

**FAXTON-ST. LUKE'S HEALTHCARE
AND AFFILIATE**

Consolidated Financial Statements

December 31, 2016 and 2015

INDEPENDENT AUDITOR'S REPORT

The Board of Directors
Mohawk Valley Health System:

We have audited the accompanying consolidated financial statements of Faxton-St. Luke's Healthcare and Affiliate, which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of operations and changes in net assets and consolidated cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

(Continued)

The Board of Directors
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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Faxton-St. Luke's Healthcare and Affiliate as of December 31, 2016 and 2015, and the results of its operations, changes in net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

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

Fust Charles Chambers LLP

May 31, 2017

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidated Balance Sheets

December 31, 2016 and 2015

<u>Assets</u>	<u>2016</u>	<u>2015</u>
Current assets:		
Cash and cash equivalents	\$ 5,802,574	1,458,858
Investments and assets limited as to use	83,284,031	78,379,823
Patient accounts receivable, net of reserve for doubtful accounts of approximately \$7,711,000 in 2016 and \$7,727,000 in 2015	31,516,572	38,999,629
Pledges receivable	335,273	571,367
Other current assets	6,853,883	5,424,254
Inventories	6,280,789	5,873,362
Prepaid expenses	3,335,552	3,003,276
Due from affiliates, net	1,367,027	4,044,954
Estimated third-party payor settlements, net	1,948,925	1,649,371
Total current assets	140,724,626	139,404,894
Investment in affiliates	86,480	830,969
Due from affiliates, net	2,004,544	1,955,488
Investments	4,528,164	4,528,164
Beneficial interest in charitable trusts	1,483,000	1,265,000
Property and equipment, net	78,352,206	77,976,553
Other assets	24,453,511	18,589,053
Total assets	\$ <u>251,632,531</u>	<u>244,550,121</u>

<u>Liabilities and Net Assets</u>	<u>2016</u>	<u>2015</u>
Current liabilities:		
Revolving note payable	\$ -	5,623,000
Current portion of long-term debt	3,186,209	3,752,367
Current portion of capital lease obligations	4,076,665	3,825,676
Accounts payable and accrued expenses	15,150,872	15,134,168
Accrued payroll, payroll taxes and benefits	12,095,220	10,392,132
Current portion of estimated insurance liabilities	4,623,654	5,798,357
Other current liabilities	4,650,197	3,032,187
	<u>43,782,817</u>	<u>47,557,887</u>
Total current liabilities		
Long-term debt, net of current portion:		
Notes payable	5,218,968	4,463,569
Civic facility revenue bonds	14,149,514	14,723,963
Capital lease obligations	5,483,062	6,284,814
	<u>24,851,544</u>	<u>25,472,346</u>
Total long-term debt, net of current portion		
Other liabilities	36,713,497	30,846,580
Estimated insurance liabilities, net of current portion	5,057,692	3,994,434
	<u>110,405,550</u>	<u>107,871,247</u>
Total liabilities		
Net assets:		
Unrestricted	132,869,688	127,892,575
Temporarily restricted	3,829,129	4,258,135
Permanently restricted	4,528,164	4,528,164
	<u>141,226,981</u>	<u>136,678,874</u>
Total net assets		
Commitments and contingencies (notes 6 and 9)		
Total liabilities and net assets	<u>\$ 251,632,531</u>	<u>244,550,121</u>

See accompanying notes to consolidated financial statements.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE
Consolidated Statements of Operations and Changes in Net Assets
Years ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Unrestricted revenues, gains and other support:		
Patient service revenue (net of contractual allowances and discounts)	\$ 273,563,013	267,603,957
Provision for bad debts	<u>(5,277,188)</u>	<u>(5,387,923)</u>
Net patient service revenue less provision for bad debts	268,285,825	262,216,034
Other operating revenue	16,830,683	13,985,931
Net assets released from restrictions used for operations	<u>741,271</u>	<u>900,853</u>
Total unrestricted revenues, gains and other support	<u>285,857,779</u>	<u>277,102,818</u>
Expenses:		
Salaries and wages	138,026,697	129,371,185
Employee benefits	24,984,148	26,411,289
Supplies and other	105,957,486	101,516,920
Depreciation and amortization	14,272,748	16,078,436
Interest	1,743,087	1,998,101
New York State gross receipts taxes	<u>1,102,309</u>	<u>1,069,659</u>
Total expenses	<u>286,086,475</u>	<u>276,445,590</u>
Net income (loss) from operations	(228,696)	657,228
Other revenue (expense):		
Contributions and other unrestricted revenue (expense)	(78,867)	(1,465,539)
Investment income, net of fees	<u>1,158,178</u>	<u>2,997,110</u>
Total other revenue, net	<u>1,079,311</u>	<u>1,531,571</u>
Excess of revenues over expenses	<u>\$ 850,615</u>	<u>2,188,799</u>

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidated Statements of Operations and Changes in Net Assets, Continued

Years ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Unrestricted net assets:		
Excess of revenues over expenses	\$ 850,615	2,188,799
Change in fair value of interest rate swaps	633,888	241,570
Net assets released for capital acquisitions	1,342,078	780,004
Contributions used for capital acquisitions	41,750	85,094
Transfer to affiliate	-	(450,000)
Reserve for doubtful accounts due from affiliate	(1,665,000)	-
Change in net unrealized gains and losses on investments	<u>3,773,782</u>	<u>(6,822,127)</u>
Increase (decrease) in unrestricted net assets	<u>4,977,113</u>	<u>(3,976,660)</u>
Temporarily restricted net assets:		
Contributions	1,436,343	1,998,338
Change in value of charitable trusts	218,000	(13,000)
Net assets released from restrictions	<u>(2,083,349)</u>	<u>(1,680,857)</u>
Increase (decrease) in temporarily restricted net assets	<u>(429,006)</u>	<u>304,481</u>
Total increase (decrease) in net assets	4,548,107	(3,672,179)
Net assets at beginning of year	<u>136,678,874</u>	<u>140,351,053</u>
Net assets at end of year	<u>\$ 141,226,981</u>	<u>136,678,874</u>

See accompanying notes to consolidated financial statements.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidated Statements of Cash Flows

Years ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities:		
Change in net assets	\$ 4,548,107	(3,672,179)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	14,272,748	16,078,436
Amortization of debt issuance costs	25,551	25,551
Provision for bad debts	5,277,188	5,387,923
Change in net unrealized gains and losses on investments	(3,773,782)	6,822,127
Change in fair value of interest rate swaps	(633,888)	(241,570)
Amortization of unearned lease income	(177,826)	(204,213)
Net realized gain on sale of investments	(396,312)	(1,585,939)
Change in value of charitable trusts	(218,000)	13,000
Loss on disposition of property and equipment	201,655	47,309
Gain in earnings of investees	(194,562)	(54,459)
Contributions for capital acquisitions	(41,750)	(85,093)
Changes in operating assets and liabilities:		
Patient accounts receivable	2,205,869	(5,715,036)
Inventories, prepaid expenses and other current assets	(210,108)	1,909,981
Due from affiliates, net	(1,096,662)	116,913
Accounts payable, accrued expenses and other liabilities	1,124,505	150,864
Estimated insurance liabilities	(111,445)	3,303,802
Estimated third-party payor settlements	(299,554)	4,470,266
Net cash provided by operating activities	<u>20,501,734</u>	<u>26,767,683</u>
Cash flows from investing activities:		
Purchases of property and equipment	(7,183,101)	(5,852,421)
Proceeds from sale of property and equipment	11,438	49,401
Purchases of investments, net	(734,114)	(1,492,637)
Change in other assets	177,441	2,085,986
Net cash used in investing activities	<u>(7,728,336)</u>	<u>(5,209,671)</u>
Cash flows from financing activities:		
Payments on revolving note payable, net	(5,623,000)	(10,377,000)
Changes in advances to affiliates, net	3,750,000	(4,250,000)
Proceeds from long-term debt	-	1,397,636
Principal payments on long-term debt and capital lease obligations	(7,145,548)	(9,183,937)
Minimum direct financing lease payments received	547,116	547,116
Contributions for capital acquisitions	41,750	85,093
Net cash used in financing activities	<u>(8,429,682)</u>	<u>(21,781,092)</u>
Increase (decrease) in cash and cash equivalents	4,343,716	(223,080)
Cash and cash equivalents at beginning of year	<u>1,458,858</u>	<u>1,681,938</u>
Cash and cash equivalents at end of year	<u>\$ 5,802,574</u>	<u>1,458,858</u>

See accompanying notes to consolidated financial statements.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

December 31, 2016 and 2015

(1) Description of Organization and Summary of Significant Accounting Policies

(a) Organization

Faxton-St. Luke's Healthcare (Healthcare), located in Utica, New York, is a not-for-profit healthcare delivery system providing inpatient, outpatient, emergency care, cancer treatment, rehabilitation, dialysis, maternity, child care, long term care, surgical, psychiatric and community services to residents of the Mohawk Valley Region. Admitting physicians are primarily practitioners in the local area.

