health Express Seller Note	9,900,000	
South Shore Health Express Bank Loan	<u>23,100,000</u>	<u> </u>
Total	256,528,611	232,981,111
Unamortized premium	15,556,372	16,273,045
Unamortized issue costs	<u>(3,244,185)</u>	<u>(3,115,808)</u>
Total long-term debt	268,840,798	246,138,348
Less current portion	<u>11,935,119</u>	<u>9,452,500</u>
Long-term debt—net	<u>\$ 256,905,679</u>	<u>\$ 236,685,848</u>

The Corporation is obligated under various revenue bonds issued by the Massachusetts Development Finance Agency (MDFA, formerly the Massachusetts Health and Educational Facilities Authority). The terms of the related loan and trust agreements place limits on the incurrence of additional borrowings and contain various covenants and financial ratio requirements. Additionally, the Corporation has granted a lien on its revenue and gross receipts from all sources (other than gifts, grants, or bequests, which, by their terms, may not be legally available for debt service) as collateral for the borrowings. The Corporation is also required to maintain certain funds, which are held by trustees. Such funds are included with assets whose use is limited. The revenue bonds require periodic interest payments and principal payments to these funds held in trust, which are proportionate to the annual interest and principal payments or sinking fund installments.

In May 1992, the Corporation issued through MDFA \$53,825,000 of general obligation fixed-rate bonds ("Series D"). The proceeds were used to refund \$31,540,000 of Series B bonds and to fund various capital expenditures.

In February 2008, the Corporation issued through MDFA \$94,585,000 of tax-exempt variable rate revenue bonds ("Series G"), the proceeds of which were used to refund its Series E bonds in the amount of \$10,905,000; refund \$34,170,000 of Series F bonds; fund new capital expenditures, including the construction of a new parking garage; and pay issuance costs. The Series G bonds were refinanced in September 2012 through the issuance of an MDFA \$78,330,000 private placement with Sovereign Bank ("Series 2012"). Principal repayment on the debt is based on a 30-year amortization beginning in November 2012 with a final payment due in 2024. Interest payments are based on 67% of a 30-day London InterBank Offered Rate (LIBOR).

In May 2016, the Corporation issued through MDFA a \$20,000,000 private placement with Santander Bank for the construction of a new critical care unit and renovation of the existing critical care unit ("Series H"). Principal repayment on the debt is based on a 30-year amortization with payments beginning in June 2016. The bonds are subject to mandatory purchase on May 10, 2026, at 100% of the outstanding principal amount, plus accrued interest to the purchase date. Interest payments are based on 67% of a 30-day LIBOR.

In May 2016, the Corporation issued through MDFA \$117,245,000 of tax-exempt general obligation fixed-rate bonds ("Series I"). The bonds were used to refund \$17,310,000 of Series F bonds and \$17,916,667 of the Series 2011 private placement with Santander Bank, as well as fund systemwide enhancements to the Corporation's information technology (IT) platform, the construction of a new critical care unit and renovation of the existing critical care unit, and other miscellaneous capital projects.

In July 2008, SSP issued through MDFA \$45,000,000 of variable rate demand revenue bonds ("Series A"), the proceeds of which were used to fund the construction of the Ambulatory Cancer Center (ACC) and pay issuance costs. In 2010, SSP refinanced the Series A bonds through the issuance of tax-exempt private placement debt with Wells Fargo Bank (the "replacement debt"). The replacement debt bears interest at a fixed rate of 2.99% and is payable in interest only through maturity in June 2016, at which time the outstanding principal is due. In May 2016, the debt was refinanced again with Wells Fargo Bank with a fixed rate of 2.47% and a maturity date of March 2033. The Corporation has also provided a guarantee to Wells Fargo Bank as part of the debt replacement. The debt has been classified in the accompanying consolidated financial statements based on the replacement terms of the replacement debt.

On November 16, 2018, SSHE issued \$33,000,000 of debt to purchase Health Express (see Note 4). The debt is made up of a \$23,100,000 direct placement with Harbor One Bank and a \$9,900,000 subordinated promissory note with the seller. The bank loan matures on November 16, 2048, and bears interest at the one month LIBOR plus the applicable rate of 2.05% plus a supplemental margin which is based on average deposits SSHE holds at the bank (.20% for fiscal year 2019). The bank loan rate is guaranteed until November 2033, at which time the rate will need to be renegotiated through the maturity date of November 2048. Principal payments will commence on November 16, 2024, in equal monthly payments of principal sufficient to fully amortize the loan over 24 years together with accrued interest. Monthly interest payments on the \$23,100,000 balance commenced in December 2018. The promissory note is payable annually with seven equal principal payments beginning on November 16, 2019, and ending on November 16, 2025, with interest at 4% annually. The bank loan has various financial covenants, including debt service coverage ratios, liquidity requirements, and debt-to-revenue ratios and is secured by certain assets and revenues of the Corporation.

The Corporation's long-term debt bears interest and matures as follows:

Issue	Interest Rate	Rate at September 30, 2019	Final Maturity
Series I	4%–5%		2041
Series H	Variable	2.94 %	2046
Series 2012	Variable	2.92 %	2024
Series D	6.50 %		2022
Series A	2.47 %		2033
Seller Note	4.00 %		2025
Bank loan	Variable	4.30 %	2048
Average variable rate		3.61 %	

Funds held by trustees under debt agreements were composed of debt service funds of \$2,287,485 and unexpended bond funds of \$0 at September 30, 2019, and debt service funds of \$2,263,365 and unexpended bond funds of \$4,894,737 at September 30, 2018.

Interest Rate Swap Agreement—In October 2008, the Corporation entered into a fixed-pay LIBOR swap agreement with an original notional amount of \$94,065,000 with an investment bank to hedge possible future interest rate increases on the variable rate debt outstanding. The Corporation's fixed interest rate on the fixed-pay LIBOR swap was 3.325%. The Corporation in return received 67% of LIBOR (2.256% at September 30, 2019 and 2018) from the investment bank. The Corporation has elected not to apply hedge accounting to the swap. The (loss) gain on the swap of \$(3,300,815) and \$3,581,205 for the years ended September 30, 2019 and 2018, respectively, is included in nonoperating gains and losses in the accompanying consolidated statements of operations and changes in net assets. The fair value of the interest rate swap agreement of \$8,582,517 and \$5,356,027 at September 30, 2019 and 2018, respectively, is included in other long-term liabilities in the accompanying consolidated balance sheets.

The Hospital and the counterparty in the interest rate swap agreement are exposed to credit risk in the event of nonperformance or early termination of the agreements. Depending upon the market price and the counterparty's credit risk at the calculation date, the counterparty is required to either collateralize or insure any aggregate exposure in excess of \$100,000.

Line of Credit—The Corporation has a committed revolving line-of-credit agreement with a bank, under which the Corporation is permitted to borrow up to \$20,000,000 through July 31, 2020. Borrowings under the agreement bear interest at one of various rates, which are determined at the time of the borrowing, based upon the Corporation's election, and are unsecured. The Corporation did not borrow and had no outstanding amounts under the line of credit during 2019 or 2018.

Payments on Debt—Annual principal payments on long-term debt as of September 30, 2019, were as follows:

Years Ending September 30	
2020	\$ 11,935,119
2021	11,426,786
2022	11,513,452
2023	11,962,619
2024	12,419,286
Thereafter	<u>197,271,349</u>
Total	<u>\$256,528,611</u>

11. CAPITAL LEASE AND OPERATING LEASE OBLIGATIONS

The Corporation leases certain of its facilities and equipment under long-term capital leases expiring through 2029 and noncancelable operating leases expiring through 2034. The operating leases generally provide for renewal options and require that the Corporation pay its share of operating expenses. Future minimum annual lease payments under capital lease obligations and noncancelable operating leases as of September 30, 2019, were as follows:

Years Ending September 30	Capital Lease Obligations	Operating Leases
2020	\$ 2,413,456	\$ 6,323,488
2021	2,382,027	6,299,483
2022	2,134,014	5,999,993
2023	1,520,315	6,068,362
2024	1,374,043	6,234,579
Thereafter	<u>9,173,613</u>	<u>41,254,981</u>
Total	18,997,468	<u>\$72,180,886</u>
Less amounts representing interest	<u>7,671,375</u>	
	11,326,093	
Less current portion	<u>1,191,079</u>	
Total	<u>\$10,135,014</u>	

Rent expense under operating leases for the years ended September 30, 2019 and 2018, was approximately \$5,550,000 and \$5,530,000, respectively, and is recorded in supplies and other in the accompanying consolidated statements of operations and changes in net assets. Future minimum annual sublease receipts under noncancelable subleases are as follows:

**Years Ending
September 30**

2020	\$ 3,338,457
2021	3,345,880
2022	3,442,827
2023	3,524,076
2024	3,534,903
Thereafter	<u>16,537,283</u>
 Total	 <u>\$33,723,426</u>

SSP has entered into leases for rental of space within the ACC. The leases commenced in October 2009 and extend through September 2029. Payments are dependent on SSP's debt service and other costs related to the ACC and are reported as other revenue in the accompanying consolidated statements of operations and changes in net assets. The estimated rental income under the agreements is as follows:

**Years Ending
September 30**

2020	\$ 2,604,243
2021	2,627,564
2022	2,660,777
2023	2,727,035
2024	2,729,024
Thereafter	<u>14,217,108</u>
 Total	 <u>\$27,565,751</u>

12. ENDOWMENTS

Endowments consist of approximately 30 individual funds established for a variety of purposes. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions and the nature of the restrictions, if any.