Faxton-St. Luke's Healthcare Foundation (Foundation) is a not-for-profit, tax-exempt corporation that carries out fund raising activities which benefit Healthcare and certain affiliates. Healthcare is the sole member of the Foundation.

Mohawk Valley Health System (MVHS), a not-for-profit corporation, is the sole corporate member of Healthcare and various other organizations involved in providing health care services to the Mohawk Valley Region.

(b) Basis of Accounting

The accompanying consolidated financial statements include the consolidated accounts of Healthcare and Foundation (the Corporation). Included on the equity method of accounting are SLM Medical Office Building, Inc. (SLM), whose stock is owned by a trust, of which Healthcare is the sole beneficiary, and Paraffin, LLC (Paraffin), of which Healthcare is the sole member. All significant intercompany balances and transactions have been eliminated in the consolidated financial statements.

SLM, is a for-profit corporation that promotes, encourages and aids in the acquisition and construction of a medical office building to promote the operations of Healthcare. During 2016, Healthcare assumed the assets and liabilities of SLM, which primarily consisted of debt and fixed assets. Paraffin is a not-for-profit limited liability company that provides laboratory services to a local hospital.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(b) Basis of Accounting, Continued

As a member of MVHS, Healthcare is affiliated with and transacts business with other healthcare providers in the MVHS network. St. Elizabeth Medical Center (SEMC), a subsidiary of MVHS, provides acute care. Senior Network Health, LLC (SNH), a wholly owned subsidiary of MVHS, provides Medicaid managed care to seniors. Mohawk Valley Home Care, LLC (MVHC), a wholly owned subsidiary of MVHS, provides nursing services. Visiting Nurse Association of Utica and Oneida County, Inc. (VNA), a wholly owned subsidiary of MVHS, provides home health care services.

(c) New Accounting Pronouncement

In April 2015, the FASB issued ASU 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs," which simplifies the presentation of debt issuance costs to be presented as a deduction from the corresponding debt liability. Amortization of debt issuance costs shall be reported as interest expense. ASU 2015-03 is effective for consolidated financial statements issued for fiscal years beginning after December 15, 2015 and is to be applied on a retrospective basis for all previous periods presented. Healthcare adopted ASU 2015-03 as of and for the year ended December 31, 2016. The retrospective adoption of ASU 2015-03 resulted in a decrease to long-term assets, and long-term liabilities of approximately \$396,000 on the balance sheet for the year ended December 31, 2015, a reclassification of approximately \$26,000 of amortization of debt issuance costs from depreciation and amortization to interest expense on the consolidated statement of operations and changes in net assets and consolidated cash flows (cash flows from operations) for the year ended December 31, 2015, but had no effect on excess of revenues over expenses or net assets as of or for the year ended December 31, 2015.

(d) Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(e) Collective Bargaining Agreements

At December 31, 2016, Healthcare has approximately 63% of its employees working under collective bargaining agreements. The agreements will expire in June 2017.

(f) Cash and Cash Equivalents

Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturity of three months or less, excluding temporary investments included in investments.

(g) Investments and Assets Limited as to Use

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value which is determined utilizing quoted market prices. Investments in insurance group fixed annuity contracts (Guaranteed Investment Contracts) are valued at contract value, which is considered the best representation of fair value. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in the excess of revenues over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses since none of the investments are classified as trading securities.

Certain investments that do not have readily determinable fair values are valued by using the net asset value (NAV) per share (or its equivalent), as a practical expedient permitted under the Fair Value Measurement Topic of the FASB Accounting Standards Codification.

The Corporation invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the Corporation's net assets.

Assets limited as to use are comprised of cash held by a financial institution as required for the Corporation's malpractice insurance.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies. Continued

(h) Inventories

Inventories are stated at the lower of average cost or net realizable value.

(i) Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is calculated over the estimated useful life of each class of depreciable asset ranging from 3 - 40 years using the straight-line method. Property and equipment under capital leases and leasehold improvements are amortized on the straight-line method over the lesser of the lease term or the estimated useful life of the asset. Amortization of equipment under capital leases and leasehold improvements is included in depreciation and amortization expense.

Gifts of long-lived assets, such as land, buildings or equipment are reported as unrestricted support and are excluded from the excess of revenues over expenses, unless explicit donor stipulations specify how the donated asset 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. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(j) Unamortized Debt Issuance Costs

Debt issuance costs are amortized using the straight-line method, which approximates the effective interest method, over the terms of the related debt. Accumulated amortization of approximately \$269,000 and \$243,000 was recorded at December 31, 2016 and 2015, respectively. Amortization expense amounted to approximately \$26,000 in 2016 and 2015, and is included in interest expense within the consolidated statements of operations and change in net assets.

(k) Insurance Claims and Related Recoveries

The Corporation recognizes liabilities associated with malpractice claims or similar contingent liabilities when the incidents that give rise to the claims occur. Further, the liability shall not be presented net of anticipated insurance recoveries. Any amounts expected to be reimbursed from an insurance company are presented in other assets.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(l) Pledges Receivable

Pledges receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debts and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to pledges receivable. At December 31, 2016 and 2015, no allowance was recorded. The original pledge amount at December 31, 2016 was discounted approximately \$8,000 using a discount rate of 1.91% to reflect the net present value. The original pledge amount at December 31, 2015 approximated the net present value. The pledges receivable, net of discount, due to be collected during 2017 is approximately \$171,000 and during 2018-2020 is approximately \$164,000.

(m) Beneficial Interest in Charitable Trusts

The Foundation has beneficial interests in various irrevocable split-interest agreements that are administered by independent trustees which consist of charitable remainder unitrusts. The Foundation's interest in these trusts is recorded at the present value of the estimated future cash flows from the trust's assets using a discount rate that reflects current market conditions and is included in temporarily restricted net assets for renovations and equipment. At December 31, 2016, the value of the beneficial interest in these agreements approximated net present value as a result of the death of one of the unitrust holders. The Foundation used a discount rate of 2.0% at 2015. Changes in the fair value of the beneficial interest are reflected as change in value of charitable trusts in the consolidated statement of changes in net assets.

(n) Temporarily Restricted Net Assets

Temporarily restricted net assets are those whose use has been limited by donors to a specific time period or purpose.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(o) Permanently Restricted Net Assets (Endowment Funds)

The Corporation maintains various donor-restricted and board-designated funds whose purpose is to provide long-term support for its charitable programs. In classifying such funds for consolidated financial statement purposes as either permanently restricted, temporarily restricted or unrestricted net assets, the Board of Directors looks to the explicit directions of the donor where applicable and the provisions of the laws of the State of New York. To constitute an endowment under New York State law, the restriction must arise from a clearly expressed donor limitation, not a limitation from within the beneficiary organization. The Board of Directors has determined that, absent donor stipulations to the contrary, the provisions of New York State law do not impose either a permanent or temporary restriction on the income or capital appreciation derived from the original gift. Therefore, all income and appreciation derived from the original gift are transferred to unrestricted net assets absent any restrictions on the use made by the donor. Permanently restricted net assets consist of endowment funds of \$4,528,164 at December 31, 2016 and 2015, and are included in long-term investments in the consolidated balance sheets.

The Corporation utilizes an investment strategy that emphasizes preservation of principal and total return consistent with prudent levels of risk. Investments are allocated over a diversified portfolio of multiple asset classes of domestic and international equities and pooled investment funds.

Interpretation of Relevant Law

Prior to September 17, 2010, New York State law required the preservation of an endowment fund's historic dollar value. Historic dollar value is defined as the aggregate fair value in dollars of an endowment fund at the time it becomes an endowment fund, each subsequent donation to the fund at the time it is made and each accumulation made pursuant to a direction in applicable gift instrument at the time an accumulation is added to the fund. The law permitted an organization to spend the income earned by an endowment fund (i.e. interest, dividends), as well as the net appreciation (realized with respect to all assets and unrealized with respect to readily marketable assets) of such fund.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(o) Permanently Restricted Net Assets (Endowment Funds), Continued

Interpretation of Relevant Law, Continued

On September 17, 2010, the New York Prudent Management of Institutional Funds Act (NYPMIFA) was signed into New York State law. The most prominent feature of NYPMIFA is the elimination of the requirement to preserve an endowment fund's historic dollar value which allows an organization to spend from an endowment whose market value has dropped below the historic dollar value, as long as it is deemed prudent under the organization's policies. In accordance with NYPMIFA, an organization must consider the following factors in exercising a standard of prudence:

1. The duration and preservation of the endowment fund
2. The purposes of the organization and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the organization
7. The investment policies of the organization
8. Where appropriate, alternatives to spending from the endowment fund and the possible effects of those alternatives on the organization

NYPMIFA requires compliance with donor intent when making investment or spending decisions with respect to an endowment fund. In addition, NYPMIFA creates a restriction on the portion of an endowment fund that is not classified as permanently restricted net assets, even in the absence of a donor restriction. Such portion is classified as temporarily restricted net assets until appropriated for expenditure by the organization.

The Corporation has interpreted NYPMIFA as requiring the preservation of the purchasing power of the donor restricted endowment funds absent explicit donor stipulations to the contrary. As a result, Healthcare continues to classify permanently restricted net assets at the historic dollar value of the fund in accordance with donor instructions.

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 NYPMIFA requires the Corporation to retain as a fund of perpetual duration. If the situation were to occur, the deficiency would be recorded in the Corporation's unrestricted net assets. A deficiency did not exist at December 31, 2016 or 2015.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies. Continued

(o) Permanently Restricted Net Assets (Endowment Funds). Continued

Return Objectives, Strategies, Spending Policy and Investment Objectives

The Corporation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment. Under this policy, as approved by the Board of Directors, the endowment assets are to be invested in a well-diversified asset mix that can be expected to generate acceptable long-term returns at an acceptable level of risk. The Corporation targets a diversified asset allocation that places a greater emphasis on equity-based investments and bonds to achieve its long-term return objectives within prudent risk constraints.

Changes in Endowment Net Assets

	2016		
	<u>Unrestricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, January 1	\$ 44,788	4,528,164	4,572,952
Investment return:			
Investment income	-	138,564	138,564
Disbursements	-	(299,005)	(299,005)
Net gain (realized and unrealized)	-	294,018	294,018
Transfer of earnings over historical value	133,577	(133,577)	-
Endowment net assets, December 31	\$ 178,365	4,528,164	4,706,529
	2015		
	<u>Unrestricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, January 1	\$ 328,656	4,528,164	4,856,820
Investment return:			
Investment income	-	111,478	111,478
Net loss (realized and unrealized)	-	(395,346)	(395,346)
Transfer of earnings over historical value	(283,868)	283,868	-
Endowment net assets, December 31	\$ 44,788	4,528,164	4,572,952

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(p) Net Patient Service Revenue and Patient Accounts Receivable

Healthcare has agreements with third-party payors that provide for payments to the various organizations within its healthcare delivery system at amounts different from their established rates. Payment arrangements include prospectively determined rates per discharge or visit, cost-based reimbursement, discounted charges, per diem payments and fee-for-service payments. Healthcare recognizes patient service revenue associated with services provided to patients who have third-party coverage on the basis of contractual rates for the services rendered, including estimated retroactive adjustments due to future audits, reviews and investigations. Retroactive adjustments are included in the recognition of revenue on an estimated basis in the period the related services are rendered and adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews and investigations. Healthcare recognizes revenue for uninsured patients who do not qualify for charity care at standard rates, less a 40% self-pay discount. On the basis of historical experience, a significant portion of Healthcare's uninsured patients will be unable or unwilling to pay for the services provided. Thus, Healthcare records a provision for bad debts related to uninsured patients in the period the services are provided. Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts) from these major payor sources, is as follows for the years ended December 31:

	2016			
	<u>Government payors</u>	<u>Commercial insurance and others</u>	<u>Self-pay</u>	<u>Total</u>
Patient service revenue (net of contractual allowances and discounts)	\$ 163,075,720	108,638,348	1,848,945	273,563,013
	\$ 163,075,720	108,638,348	1,848,945	273,563,013
	2015			
	<u>Government payors</u>	<u>Commercial insurance and others</u>	<u>Self-pay</u>	<u>Total</u>
Patient service revenue (net of contractual allowances and discounts)	\$ 151,712,147	112,022,692	3,869,118	267,603,957
	\$ 151,712,147	112,022,692	3,869,118	267,603,957

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(p) Net Patient Service Revenue and Patient Accounts Receivable, Continued

Revenue from the Medicare and Medicaid programs accounted for approximately 60% and 57% of Healthcare's patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts) for 2016 and 2015, respectively. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Patient service revenue increased approximately \$1,443,000 and \$60,000 in 2016 and 2015, respectively, related to either settlement of prior year issues or changes in estimates associated with third-party issues. As of December 31, 2016, all cost reports through 2015 have been filed and Medicare cost reports through 2012 have been final settled.

Healthcare grants unsecured credit to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at December 31 was as follows:

	<u>2016</u>	<u>2015</u>
Medicare	33%	37%
Medicaid	18%	19%
Private payors	4%	3%
Insurance and all others	<u>45%</u>	<u>41%</u>
	<u>100%</u>	<u>100%</u>

Patient accounts receivable are reduced by a reserve for doubtful accounts. In evaluating the collectability of patient accounts receivable, Healthcare analyzes past payment history and identifies trends for each of its major payor sources of revenue to estimate the appropriate reserve for doubtful accounts and provision for bad debts. For receivables associated with patients who have third-party coverage, Healthcare analyzes contractually due amounts and provides a reserve for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments, 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), Healthcare records a reserve for doubtful accounts and a provision for bad debts in the period of service based on 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 amount actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies. Continued

(p) Net Patient Service Revenue and Patient Accounts Receivable. Continued

Healthcare's reserve for doubtful accounts was approximately 79% and 82% of self-pay accounts receivable at December 31, 2016 and 2015, respectively. Healthcare has not changed its charity care policy during 2016 or 2015. Healthcare does not maintain a material allowance for doubtful accounts from third-party payors, nor did it have significant write-offs from third-party payors.

(q) Charity Care

Healthcare provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Because Healthcare does not pursue collection of such amounts, they are not reported as net patient service revenue. During 2016 and 2015, costs incurred by Healthcare in the provision of charity care were based on the ratio of Healthcare's costs to gross charges and approximated \$490,000 and \$350,000, respectively.

(r) Contributions

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. Contributions are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the consolidated statements of operations and changes in net assets.

Conditional contributions or intents to give are recorded when donor-imposed stipulations have been substantially met.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(1) Description of Organization and Summary of Significant Accounting Policies, Continued

(s) Excess of Revenues over Expenses

The consolidated statements of operations and changes in net assets include excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include changes in unrealized gains and losses on investments other than trading securities, the effective portion of gains and losses on derivative instruments, permanent transfers of assets to and from affiliates for other than goods and services and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets).

(t) Income Taxes

Healthcare and the Foundation are not-for-profit corporations and have been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code. As of December 31, 2016 and 2015, Healthcare and the Foundation did not have any unrecognized tax benefits or any related accrued interest or penalties. The tax years open to examination by federal and state taxing authorities are 2013 through 2016. Healthcare and the Foundation do not anticipate the total unrecognized tax benefits will change in the next twelve months.

(u) Concentration of Credit Risk

The Corporation invests cash and cash equivalents with financial institutions, and has determined that the amount of credit exposure at any one financial institution is immaterial to the Corporation's financial position.

(v) Subsequent Events

In April 2017, MVHS was notified by the New York State Department of Health of an award of \$300 million granted under the Statewide Health Care Facility Transformation Program. This program provides funds to health care providers for the purpose of strengthening and protecting continued access to health care services in communities throughout New York State which are associated with a merger, consolidation or significant corporate restructuring activity that is part of an overall transformation plan intended to create a financially sustainable system of care. This award will be used by MVHS to consolidate inpatient care from Healthcare and SEMC into one, new integrated health campus. The cost projection for the new campus is estimated to be \$480 million for a 750,000 square-foot facility. The remaining \$180 million will come from MVHS capital, bonds and fundraising. The planning and construction for this project is expected to take approximately 5 years.