Endowment Net Asset Composition by Type of Fund	Without Donor Restrictions	With Donor Restrictions	Total
September 30, 2019— Donor-restricted endowment funds	\$ 2,283,049	\$ 1,309,829	\$ 3,592,878
September 30, 2018— Donor-restricted endowment funds	2,283,049	1,283,520	3,566,569
Changes in Endowment Net Assets for the Fiscal Year Ended September 30, 2019	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets—beginning of year	\$ 2,283,049	\$ 1,283,520	\$ 3,566,569
Contributions	<u> </u>	<u>26,308</u>	<u>26,308</u>
Endowment net assets—end of year	<u>\$ 2,283,049</u>	<u>\$ 1,309,828</u>	<u>\$ 3,592,877</u>
Changes in Endowment Net Assets for the Fiscal Year Ended September 30, 2018	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets—beginning of year	\$ 2,283,049	\$ 981,910	\$ 3,264,959
Contributions	<u> </u>	<u>301,610</u>	<u>301,610</u>
Endowment net assets—end of year	<u>\$ 2,283,049</u>	<u>\$ 1,283,520</u>	<u>\$ 3,566,569</u>

Funds with Deficiencies—From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or current law requires the Corporation to retain as a fund of perpetual duration (underwater endowments). There were no such deficiencies as of September 30, 2019 or 2018.

Return Objectives and Risk Parameters—The Corporation has investment and spending practices for endowment assets that intend to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Corporation must hold in perpetuity or for a donor-specified period(s). The policy allows the endowment assets to be invested in a manner that is intended to produce results that exceed the price and yield results of the allocation index while assuming a moderate level of investment risk. The Corporation expects its endowment funds to provide a rate of return that preserves the gift and generates earnings to achieve the endowment purpose.

Strategies Employed for Achieving Objectives—To satisfy its long-term rate-of-return objectives, the Corporation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and interest and dividend income. The Corporation uses a diversified asset allocation to achieve its long-term return objectives within prudent risk constraints to preserve capital.

13. NET ASSETS

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

	2019	2018
Subject to expenditure for health care operations	\$ 19,793,308	\$ 9,069,924
Endowments subject to the Corporation's endowment spending policy and appropriation	<u>14,502,996</u>	<u>15,021,241</u>
Net assets with donor restrictions	<u>\$ 34,296,304</u>	<u>\$ 24,091,165</u>

Net assets without donor restrictions were as follows for the years ended September 30, 2019 and 2018:

	2019	2018
Undesignated	\$ 158,970,120	\$ 147,921,276
Board-designated for operations and other	<u>217,841,753</u>	<u>209,220,561</u>
Net assets without donor restrictions	<u>\$ 376,811,873</u>	<u>\$ 357,141,837</u>

14. EMPLOYEE BENEFIT PLANS

The Hospital has a defined benefit pension plan (the "Plan") covering substantially all employees. The Plan's benefit formula is based on a participant's service and highest five-year final-average level of compensation. The Hospital's funding policy is to make contributions to the Plan at least equal to the minimum required under the law.

On December 21, 2005, the Corporation's Board voted to freeze participation and future service credits under the Plan, effective January 1, 2007. Benefits under the Plan have been supplemented by a defined contribution plan consisting of the Corporation's funded core and matching contribution features through a 403(b) plan. Pension expense related to the defined contribution plan was approximately \$16,307,000 and \$16,015,000 for the years ended September 30, 2019 and 2018, respectively, and is included in salaries, wages, and employee benefits expense in the statements of operations and changes in net assets.

The Corporation uses a September 30 measurement date for measuring the assets and obligations of the Plan. During the years ended September 30, 2019 and 2018, the Plan's changes benefit obligation consisted of the following:

	2019	2018
Benefit obligation—beginning of year	\$ 162,721,643	\$ 182,072,988
Service cost and assumed expenses	550,000	600,000
Interest cost	6,806,201	6,765,345
Actuarial loss (gain)	22,432,156	(11,619,526)
Benefits paid	(7,865,917)	(7,486,314)
Actual administrative expenses paid	(463,190)	(552,644)
Plan amendments	<u> </u>	<u>(7,058,206)</u>
Benefit obligation—end of year	<u>\$ 184,180,893</u>	<u>\$ 162,721,643</u>

Plan Amendments—Effective March 31, 2018, all actively employed participants became fully vested in the Plan, and active participants will no longer receive additional cost-of-living adjustments on their accrued benefit.