Subsequent events have been evaluated through May 31, 2017, which is the date consolidated financial statements were issued.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(2) Investments and Assets Limited as to Use

At December 31, investments and assets limited as to use, at fair value, are comprised of the following:

	<u>2016</u>	<u>2015</u>
Investments:		
Cash and cash equivalents	\$ 377,336	812,716
Mutual funds	49,664,271	44,593,424
Common stock	2,516,036	2,227,704
Pooled investment funds	<u>35,325,259</u>	<u>35,360,634</u>
	87,882,902	82,994,478
Accrued investment income	<u>-</u>	<u>353,578</u>
Total investments	87,882,902	83,348,056
Assets limited as to use - cash and cash equivalent	<u>250,000</u>	<u>250,000</u>
Total investments and assets limited as to use	<u>\$ 88,132,902</u>	<u>83,598,056</u>

The above amounts are included in the accompanying consolidated financial statements as follows:

	<u>2016</u>	<u>2015</u>
Investments and assets limited as to use - current assets	\$ 83,284,031	78,379,823
Cash and cash equivalents	320,707	690,069
Investments - long term	<u>4,528,164</u>	<u>4,528,164</u>
	<u>\$ 88,132,902</u>	<u>83,598,056</u>

Investment income (loss) and gains (losses) on investments are comprised of the following for the years ended December 31:

	<u>2016</u>	<u>2015</u>
Investment income:		
Interest income and dividends, net of fees	\$ 761,866	1,411,171
Realized gains	<u>396,312</u>	<u>1,585,939</u>
	1,158,178	2,997,110
Change in net unrealized gains and losses on investments	<u>3,773,782</u>	<u>(6,822,127)</u>
	<u>\$ 4,931,960</u>	<u>(3,825,017)</u>

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(2) Investments and Assets Limited as to Use, Continued

The Corporation continually reviews investments for other-than-temporary impairment whenever the fair value of an investment is less than amortized cost and evidence indicates that an investment's carrying amount is not recoverable within a reasonable period of time. In the evaluation of whether an impairment is other-than-temporary, the Corporation considers the reasons for the impairment, its ability and intent to hold the investment until the market price recovers or the investment matures, compliance with its investment policy, the severity and duration of the impairment, and expected future performance.

The Corporation's investments in common stocks, mutual funds and pooled investment funds consist of investments diversified in several different industries. The Corporation evaluated the near-term prospects of the issuer in relation to the severity and duration of impairment. Based upon the evaluation and the Corporation's ability and intent to hold the securities for a reasonable period of time sufficient for a forecasted recovery of fair value, the Corporation does not consider the securities in an unrealized loss position to be other-than-temporarily impaired at December 31, 2016 or 2015.

The following table presents the gross unrealized losses and fair value of the Corporation's investment portfolio with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2016 and 2015:

<u>Securities</u>	2016					
	<u>Less than Twelve Months</u>		<u>Twelve Months or Greater</u>		<u>Total</u>	
	<u>Fair value</u>	<u>Unrealized losses</u>	<u>Fair value</u>	<u>Unrealized losses</u>	<u>Fair value</u>	<u>Unrealized losses</u>
Mutual funds	\$ -	-	22,076,737	(1,623,864)	22,076,737	(1,623,864)
Common stocks	301,948	(19,785)	203,942	(55,044)	505,890	(74,829)
Pooled investment funds	-	-	2,523,034	(1,355,619)	2,523,034	(1,355,619)
	<u>\$ 301,948</u>	<u>(19,785)</u>	<u>24,803,713</u>	<u>(3,034,527)</u>	<u>25,105,661</u>	<u>(3,054,312)</u>
<u>Securities</u>	2015					
	<u>Less than Twelve Months</u>		<u>Twelve Months or Greater</u>		<u>Total</u>	
	<u>Fair value</u>	<u>Unrealized losses</u>	<u>Fair value</u>	<u>Unrealized losses</u>	<u>Fair value</u>	<u>Unrealized losses</u>
Mutual funds	\$ 13,733,281	(1,048,785)	8,719,906	(1,892,951)	22,453,187	(2,941,736)
Common stocks	720,636	(124,472)	220,999	(117,152)	941,635	(241,624)
Pooled investment funds	1,034,462	(65,538)	2,013,311	(1,515,042)	3,047,773	(1,580,580)
	<u>\$ 15,488,379</u>	<u>(1,238,795)</u>	<u>10,954,216</u>	<u>(3,525,145)</u>	<u>26,442,595</u>	<u>(4,763,940)</u>

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(3) Property and Equipment

Property and equipment is comprised of the following at December 31:

	<u>2016</u>	<u>2015</u>
Land and land improvements	\$ 7,661,125	7,496,286
Buildings	124,904,575	118,577,613
Fixed equipment	46,193,246	42,961,551
Movable equipment	118,574,318	123,654,847
Property and equipment under capitalized leases	21,877,952	20,118,609
	<u>319,211,216</u>	<u>312,808,906</u>
Less accumulated depreciation and amortization	<u>(242,097,684)</u>	<u>(236,445,605)</u>
	77,113,532	76,363,301
Construction-in-progress	1,238,674	1,613,252
	<u>1,238,674</u>	<u>1,613,252</u>
Property and equipment, net	\$ <u>78,352,206</u>	<u>77,976,553</u>

Depreciation and amortization expense amounted to approximately \$14,273,000 and \$16,078,000 for the years ended December 31, 2016 and 2015, respectively.

(4) Direct Financing Lease

In 2001, Healthcare completed construction of a medical office building with a cost of approximately \$5 million on land owned by an affiliate of Slocum-Dickson Medical Group, P.C. (SDMG). The building is leased to SDMG under a direct financing lease for minimum lease payments of approximately \$45,000 per month through November 2021.

The consolidated balance sheet presentation of the direct financing lease at December 31 is as follows:

	<u>2016</u>	<u>2015</u>
Minimum lease payments receivable	\$ 2,671,015	3,218,131
Unearned lease income	<u>(436,342)</u>	<u>(614,168)</u>
Net investment in direct financing lease	2,234,673	2,603,963
Less current portion, included in other current assets	<u>547,116</u>	<u>547,116</u>
Long-term net investment in direct financing lease, included in other assets	\$ <u>1,687,557</u>	<u>2,056,847</u>

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(5) Extended Sick Leave

The Corporation employees are permitted to accumulate unused extended sick leave time up to specified maximum amounts. The Corporation accrues the estimated expense related to extended sick leave based on pay rates currently in effect. Upon retirement, employees who have met certain criteria shall have the option to receive payment or receive sick leave credits to pay for post-employment health insurance payments based upon the formula in place. The Corporation has accrued an estimated liability of approximately \$11,405,000 and \$10,893,000 at December 31, 2016 and 2015, respectively, for these anticipated termination payments.

Amounts are included in the accompanying consolidated financial statements as follows at December 31:

	<u>2016</u>	<u>2015</u>
Accrued payroll, payroll taxes and benefits	\$ 580,000	658,000
Other liabilities	<u>10,825,000</u>	<u>10,235,000</u>
	<u>\$ 11,405,000</u>	<u>10,893,000</u>

(6) Long-Term Debt and Lease Obligations

Long-term debt consists of the following at December 31:

	<u>2016</u>	<u>2015</u>
Variable rate demand 2006 Civic Facility Revenue Bonds (a)	\$ 15,120,000	15,740,000
Revolving note payable (b)	-	5,623,000
Note payable in monthly principal installments of \$75,000, maturing April 2018 (c)	1,200,000	2,100,000
Note payable in monthly installments beginning July 2016 of \$65,617 at a fixed rate of 2.6% maturing May 2021 (d)	3,338,027	1,174,189
Mortgage payable in monthly installments of \$44,248 at a fixed rate of 4.5%, maturing January 2020 and collateralized by the related building	1,413,214	1,830,328

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(6) Long-Term Debt and Lease Obligations, Continued

	<u>2016</u>	<u>2015</u>
Note payable in monthly installments of \$27,664 at a fixed rate of 4.0%, maturing October 2018	585,646	887,116
Note payable in monthly installments of \$15,249 at a fixed rate of 5.5% through March 2017	55,773	230,316
Note payable in monthly installments of \$9,223 at a fixed rate of 4.0% maturing July 2020	368,003	461,627
Note payable in monthly installments beginning April 2016 of \$9,137 at an adjustable fixed rate of 4.0% (through March 2021) maturing March 2026	844,514	900,000
Other	-	12,360
Capital lease obligations (interest rates ranging from 2.6% to 8.0%)	<u>9,559,727</u>	<u>10,110,490</u>
	32,484,904	39,069,426
Less unamortized debt issuance costs	<u>(370,486)</u>	<u>(396,037)</u>
	32,114,418	38,673,389
Less current portion:		
Revolving note payable	-	(5,623,000)
Debt	(3,186,209)	(3,752,367)
Capital lease obligations	<u>(4,076,665)</u>	<u>(3,825,676)</u>
Long-term debt, net of current portion and unamortized debt issuance costs	<u>\$ 24,851,544</u>	<u>25,472,346</u>

(a) Healthcare, through the Oneida County Industrial Development Agency (OCIDA), has issued serial and term Civic Facility Revenue Bonds as follows:

<u>Series</u>	<u>Term</u>	<u>Annual principal payments</u>
Faxton-St. Luke's Healthcare:		
2006E - tax-exempt	2031	\$250,000 - \$525,000
2006F - taxable	2031	\$350,000 - \$955,000

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(6) Long-Term Debt and Lease Obligations, Continued

The bonds are insured and are collateralized by Healthcare's gross receipts (as defined), including all rights to receive such receipts whether in the form of accounts receivable, contract rights or other rights. Healthcare entered into a lease agreement with OCIDA, which also acts as security for payment of the revenue bonds. Additional security is provided by a Master Trust Indenture under which the initial Members of the Obligated Group (Healthcare and MVHS) are jointly and severally responsible for payment of the bonds. Various agreements relating to the bonds establish covenants with which Healthcare has agreed to comply, including provisions regarding liquidity ratio, minimum debt service coverage ratio and liquidity to funded debt. At December 31, 2016 and 2015, the Obligated Group was in compliance with the covenants that are considered events of default.

The bonds bear interest based on one of three modes - the weekly rate, the term rate, or the fixed rate - for periods selected by Healthcare. The interest rate for each mode will be the current market interest rate as determined by the remarketing agent of the bonds. Healthcare used the weekly rate during 2016 and 2015. At December 31, 2016, the bonds carried interest at rates of 0.83% (tax-exempt) and 0.88% (taxable). At December 31, 2015, the bonds carried interest at rates of 0.03% (tax-exempt) and 0.40% (taxable).

The bonds are remarketed by a remarketing agent in accordance with the terms of a remarketing agreement. The bonds will be remarketed whenever a new interest rate is in effect. If the bonds cannot be remarketed, they would be due and payable under the terms of the remarketing agreement; however, the bonds are credit-enhanced by an irrevocable letter of credit, which is set to expire June 26, 2018. In the event that the remarketing agent is unable to remarket the bonds, the bond trustee will make a draw on the letter of credit and the tendered variable rate bonds will become bank bonds.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(6) Long-Term Debt and Lease Obligations, Continued

As a result of the aforementioned 2006 bond issuances, Healthcare has entered into two interest rate swap contracts to reduce its risk of exposure to changes in interest rates. The interest rate swaps effectively convert the variable rates of the 2006 bonds to fixed rates of 5.938% and 4.216% through June 2031. The swaps have been designated as cash flow hedges of the variable interest rates and are recorded at fair value as a liability of \$3,964,349 in other liabilities on the accompanying consolidated balance sheet as of December 31, 2016. The amounts exchanged are based on the notional amounts whereby Healthcare pays the swap counter-party interest at a fixed rate (4.216% - tax-exempt, 5.938% - taxable) and the swap counter-party pays Healthcare a variable rate (based on 70% of 1 month LIBOR tax-exempt, BMA Rate - taxable). The notional amounts and fair values based on quoted market prices, of Healthcare's interest rate swaps are as follows at December 31, 2016:

	<u>Notional amount</u>	<u>Liability fair value</u>
Healthcare - Series E	\$ 5,660,000	1,166,636
Healthcare - Series F	<u>9,460,000</u>	<u>2,797,713</u>
	<u>\$ 15,120,000</u>	<u>3,964,349</u>

The mark-to-market adjustments resulted in an increase of approximately \$634,000 and \$239,000 in unrestricted net assets for the years ended December 31, 2016 and 2015, respectively. Changes in value of the swaps determined to arise from ineffectiveness of the instruments, as determined through the hypothetical derivative method, are recorded as a component of interest expense in the consolidated statements of operations and changes in net assets. For the years ended December 31, 2016 and 2015, there was no significant ineffectiveness. Healthcare expects that the loss existing in unrestricted net assets to be reclassified into net loss from operations within the next 12 months will not be significant.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(6) Long-Term Debt and Lease Obligations, Continued

(b) At December 31, 2016 and 2015, Healthcare had a \$24,500,000 revolving note payable with a bank, collateralized by certain investments. The revolving note payable on short-term borrowings bears a daily interest rate at prime (3.75% at December 31, 2016). The revolving note payable on long-term borrowings bears a monthly interest rate at 1 month LIBOR plus 95 basis points (1.72% at December 31, 2016). The revolving note payable is available through July 2017. At December 31, 2016, a portion of the revolving note payable was reserved for four letters of credit totalling approximately \$7,317,000 primarily related to self-insured liabilities. At December 31, 2015, Healthcare had \$623,000 outstanding on the short-term borrowings. At December 31, 2016 and 2015, Healthcare had \$0 and \$5,000,000 outstanding on the long-term borrowings, respectively. The revolving note payable contains financial covenants including a debt service coverage ratio requirement, a days cash on hand requirement and a minimum unrestricted liquidity to funded debt ratio. At December 31, 2016 and 2015, Healthcare was in compliance with the covenants that are considered events of default.

(c) The note payable bears interest at a rate of 1 month LIBOR plus 2.15% (2.92% at December 31, 2016). In connection with the note payable, Healthcare has entered into an interest rate swap contract to reduce its risk of exposure to changes in interest rates. The interest rate swap effectively converts the variable rates of the note payable to a fixed rate of 3.0% through April 2018. The swap has been designated as a cash flow hedge of the variable interest rate and is recorded at fair value as a liability of \$2,201 in other liabilities on the accompanying consolidated balance sheet as of December 31, 2016. The amounts exchanged are based on the notional amounts whereby Healthcare pays the swap counter-party interest at a fixed rate (3.0%) and the swap counter-party pays Healthcare a variable rate. The notional amount and fair value based on quoted market prices, of Healthcare's interest rate swap is as follows at December 31, 2016:

	<u>Notional amount</u>	<u>Liability fair value</u>
Healthcare - note payable	\$ 1,200,000	2,201

The mark-to-market adjustments resulted in an increase of \$2,713 in unrestricted net assets for the year ended December 31, 2015. Healthcare did not record mark-to-market adjustments for the year ended December 31, 2016. Changes in value of the swap determined to arise from ineffectiveness of the instrument, as determined through the hypothetical derivative method, is recorded as a component of interest expense in the consolidated statements of operations and changes in net assets. For the years ended December 31, 2016 and 2015, there was no significant ineffectiveness. Healthcare expects that the loss existing in unrestricted net assets to be reclassified into net loss from operations within the next 12 months will not be significant.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(6) Long-Term Debt and Lease Obligations. Continued

(d) In May 2016, SLM's note payable, with principal balance of \$3,683,334, of which approximately \$1,100,000 was already allocated and recorded by Healthcare, was assigned to Healthcare. In conjunction with the assignment, the bank agreed to extend the maturity date of loan through May 2021. The note payable is collateralized by the building constructed with the original funds. The note payable agreement contains various covenants including provisions regarding minimum days cash on hand, minimum debt service coverage ratio, and minimum unrestricted liquidity to funded debt ratio. At December 31, 2016, Healthcare was in compliance with the financial covenants that are considered events of default.

Healthcare leases certain equipment under capital leases. Healthcare also leases equipment and facilities under noncancellable operating leases, including leases with affiliates. The net book value of the equipment capitalized under lease agreements at December 31, 2016 and 2015 amounted to approximately \$10,303,000 and \$10,691,000, respectively.

The table below reflects principal payments and the present value of future minimum capital lease payments over the next five years and beyond and assumes that the letter of credit related to the 2006 Series E and F Bonds are renewed in 2018 and that Bank of New York does not exercise its put option for the 2006 Series Bonds in 2018. If the letter of credit is not renewed, the outstanding of the 2006 Series Bonds would be due on demand, as described above, in 2018.

	Long-term debt	Capital lease obligations	<u>Operating leases</u>	
			<u>Affiliates</u>	<u>Other</u>
Years ended December 31:				
2017	\$ 3,186,209	4,354,004	624,413	2,530,891
2018	2,675,447	2,844,022	624,413	1,627,291
2019	2,184,324	1,337,161	624,413	475,312
2020	1,670,431	937,621	624,413	428,956
2021	1,301,287	446,030	624,413	262,623
Thereafter	<u>11,907,479</u>	<u>266,084</u>		
Total payments	<u>\$ 22,925,177</u>	10,184,922		
Less amounts representing interest		<u>625,195</u>		
Present value of capital lease obligations		9,559,727		
Less current portion		<u>4,076,665</u>		
Capital lease obligations, net of current portion		<u>\$ 5,483,062</u>		

Rent expense under operating leases amounted to approximately \$5,619,000 and \$5,767,000 in 2016 and 2015, respectively.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(7) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes at December 31:

	<u>2016</u>	<u>2015</u>
Funds held in trust by others (for capital)	\$ 1,483,000	1,265,000
Children's Miracle Network	795,729	636,974
Continuous Learning Center	117,978	115,827
Scholarship assistance	31,199	31,199
Programs	511,354	709,973
Renovations	<u>889,869</u>	<u>1,499,162</u>
	<u>\$ 3,829,129</u>	<u>4,258,135</u>

Permanently restricted net assets at December 31 are restricted to:

	<u>2016</u>	<u>2015</u>
Investments to be held in perpetuity, the income from which is to support charity care, health care services, scholarships and facility maintenance	<u>\$ 4,528,164</u>	<u>4,528,164</u>

(8) Pension Plans

The Corporation sponsors a 401(k) plan that covers substantially all full-time non-union employees. The Corporation contributes 4% of eligible compensation to the plan (5% for employees hired before December 1, 2001). The Corporation also makes a matching contribution up to 100% of the first 4% of employee contributions to the 401(k) plan. The Corporation also sponsors a 403(b) plan that covers union and certain other employees. The Corporation contributes 5% of eligible compensation to the plan and also makes a matching contribution for employees with 5 years of service, up to 100% of the first 5% of employee contributions to the 403(b) plan.