The accumulated benefit obligation at September 30, 2019 and 2018, was \$184,180,893 and \$162,721,643, respectively. A 3.26% and 4.32% discount rate was used to determine the benefit obligations at September 30, 2019 and 2018, respectively. During the years ended September 30, 2019 and 2018, the changes in Plan assets consisted of the following:

	2019	2018
Fair value of Plan assets—beginning of year	\$ 171,107,694	\$ 172,023,786
Actual return on Plan assets	29,233,537	1,955,025
Employer contribution		5,000,000
Benefits and other expenses paid	<u>(8,329,107)</u>	<u>(7,871,117)</u>
Fair value of Plan assets—end of year	<u>\$ 192,012,124</u>	<u>\$ 171,107,694</u>

The asset allocation for the Plan at the end of 2019 and 2018, and the target allocation for 2019, by asset category, is as follows:

	Target 2019	Percentage of Plan Assets at Year-End	
		2019	2018
Domestic equities	15 %	15 %	16 %
Cash		1	0
International equities	5	4	5
Investment-grade bonds	<u>80</u>	<u>80</u>	<u>79</u>
Total	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

The investment policy and strategy, as established by the Board, is to provide for growth of capital with a moderate level of volatility by investing assets based on the target allocations stated above. The Corporation rebalances its investments quarterly to meet the above target allocations. The Corporation reviews its investment policy periodically to determine if the policy or allocations should be changed.

To determine the expected long-term rate of return, the Corporation considers the historical returns of the major market indicators related to the target asset allocation, as well as the current economic and financial market conditions. As of September 30, 2019 and 2018, the funded status of the Plan was as follows:

	2019	2018
Fair value of Plan assets—end of year	\$ 192,012,124	\$ 171,107,694
Benefit obligation—end of year	<u>184,180,893</u>	<u>162,721,643</u>
Net amount recognized—noncurrent pension asset	<u>\$ 7,831,231</u>	<u>\$ 8,386,051</u>

Net assets without donor restrictions at September 30, 2019 and 2018, include unrecognized actuarial losses of \$35,984,076 and \$36,484,000, respectively, related to the Plan. Approximately, \$526,000 is expected to be recognized in net periodic pension cost in 2020. As of September 30, 2019 and 2018, the components of net pension cost were as follows:

	2019	2018
Service cost and assumed administrative expenses	\$ 550,000	\$ 600,000
Interest cost	6,806,207	6,765,345
Expected return on Plan assets	(7,188,523)	(7,696,170)
Recognized net actuarial loss	<u>886,816</u>	<u>1,388,446</u>
Net pension cost	<u>\$ 1,054,500</u>	<u>\$ 1,057,621</u>

Weighted-average assumptions used to determine pension cost for the years ended September 30, 2019 and 2018, are as follows:

	2019	2018
Discount rate	2.26 %	4.32 %
Expected return on Plan assets	4.00	4.50

Expected Cash Flows—Expected benefit payments as of September 30, 2019, are as follows:

**Years Ending
September 30**

2020	\$11,638,477
2021	12,029,263
2022	11,497,965
2023	11,361,391
2024	10,949,422
2025–2029	52,505,444

No contribution is expected to be made to the Plan during the year ending September 30, 2020.

Changes in the benefit obligation due to Plan amendments are amortized on a straight-line basis over the average future service period of active participants expected to receive benefits.

15. MALPRACTICE AND WORKERS' COMPENSATION INSURANCE AND CONTINGENT LIABILITIES

Malpractice Insurance—Malpractice insurance coverage, including coverage for catastrophic claims, for the Corporation has been obtained on a claims-made basis and is subject to annual renewal. The Corporation intends to renew its coverage on a claims-made basis and has no reason to believe that it may be prevented from renewing such coverage.

The Corporation maintains a program of self-insurance to provide for the cost of malpractice liabilities not covered under its claims-made policy. Malpractice expense is based upon estimates made by the Corporation's independent consulting actuary. At September 30, 2019 and 2018, the estimated malpractice liabilities, including unreported claims were approximately \$7,928,000 and \$7,917,000, respectively. Accrued malpractice claim costs as of September 30, 2019 and 2018, are reported without consideration of insurance recoveries.

Assets of the malpractice fund, which amounted to approximately \$4,917,000 and \$4,612,000 at September 30, 2019 and 2018, respectively, are reported as assets whose use is limited within internally designated investments.

Workers' Compensation Insurance—The Corporation is self-insured for workers' compensation claims. At September 30, 2019 and 2018, the net estimated amount of accrued claims, including a provision for unreported claims, was approximately \$6,295,000 and \$6,816,000, respectively. Such amounts are included in other long-term liabilities or accounts payable and accrued liabilities in the accompanying consolidated balance sheets.

Other Contingencies—The Corporation has been named as a defendant in a number of legal proceedings, which have arisen in the normal course of business. In addition, the health care industry as a whole is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations can be subject to future governmental review and interpretation, as well as regulatory actions unknown or

unasserted at this time. Such compliance in the health care industry has recently come under increased governmental scrutiny, which could result in the imposition of significant fines and penalties, as well as significant repayments previously billed and collected revenue for patient services. Management does not believe that these matters will have a material adverse effect on the Corporation's consolidated financial statements.

16. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair Value Measurements—GAAP provides a framework for measuring fair value. Fair value is the price that would be received upon the sale of an asset or paid upon the transfer of a liability in an orderly transaction between market participants at the measurement date. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value, as follows: Level 1, which refers to securities valued using unadjusted quoted prices from active markets for identical assets; Level 2, which refers to securities not traded on an active market but for which observable market inputs are readily available; and Level 3, which refers to securities valued based on significant unobservable inputs. Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

As of September 30, 2019 and 2018, information about the Corporation's financial assets and liabilities that are measured at fair value on a recurring basis are as follows:

2019	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Fair Value
Assets:				
Cash and money market investments	\$ 51,018,001	\$ -	\$ -	\$ 51,018,001
Mutual funds	<u>81,287,914</u>	<u> </u>	<u> </u>	<u>81,287,914</u>
Total assets at fair value	<u>132,305,915</u>	<u>-</u>	<u>-</u>	<u>132,305,915</u>
Investments measured at net asset value (NAV)—Common collective trusts	<u> </u>	<u> </u>	<u> </u>	<u>204,845,386</u>
Total investments measured at NAV	<u>-</u>	<u>-</u>	<u> </u>	<u>204,845,386</u>
Total assets	<u>132,305,915</u>	<u> </u>	<u> </u>	<u>337,151,301</u>
Liabilities—interest rate swap	<u>\$ -</u>	<u>\$(8,582,517)</u>	<u>\$ -</u>	<u>\$ (8,582,517)</u>

2018	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Fair Value
Assets:				
Cash and money market investments	\$ 19,410,124	\$ -	\$ -	\$ 19,410,124
Mutual funds	80,726,982			80,726,982
Other				
Total assets at fair value	<u>100,137,106</u>	<u>-</u>	<u>-</u>	<u>100,137,106</u>
Investments measured at NAV:				
Common collective trusts				201,900,278
Money market funds				<u>4,894,737</u>
Total investments measured at NAV	<u>-</u>	<u>-</u>	<u>-</u>	<u>206,795,015</u>
Total assets	<u>\$100,137,106</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$306,932,121</u>
Liabilities—interest rate swap	<u>\$ -</u>	<u>\$(5,356,027)</u>	<u>\$ -</u>	<u>\$ (5,356,027)</u>

As of September 30, 2019 and 2018, information about the Corporation's pension plan assets that are measured at fair value on a recurring basis is as follows:

2019	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Fair Value
Assets:				
Cash and money market investments	\$ 1,360,532	\$ -	\$ -	\$ 1,360,532
Mutual funds	<u>158,130,280</u>			<u>158,130,280</u>
Total assets at fair value	<u>\$159,490,812</u>	<u>\$ -</u>	<u>\$ -</u>	159,490,812
Investments measured at NAV—Common collective trusts				
				<u>32,521,312</u>
Total assets				<u>\$192,012,124</u>

2018	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Fair Value
Assets:				
Cash and money market investments	\$ 793,025	\$ -	\$ -	\$ 793,025
Mutual funds	<u>142,966,511</u>	<u> </u>	<u> </u>	<u>142,966,511</u>
Total assets at fair value	<u>\$143,759,536</u>	<u>\$ -</u>	<u>\$ -</u>	143,759,536
Investments measured at NAV—Common collective trusts				<u>27,348,159</u>
Total assets				<u>\$171,107,695</u>

Transfers between Levels—The availability of observable market data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period. For the years ended September 30, 2019 and 2018, there were no transfers between levels.

Asset Valuation Techniques—Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The following is a description of the valuation techniques used for assets measured at fair value. There have been no changes in the techniques used at September 30, 2019 and 2018.

Cash and Money Market Investments—The carrying value of cash investments approximates fair value as maturities are less than three months and/or include money market funds that are based on quoted prices and actively traded. The fair values of certain money market funds are based on NAV as a practical expedient. There are no unfunded commitments on these investments. These investments are included in unexpended bond proceeds and debt service funds in the accompanying consolidated balance sheets.

Mutual Fund Investments—Mutual fund investments are valued at the daily closing price as reported by the fund. Mutual funds held by the Plan are open-ended mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily NAV and to transact at that price. The mutual funds held are deemed to be actively traded.

Common Collective Trusts—The estimated fair values of common collective trusts are determined based upon information provided by the trustee. The NAV, as provided by the trustee, is used as a practical expedient to estimate fair value. The NAV is based on the fair value of the underlying investments held by the fund, less its liabilities. This practical expedient is not used when it is determined to be probable that the fund will sell the investments for amounts different than the reported NAV. The Corporation's interest may be redeemed at NAV on a daily basis with no redemption restrictions. At September 30, 2019 and 2018, there were no unfunded commitments to the common collective trusts.