Pension expense under all plans aggregated approximately \$6,486,000 in 2016 and approximately \$6,166,000 in 2015.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(9) Contingencies

Professional Liability Insurance

Malpractice insurance coverage is provided under a claims-made based policy, which provides for \$1,000,000 coverage for each claim, not to exceed \$3,000,000 in aggregate annual coverage. Additionally, the insurance policy includes a per claim \$50,000 uninsured deductible, not to exceed \$250,000 in aggregate annual coverage. A deposit for the \$250,000 has been established as required. In addition, the Corporation has purchased excess insurance policies. Claims alleging malpractice have been asserted against the Corporation and are currently in various stages of litigation. There are known claims and incidents that may result in the assertion of additional claims, as well as claims from unknown incidents that may be asserted relating to services provided to patients. Accrued malpractice losses in management's opinion provide an adequate reserve for loss contingencies. The Corporation has accrued a liability included in other liabilities of approximately \$18,935,000 and \$12,012,000 at December 31, 2016 and 2015, respectively. A corresponding receivable included in other assets of approximately \$16,575,000 and \$9,152,000, respectively, has been recorded to record anticipated recoveries from the insurance company.

Self-Insured Risks

The Corporation and certain affiliates are self-insured for employee healthcare costs. The group has obtained a stop loss coverage policy for healthcare costs to supplement its self-insurance coverage. An accrual for healthcare claims, including those incurred but not reported, is included in the current portion of estimated self-insured liabilities.

Workers' Compensation Insurance

The Corporation is primarily self-insured for employee workers' compensation and disability claims along with certain of its affiliates for certain years 2007 and prior. During 2016 and 2015, the Corporation and certain of its affiliates were enrolled in a high deductible plan with an insurance company with a deductible of \$500,000 for each employee and occurrence, and an aggregate deductible of \$7,900,000. Self-insured and high deductible liabilities are based on claims filed and estimates for claims incurred but not reported. As required by the State of New York Workers' Compensation Board, the Corporation has purchased letters of credit to guarantee payment of workers' compensation claims. Stop loss insurance for losses exceeding certain amounts has been purchased for workers' compensation. Each affiliate is jointly and severally liable for the satisfaction of all obligations. These liabilities are recorded at discounted amounts using a 3% and 4% interest rate in 2016 and 2015, respectively. From 2010 to 2014, the Corporation and certain of its affiliates were insured in a retrospectively rated workers' compensation and disability policy and premiums are accrued based on the ultimate cost of the experience to date of the Corporation and its affiliates. The Corporation has accrued a liability included in other liabilities and a corresponding receivable in other receivables for anticipated recoveries from the insurance company of approximately \$7,353,000 and \$6,642,000 as of December 31, 2016 and 2015, respectively.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(10) Affiliated Entities

The following represents summarized financial information from the consolidated financial statements of the Corporation's affiliates that are included in the accompanying consolidated financial statements on the equity method of accounting.

<u>2016</u>	<u>SLM</u>	<u>Paraffin</u>
Total assets	\$ -	244,868
Total liabilities	-	158,388
	<hr/>	<hr/>
Net assets	\$ -	86,480
	<hr/>	<hr/>
Total revenues	1,231,651	1,936,962
Total expenses	(1,140,472)	(1,833,579)
	<hr/>	<hr/>
Excess of revenues over expenses	\$ 91,179	103,383
	<hr/>	<hr/>
 <u>2015</u>	 <u>SLM</u>	 <u>Paraffin</u>
Total assets	\$ 4,648,163	146,745
Total liabilities	3,800,291	163,648
	<hr/>	<hr/>
Net assets (deficit)	\$ 847,872	(16,903)
	<hr/>	<hr/>
Total revenues	1,356,118	1,838,798
Total expenses	(1,238,396)	(1,902,061)
	<hr/>	<hr/>
Excess (deficiency) of revenues over expenses	\$ 117,722	(63,263)
	<hr/>	<hr/>

The following are approximate dollar amounts of significant transactions and balances with affiliated entities.

St. Elizabeth Medical Center

During 2016 and 2015, Healthcare advanced funds to the Medical Center. As of December 31, 2015, there was \$3,750,000 outstanding on this advance which is included within current portion of due from affiliates. There were no amounts outstanding at December 31, 2016. Total interest charged in 2016 and 2015 amounted to approximately \$28,000 and \$13,000, respectively.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(10) Affiliated Entities, Continued

St. Elizabeth Medical Center, Continued

Healthcare has contracted with the Medical Center to provide certain operational services, including shared employment, provider coverage, patient care, rental of office space, and other shared services as needed. In 2016 and 2015, Healthcare purchased services totalling approximately \$2,609,000 and \$1,420,000 respectively, from the Medical Center and sold services totalling approximately \$3,968,000 and \$2,115,000 respectively.

During 2015, Healthcare forgave a \$450,000 liability payable from the Medical Center which related to a joint venture prior to their affiliation. This was recorded as a transfer to affiliate for the year ended December 31, 2015.

St. Luke's Home

Healthcare has contracted with the Home to provide certain operational services. In 2016 and 2015, Healthcare purchased approximately \$1,233,000 and \$1,152,000, respectively for services rendered and rental of space within the Home. Healthcare billed the Home for services totalling approximately \$495,000 and \$469,000, respectively.

Visiting Nurses Association

Healthcare charges VNA for certain shared operating expenses paid on its behalf. Additionally, during 2015, Healthcare advanced funds to VNA to pay down the outstanding balance on their short-term borrowing arrangement. At December 31, 2016 and 2015, there was \$500,000 outstanding on this advance. Healthcare charged interest on a monthly basis through May 2016 using a monthly LIBOR rate plus 70 basis points. Total interest charged in 2016 and 2015 amounted to approximately \$2,000. The net receivable, before reserve, as of December 31, 2016 and 2015 was approximately \$3,280,000 and \$1,602,000, respectively. In 2016, Healthcare recorded a reserve for \$1,665,000 on the amounts due from VNA based on management's evaluation of VNA's historical and expected future cash flows. This reserve for doubtful accounts was recorded in the consolidated statements of operations and consolidated changes in net assets as a reduction of unrestricted net assets.

Healthcare billed VNA for certain shared services totalling approximately \$47,000 and \$109,000 in 2016 and 2015, respectively.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(10) Affiliated Entities. Continued

Senior Network Health

During 2016, Healthcare paid in full amounts previously loaned from SNH. The balance of the loan was approximately \$301,000 at December 31, 2015.

Healthcare billed SNH for certain shared services totalling approximately \$169,000 and \$220,000 in 2016 and 2015, respectively.

New Hartford Scanner Associates

New Hartford Scanner Associates (NHSA) is a joint venture between Healthcare and several radiologists to provide CT scan services. Healthcare receives income from NHSA, which amounted to approximately \$563,000 and \$621,000 in 2016 and 2015, respectively. Healthcare charges NHSA for equipment, which amounted to approximately \$120,000 in 2016 and 2015.

Mohawk Valley EC, LLC

Faxton-St. Luke's Healthcare, St. Elizabeth Medical Center and Mohawk Valley EC Holdings, LLC entered into an agreement for the purpose of owning and operating a single-specialty ambulatory surgery center, exclusively providing gastroenterology services in Oneida County. As part of the agreement, the three members formed the Mohawk Valley EC, LLC (MVEC), a New York limited liability company. Healthcare maintains a 20% interest and sharing ratio in MVEC. The amount recognized as income based on Healthcare's share is approximately \$219,000 and \$210,000 for the years ended December 31, 2016 and 2015, respectively.

Healthcare recognizes income from these joint ventures in other revenue.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(10) Affiliated Entities, Continued

Net receivables (payables) at December 31 from (to) affiliates for loans and advances, services performed and billing of other pass-through expenses to and from the Corporation were approximately as follows:

	<u>2016</u>	<u>2015</u>
Home	\$ (1,209,000)	(1,214,000)
MVHS	486,000	436,000
SEMC	1,939,000	5,119,000
New Hartford Scanner Associates	289,000	399,000
VNA	3,280,000	1,602,000
SLM	-	(64,000)
Paraffin	(74,000)	19,000
SNH	311,000	(395,000)
MVHC	15,000	99,000
	5,037,000	6,001,000
Reserve for doubtful accounts	(1,665,000)	-
	\$ 3,372,000	6,001,000

(11) Statements of Cash Flows - Supplemental Disclosures

The Corporation's non-cash investing and financing activity and cash payments for interest for the years ended December 31 were as follows:

	<u>2016</u>	<u>2015</u>
Capital lease obligations issued for property and equipment	\$ 3,674,880	1,026,801
Cash paid for interest	1,720,080	1,972,500
SLM Transfer:		
Debt obligations assumed, net	2,509,145	-
Net book value of fixed asset assumed	3,423,729	-

(12) Functional Expenses

The Corporation provides general health care services to residents of the Mohawk Valley Region. Expenses related to providing these services are as follows:

	<u>2016</u>	<u>2015</u>
Health care services	\$ 247,801,023	238,200,885
General and administrative	37,490,599	37,269,742
Fundraising	794,853	974,963
	\$ 286,086,475	276,445,590

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(13) Fair Value of Financial Instruments

The Fair Value Measurement Topic of the FASB Accounting Standards Codification requires disclosures that categorize assets and liabilities measured at fair value based on a fair value hierarchy. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which is determined by the lowest level input that is significant to the fair value measurement in its entirety.

The following methods and assumptions were used by the Corporation in estimating the fair value of its financial instruments:

Cash and Cash Equivalents: The amount reported on the balance sheet for cash and cash equivalents approximates fair value.

Mutual Funds and Common Stock: The fair values, which are the amounts reported on the consolidated balance sheets, are based on quoted market prices, if available, or estimated using quoted market prices for similar securities.

Pooled Investment Funds: Fair values are based on NAV per share as determined by the fund's investment manager or general partner.

Estimated Third-Party Payor Settlements: The amount reported on the consolidated balance sheet for estimated third-party payor settlements approximates its fair value.

Long-Term Debt: The fair value of fixed rate issues was determined by price quotes from an investment banker or estimated using discounted cash flow analysis, based on the current incremental borrowing rate of similar types of borrowing arrangements (considered a Level 2 input). The fair value of variable rate debt approximates its reported value on the consolidated balance sheet. Fixed rate long-term debt is the only financial instrument with a difference between recorded and fair value. The recorded value of fixed rate long-term debt on the consolidated balance sheet at December 31, 2016 approximates its fair value.

The following tables present information about assets and liabilities that are measured at fair value on a recurring basis as of December 31 and indicate the fair value hierarchy of the valuation techniques utilized to determine such fair value. In general, fair values determined by Level 1 inputs utilize quoted prices in active markets for identical assets or liabilities. The Corporation considers a security that trades at least weekly to have an active market. Fair values determined by Level 2 inputs utilize data points that are observable, such as quoted prices, interest rates and yield curves. Investments valued using NAV as a practical expedient are classified as Level 2 if the investment is redeemable at NAV (as adjusted for subsequent gains or losses through the effective date of redemption) in the near-term (generally within a 3-month period) without significant restrictions on redemption. Fair values determined by Level 3 inputs are unobservable data points for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. Investments valued using NAV as a practical expedient are classified as Level 3 if the investment is not redeemable in the near-term or has significant restrictions.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(13) Fair Value of Financial Instruments. Continued

	Total	Fair value measurements at December 31, 2016		
		Level 1	Level 2	Level 3
Assets:				
Cash and cash equivalents	\$ 320,707	320,707	-	-
Asset limited as to use - cash and cash equivalents	250,000	250,000	-	-
Investments:				
Cash and cash equivalents	56,629	56,629	-	-
Mutual funds:				
U.S. large cap	29,383,132	29,383,132	-	-
U.S. mid cap	6,721,491	6,721,491	-	-
Emerging markets	2,346,271	2,346,271	-	-
Fixed income funds	10,914,537	10,914,537	-	-
Other	298,840	298,840	-	-
	49,664,271	49,664,271	-	-
Common stock:				
Consumer	319,857	319,857	-	-
Energy	323,899	323,899	-	-
Financial	557,014	557,014	-	-
Healthcare	351,154	351,154	-	-
Industrial	336,418	336,418	-	-
Information technology	161,670	161,670	-	-
Materials	213,108	213,108	-	-
Utilities	252,916	252,916	-	-
	2,516,036	2,516,036	-	-
Pooled investment funds:				
Hedge funds	16,597,116	-	16,597,116	-
Real estate funds	4,988,137	-	4,988,137	-
Bond funds	4,102,897	-	4,102,897	-
Foreign equity funds	9,637,109	-	9,637,109	-
	35,325,259	-	35,325,259	-
Beneficial interest in charitable trust	1,483,000	-	1,483,000	-
Total assets at fair value	\$ 89,615,902	52,807,643	36,808,259	-
Cash and cash equivalents	320,707	320,707	-	-
Investments	89,295,195	52,486,936	36,808,259	-
Total	\$ 89,615,902	52,807,643	36,808,259	-
Liabilities:				
Interest rate swaps	\$ 3,966,550	-	3,966,550	-

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(13) Fair Value of Financial Instruments, Continued

	Total	Fair value measurements at December 31, 2015		
		Level 1	Level 2	Level 3
Assets:				
Cash and cash equivalents	\$ 690,069	690,069	-	-
Assets limited as to use - cash and cash equivalents	250,000	250,000	-	-
Investments:				
Cash and cash equivalents	122,647	122,647	-	-
Mutual funds:				
U.S. large cap	24,838,160	24,838,160	-	-
U.S. mid cap	5,174,798	5,174,798	-	-
Emerging markets	3,285,255	3,285,255	-	-
Fixed income funds	11,023,237	11,023,237	-	-
Other	271,974	271,974	-	-
	44,593,424	44,593,424	-	-
Common stock:				
Consumer	380,963	380,963	-	-
Energy	144,405	144,405	-	-
Financial	532,409	532,409	-	-
Healthcare	203,332	203,332	-	-
Industrial	335,455	335,455	-	-
Information technology	133,569	133,569	-	-
Materials	202,514	202,514	-	-
Utilities	295,057	295,057	-	-
	2,227,704	2,227,704	-	-
Pooled investment funds:				
Hedge funds	19,124,150	-	19,124,150	-
Real estate funds	4,806,977	-	4,806,977	-
Bond funds	3,956,277	-	3,956,277	-
Foreign equity funds	7,473,230	-	7,473,230	-
	35,360,634	-	35,360,634	-
Beneficial interest in charitable trust	1,265,000	-	1,265,000	-
Total assets at fair value	\$ 84,509,478	47,883,844	36,625,634	-
Cash and cash equivalents	690,069	690,069	-	-
Investments	83,819,409	47,193,775	36,625,634	-
Total	\$ 84,509,478	47,883,844	36,625,634	-
Liabilities:				
Interest rate swaps	\$ 4,600,438	-	4,600,438	-

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(13) Fair Value of Financial Instruments, Continued

The following is a summary of the investments whose NAV approximates fair value and the related redemption restrictions associated with each major category at December 31:

<u>Pooled investment funds</u>	2016		
	<u>Total fair value</u>	<u>Redemption frequency</u>	<u>Redemption notice periods</u>
Hedge funds	\$ 16,597,116	Monthly	90 days
Real estate funds	4,988,137	Monthly	None
Bond funds	4,102,897	Monthly	10 days
Foreign equity funds	<u>9,637,109</u>	Monthly	10 days
	<u>\$ 35,325,259</u>		
<u>Pooled investment funds</u>	2015		
	<u>Total fair value</u>	<u>Redemption frequency</u>	<u>Redemption notice periods</u>
Hedge funds	\$ 19,124,150	Monthly	90 days
Real estate funds	4,806,977	Monthly	None
Bond funds	3,956,277	Monthly	10 days
Foreign equity funds	<u>7,473,230</u>	Monthly	10 days
	<u>\$ 35,360,634</u>		

Hedge Funds

Hedge fund strategies involve funds with investment managers who have the authority to invest in various asset classes at their discretion and who have the ability to employ multiple investments strategies within their respective portfolios. Investment strategies may include the following categories: merger arbitrage, distressed, long/short credit, fixed income arbitrage and convertible arbitrage. These funds attempt to reduce individual manager risk by allocating capital among multiple investment managers. Funds with hedged strategies generally hold securities or other financial instruments for which a ready market exists and may include stocks, bonds, put or call options, swaps, currency hedges, and other instruments, and are valued accordingly.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Notes to Consolidated Financial Statements

(13) Fair Value of Financial Instruments, Continued

Real Estate Funds

Real estate funds hold interests in publicly traded equity securities issued by real estate investment trusts ("REIT"), private real estate partnerships, and privately held REIT's. Strategies of these funds often require the estimation of fair values by the fund managers in the absence of readily determinable market values. Because of the inherent uncertainties of valuation, these estimated fair values may differ significantly from values that would have been used had a ready market existed, and the differences could be material. Such valuations are determined by fund managers and generally consider variables such as operating results, comparable earnings multiples, projected cash flows, recent sales prices, and other pertinent information, and may reflect discounts for the illiquid nature of certain investments held. Moreover, the fair values of the Corporation's interests in shares or units of these funds, because of the liquidity and capital commitment terms that vary depending on the specific fund or partnership agreement, may differ from the fair value of the funds' underlying net assets.