Pledges Receivable—The current yields for one- to 10-year US Treasury notes are used to discount pledges receivable. The Corporation considers these yields to be a Level 2 input in the context of the fair value hierarchy. Pledges received during 2019 were discounted at rates ranging from 1.51% to 3.05% (1.92% to 3.05% in 2018). Pledges received in 2019 and 2018, which have been recorded at fair value, totaled approximately \$11,597,421 and \$2,082,846, respectively.

Interest Rate Swap—The Corporation uses inputs other than quoted prices that are observable to value the interest rate swap. The Corporation considers these inputs to be Level 2 inputs in the context of the fair value hierarchy. The fair value of the interest rate swap liability was approximately \$8,582,000 and \$5,356,000 at September 30, 2019 and 2018, respectively. This value represents the estimated amount the Corporation would receive or pay to terminate agreements, taking into consideration current interest rates and the current creditworthiness of the counterparty.

The following methods and assumptions were used by the Corporation in estimating the fair value of the Corporation's financial instruments that are not measured at fair value on a recurring basis for disclosures in the consolidated financial statements:

Accounts Receivable, Other Current and Noncurrent Assets, Accounts Payable and Accrued Liabilities, and the Accrual for Estimated Settlements with Third-Party Payors—The carrying amounts of these items are reasonable estimates of their fair value.

Long-Term Debt—The fair value of the Corporation's long-term debt is estimated based on quoted market prices for the same or similar issues. The fair value inputs for long-term debt are considered Level 2. The fair value of long-term debt was approximately \$295,492,000 and \$238,235,000 at September 30, 2019 and 2018, respectively.

17. CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Corporation to concentrations of credit risk are patient accounts receivable, cash and cash equivalents, pledges receivable, and investments. The Corporation invests available cash in money market securities of various banks, commercial paper of domestic companies with high-credit ratings, common collective trusts, mutual funds, and securities backed by the US government.

The Corporation is located in southeastern Massachusetts and grants credit without collateral to its patients, many of whom are local residents and are insured under third-party payor agreements.

The Corporation's net accounts receivable and net revenue from patients and third-party payors as of and for the years ended September 30, 2019 and 2018, were as follows:

	Accounts Receivable		Net Revenue	
	2019	2018	2019	2018
Medicare	29 %	29 %	38 %	37 %
Medicaid	10	10	8	9
BlueCross and HMOs	35	36	43	45
Self-pay patients	16	15	1	1
Commercial	4	4	6	5
Other third-party payors	<u>6</u>	<u>6</u>	<u>4</u>	<u>3</u>
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

A significant portion of the accounts receivable from HMOs is derived from BlueCross and two other Massachusetts-managed care companies. Although management expects the amounts recorded as net accounts receivable to be collectible at September 30, 2019, this concentration of credit risk is expected to continue in the near term.

18. FUNCTIONAL EXPENSES

The Corporation provides general health care services to residents within its geographic locations. Expenses by functional classification for the year ended September 30, 2019, are as follows:

	Health Care Services	General and Administrative	Fund- raising	Total
Salaries, wages, and employee benefits	\$ 386,366,039	\$ 124,632,235	\$ 2,117,484	\$ 513,115,758
Supplies and other	130,109,696	32,582,836	639,109	163,331,641
Professional fees and other	8,342,671	24,030,114	101,742	32,474,527
Depreciation and amortization	22,586,758	11,123,864		33,710,622
Interest	<u>7,639,327</u>	<u>4,166,347</u>		<u>11,805,674</u>
	<u>\$ 555,044,491</u>	<u>\$ 196,535,396</u>	<u>\$ 2,858,335</u>	<u>\$ 754,438,222</u>

For the year ended September 30, 2018, substantially all expenses reported in the consolidated statement of operations and changes in net assets are related to the delivery of health care services.

The financial statements report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include human resources, finance and treasury, legal, technology services, and other functions. These expenses are allocated to health care services and general and administrative services based on the functional department for which they are incurred. Departmental expenses may include allocations of costs based on direct assignment, expenses or other methods.

19. SUBSEQUENT EVENTS

Subsequent events have been evaluated through December 20, 2019, the date of issuance of these consolidated financial statements.

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SUPPLEMENTAL CONSOLIDATING SCHEDULES

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

SUPPLEMENTAL CONSOLIDATING SCHEDULE—BALANCE SHEET INFORMATION AS OF SEPTEMBER 30, 2019

	South Shore Health System, Inc.	South Shore Hospital, Inc.	South Shore Property, Inc.	Coastal Medical Associates, Inc.	Connected Care of Southeastern Massachusetts, Inc.	South Shore Health Express, Inc.	Eliminations	Total
ASSETS								
CURRENT ASSETS:								
Cash and cash equivalents	\$ 398,344	\$ 40,095,584	\$ 1,194,929	\$ 4,035,951	\$ -	\$ 1,428,396	\$ -	\$ 47,153,204
Short-term investments	51,825,346							51,825,346
Current portion of assets whose use is limited		2,013,910	273,577		4,106,570			6,394,057
Patient accounts receivable		65,618,150		4,631,879		747,413		70,997,442
Inventories		7,621,605		596,126		279,733		8,497,464
Prepaid and other current assets	59,271	17,462,220	289,639	6,987,770		441,144		25,240,044
Due from affiliates		2,585,880	22,712	539,171			(3,147,763)	
Total current assets	<u>52,282,961</u>	<u>135,397,349</u>	<u>1,780,857</u>	<u>16,790,897</u>	<u>4,106,570</u>	<u>2,896,686</u>	<u>(3,147,763)</u>	<u>210,107,557</u>
ASSETS WHOSE USE IS LIMITED OR RESTRICTED:								
Internally designated investments		217,841,753						217,841,753
Donor-restricted investments	2,804,662	25,031,394						27,836,056
Other investments	596,693	5,333,084	22,261,146	5,063,166				33,254,089
Unexpended bond proceeds								
Total assets whose use is limited or restricted—net of current portion	<u>3,401,355</u>	<u>248,206,231</u>	<u>22,261,146</u>	<u>5,063,166</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>278,931,898</u>
PROPERTY AND EQUIPMENT—Net	244,673	266,444,317	40,589,997	6,651,384	9,282	2,196,947		316,136,600
PENSION ASSET		7,831,231						7,831,231
GOODWILL—Net						24,120,112		24,120,112
INTANGIBLE ASSETS						3,744,000		3,744,000
OTHER ASSETS	66,000	26,587,542		92,840		17,562		26,763,944
TOTAL	<u>\$55,994,989</u>	<u>\$684,466,670</u>	<u>\$64,632,000</u>	<u>\$28,598,287</u>	<u>\$4,115,852</u>	<u>\$32,975,307</u>	<u>\$(3,147,763)</u>	<u>\$867,635,342</u>

(Continued)

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

SUPPLEMENTAL CONSOLIDATING SCHEDULE—BALANCE SHEET INFORMATION AS OF SEPTEMBER 30, 2019

	South Shore Health System, Inc.	South Shore Hospital, Inc.	South Shore Property, Inc.	Coastal Medical Associates, Inc.	Connected Care of Southeastern Massachusetts, Inc.	South Shore Health Express, Inc.	Eliminations	Total
LIABILITIES AND NET ASSETS								
CURRENT LIABILITIES:								
Current portion of long-term debt	\$ -	\$ 8,395,833	\$ 2,125,000	\$ -	\$ -	\$ 1,414,286	\$ -	\$ 11,935,119
Current portion of capital lease obligations		1,191,079						1,191,079
Accounts payable and accrued liabilities	21,002	83,128,541	16,355,171	10,222,987	1,804,714	1,049,756		112,582,171
Current portion of estimated settlements with third-party payors		4,081,800		848,310	4,188,225			9,118,335
Due to affiliates	<u>609,981</u>		<u>33,032</u>	<u>2,390,473</u>	<u>84,041</u>	<u>30,236</u>	<u>(3,147,763)</u>	
Total current liabilities	<u>630,983</u>	<u>96,797,253</u>	<u>18,513,203</u>	<u>13,461,770</u>	<u>6,076,980</u>	<u>2,494,278</u>	<u>(3,147,763)</u>	<u>134,826,704</u>
LONG-TERM DEBT—Net of current portion		189,079,666	36,576,960			31,249,053		256,905,679
CAPITAL LEASE OBLIGATIONS—Net of current portion		10,135,014						10,135,014
ESTIMATED SETTLEMENTS WITH THIRD-PARTY PAYOR—Net of current portion		16,766,408						16,766,408
MALPRACTICE LIABILITY		7,888,404						7,888,404
OTHER LONG-TERM LIABILITIES	<u>78,365</u>	<u>22,459,194</u>		<u>7,467,397</u>				<u>30,004,956</u>
Total liabilities	<u>709,348</u>	<u>343,125,939</u>	<u>55,090,163</u>	<u>20,929,167</u>	<u>6,076,980</u>	<u>33,743,331</u>	<u>(3,147,763)</u>	<u>456,527,165</u>
NET ASSETS:								
Without donor restrictions	52,172,417	310,157,651	9,541,837	7,669,120	(1,961,128)	(768,024)		376,811,873
With donor restrictions	<u>3,113,224</u>	<u>31,183,080</u>						<u>34,296,304</u>
Total net assets (deficit)	<u>55,285,641</u>	<u>341,340,731</u>	<u>9,541,837</u>	<u>7,669,120</u>	<u>(1,961,128)</u>	<u>(768,024)</u>	<u>-</u>	<u>411,108,177</u>
TOTAL	<u>\$ 55,994,989</u>	<u>\$ 684,466,670</u>	<u>\$ 64,632,000</u>	<u>\$ 28,598,287</u>	<u>\$ 4,115,852</u>	<u>\$ 32,975,307</u>	<u>\$(3,147,763)</u>	<u>\$ 867,635,342</u>

(Concluded)

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

SUPPLEMENTAL CONSOLIDATING SCHEDULE—STATEMENT OF OPERATIONS INFORMATION FOR THE YEAR ENDED SEPTEMBER 30, 2019

	South Shore Health System, Inc.	South Shore Hospital, Inc.	South Shore Property, Inc.	Coastal Medical Associates, Inc.	Connected Care of Southeastern Massachusetts, Inc.	South Shore Health Express, Inc.	Eliminations	Total
NET PATIENT SERVICE REVENUE	\$ -	\$613,290,140	\$ -	\$78,342,851	\$ (563,245)	\$ 9,767,627	\$ -	\$700,837,373
OTHER REVENUE	329,778	37,486,224	5,748,148	6,478,478		324,269	(7,328,061)	43,038,836
NET ASSETS RELEASED FROM RESTRICTIONS USED FOR OPERATIONS	<u> </u>	<u>2,263,641</u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u>2,263,641</u>
Total unrestricted revenue, gains, and other support	<u>329,778</u>	<u>653,040,005</u>	<u>5,748,148</u>	<u>84,821,329</u>	<u>(563,245)</u>	<u>10,091,896</u>	<u>(7,328,061)</u>	<u>746,139,850</u>
EXPENSES:								
Salaries, wages, and employee benefits		385,241,948		41,148,403	484,213	4,626,896		431,501,460
Physician services		53,003,883		29,061,480	773,549	718,309	(5,114,907)	78,442,314
Supplies and other	1,307,517	171,015,129	1,735,632	17,505,747	3,957,202	1,757,244	(2,213,154)	195,065,317
Depreciation and amortization		28,778,384	1,489,934	998,321	2,655	2,441,328		33,710,622
Interest		<u>9,270,638</u>	<u>1,218,892</u>	<u> </u>	<u> </u>	<u>1,316,144</u>	<u> </u>	<u>11,805,674</u>
Total expenses	<u>1,307,517</u>	<u>647,309,982</u>	<u>4,444,458</u>	<u>88,713,951</u>	<u>5,217,619</u>	<u>10,859,921</u>	<u>(7,328,061)</u>	<u>750,525,387</u>
OPERATING (LOSS) INCOME	<u>(977,739)</u>	<u>5,730,023</u>	<u>1,303,690</u>	<u>(3,892,622)</u>	<u>(5,780,864)</u>	<u>(768,025)</u>	<u> </u>	<u>(4,385,537)</u>
NONOPERATING GAINS AND LOSSES:								
Investment income	618,423	1,842,974						2,461,397
Gain on sales of investments—net	2,349,502	2,511,237						4,860,739
Impairment of investments								
Loss on interest rate swap agreements		(3,300,815)						(3,300,815)
Unrestricted gifts and bequests	(20,306)	692,547						672,241
Fund-raising costs		(2,858,335)						(2,858,335)
Pension expense		<u>(1,054,500)</u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u>(1,054,500)</u>
Nonoperating gains (loss)—net	<u>2,947,619</u>	<u>(2,166,892)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>780,727</u>

(Continued)

SOUTH SHORE HEALTH SYSTEM, INC. AND SUBSIDIARIES

SUPPLEMENTAL CONSOLIDATING SCHEDULE—STATEMENT OF OPERATIONS INFORMATION FOR THE YEAR ENDED SEPTEMBER 30, 2019

	South Shore Health System, Inc.	South Shore Hospital, Inc.	South Shore Property, Inc.	Coastal Medical Associates, Inc.	Connected Care of Southeastern Massachusetts, Inc.	South Shore Health Express, Inc.	Eliminations	Total
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	\$ 1,969,880	\$ 3,563,131	\$1,303,690	\$(3,892,622)	\$(5,780,864)	\$ (768,025)	\$ -	\$ (3,604,810)
CHANGE IN NET UNREALIZED GAINS AND LOSSES ON INVESTMENTS	286,770	4,472,154						4,758,924
PENSION-RELATED ADJUSTMENTS		499,680						499,680
GAIN ON INTEREST RATE SWAP AGREEMENT		67,340						67,340
TRANSFERS TO (FROM) AFFILIATES	(18,307,631)		6,407,631	7,500,000	4,400,000			
NET ASSETS RELEASED FROM RESTRICTIONS USED FOR PURCHASE OF PROPERTY AND EQUIPMENT		1,052,376						1,052,376
(DECREASE) INCREASE IN NET ASSETS WITHOUT DONOR RESTRICTIONS	<u>\$(16,050,981)</u>	<u>\$ 9,654,681</u>	<u>\$7,711,321</u>	<u>\$ 3,607,378</u>	<u>\$(1,380,864)</u>	<u>\$ (768,025)</u>	<u>\$ -</u>	<u>\$ 2,773,510</u>

(Concluded)