Bond Funds

Bond funds are invested in a globally diversified portfolio of primarily debt and debt-like securities. The funds are controlled by an investment manager. The investment manager generally will acquire positions in debt securities and currencies that are rated investment grade by Standard & Poor's Credit Market Services, or if unrated, an equivalent rating determined by the investment manager at its sole discretion.

Foreign Equity Funds

Foreign equity funds are invested in a diversified portfolio of equity securities of companies ordinarily located in any country other than the United States and Canada. The funds are controlled by an investment manager.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidating Balance Sheet

December 31, 2016
with comparative consolidated amounts for 2015

<u>Assets</u>	<u>Faxton- St. Luke's Healthcare</u>	<u>Faxton- St. Luke's Healthcare Foundation</u>	<u>Eliminations</u>	<u>Consolidated</u>	
				<u>2016</u>	<u>2015</u>
Current assets:					
Cash and cash equivalents	\$ 5,450,066	352,508	-	5,802,574	1,458,858
Investments and assets limited as to use	79,476,377	3,807,654	-	83,284,031	78,379,823
Patient accounts receivable, net of reserve for doubtful accounts of approximately \$7,711,000 in 2016 and \$7,727,000 in 2015	31,516,572	-	-	31,516,572	38,999,629
Pledges receivable	-	335,273	-	335,273	571,367
Other current assets	6,853,883	-	-	6,853,883	5,424,254
Inventories	6,280,789	-	-	6,280,789	5,873,362
Prepaid expenses	3,283,008	52,544	-	3,335,552	3,003,276
Due to affiliates, net	1,531,083	-	(164,056)	1,367,027	4,044,954
Estimated third-party payor settlements, net	1,948,925	-	-	1,948,925	1,649,371
Total current assets	136,340,703	4,547,979	(164,056)	140,724,626	139,404,894
Interest in Faxton-St. Luke's Healthcare Foundation	6,638,537	-	(6,638,537)	-	-
Investment in affiliates	86,480	-	-	86,480	830,969
Due from affiliates, net	2,004,544	-	-	2,004,544	1,955,488
Investments	4,528,164	-	-	4,528,164	4,528,164
Beneficial interest in charitable trusts	-	1,483,000	-	1,483,000	1,265,000
Property and equipment, net	77,417,624	934,582	-	78,352,206	77,976,553
Other assets	24,453,511	-	-	24,453,511	18,589,053
Total assets	\$ <u>251,469,563</u>	<u>6,965,561</u>	<u>(6,802,593)</u>	<u>251,632,531</u>	<u>244,550,121</u>

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidating Balance Sheets, Continued

December 31, 2016

with comparative consolidated amounts for 2015

<u>Liabilities and Net Assets</u>	<u>Faxton- St. Luke's Healthcare</u>	<u>Faxton- St. Luke's Healthcare Foundation</u>	<u>Eliminations</u>	<u>Consolidated</u>	
				<u>2016</u>	<u>2015</u>
Current liabilities:					
Revolving note payable	\$ -	-	-	-	5,623,000
Current portion of long-term debt	3,186,209	-	-	3,186,209	3,752,367
Current portion of capital lease obligations	4,076,665	-	-	4,076,665	3,825,676
Accounts payable and accrued expenses	15,119,400	31,472	-	15,150,872	15,134,168
Accrued payroll, payroll taxes and benefits	12,095,220	-	-	12,095,220	10,392,132
Current portion of estimated insurance liabilities	4,623,654	-	-	4,623,654	5,798,357
Due to affiliates, net	-	164,056	(164,056)	-	-
Other current liabilities	4,518,701	131,496	-	4,650,197	3,032,187
Total current liabilities	43,619,849	327,024	(164,056)	43,782,817	47,557,887
Long-term debt, net of current portion:					
Notes payable	5,218,968	-	-	5,218,968	4,463,569
Civic facility revenue bonds	14,149,514	-	-	14,149,514	14,723,963
Capital lease obligations	5,483,062	-	-	5,483,062	6,284,814
Total long-term debt, net of current portion	24,851,544	-	-	24,851,544	25,472,346
Other liabilities	36,713,497	-	-	36,713,497	30,846,580
Estimated insurance liabilities, net of current portion	5,057,692	-	-	5,057,692	3,994,434
Total liabilities	110,242,582	327,024	(164,056)	110,405,550	107,871,247
Net assets:					
Unrestricted	132,869,688	2,840,607	(2,840,607)	132,869,688	127,892,575
Temporarily restricted	3,829,129	3,797,930	(3,797,930)	3,829,129	4,258,135
Permanently restricted	4,528,164	-	-	4,528,164	4,528,164
Total net assets	141,226,981	6,638,537	(6,638,537)	141,226,981	136,678,874
Commitments and contingencies (notes 6 and 9)					
Total liabilities and net assets	\$ 251,469,563	6,965,561	(6,802,593)	251,632,531	244,550,121

See accompanying independent auditor's report.

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidating Statements of Operations and Changes in Net Assets

Year ended December 31, 2016
with comparative consolidated amounts for 2015

	Faxton- St. Luke's Healthcare	Faxton- St. Luke's Healthcare Foundation	Eliminations	Consolidated	
				2016	2015
Unrestricted revenues, gains and other support:					
Patient service revenue (net of contractual allowances and discounts)	\$ 273,563,013	-	-	273,563,013	267,603,957
Provision for bad debts	(5,277,188)	-	-	(5,277,188)	(5,387,923)
Net patient service revenue less provision for bad debts	268,285,825	-	-	268,285,825	262,216,034
Other operating revenue	16,830,683	-	-	16,830,683	13,985,931
Net assets released from restrictions used for operations	293,032	2,083,349	(1,635,110)	741,271	900,853
Total unrestricted revenues, gains and other support	285,409,540	2,083,349	(1,635,110)	285,857,779	277,102,818
Expenses:					
Salaries and wages	137,717,892	308,805	-	138,026,697	129,371,185
Employee benefits	24,912,686	71,462	-	24,984,148	26,411,289
Supplies and other	105,543,613	2,048,983	(1,635,110)	105,957,486	101,516,920
Depreciation and amortization	14,272,035	713	-	14,272,748	16,078,436
Interest	1,743,087	-	-	1,743,087	1,998,101
New York State gross receipts taxes	1,102,309	-	-	1,102,309	1,069,659
Total expenses	285,291,622	2,429,963	(1,635,110)	286,086,475	276,445,590
Net income (loss) from operations	117,918	(346,614)	-	(228,696)	657,228
Other revenue (expense):					
Contributions and other unrestricted revenue (expense)	(191,716)	112,849	-	(78,867)	(1,465,539)
Investment income, net of fees	1,032,218	125,960	-	1,158,178	2,997,110
Total other revenue, net	840,502	238,809	-	1,079,311	1,531,571
Excess (deficiency) of revenues over expenses	\$ 958,420	(107,805)	-	850,615	2,188,799

FAXTON-ST. LUKE'S HEALTHCARE AND AFFILIATE

Consolidating Statements of Operations and Changes in Net Assets, Continued

Year ended December 31, 2016
with comparative consolidated amounts for 2015

	Faxton- St. Luke's Healthcare	Faxton- St. Luke's Healthcare Foundation	Eliminations	<u>Consolidated</u>	
				2016	2015
Unrestricted net assets:					
Excess (deficiency) of revenues over expenses	\$ 958,420	(107,805)	-	850,615	2,188,799
Change in fair value of interest rate swaps	633,888	-	-	633,888	241,570
Change in interest in unrestricted net assets of Foundation	61,219	-	(61,219)	-	-
Net assets released for capital acquisitions	1,342,078	-	-	1,342,078	780,004
Contributions used for capital acquisitions	41,750	-	-	41,750	85,094
Transfer to affiliate	-	-	-	-	(450,000)
Reserve for doubtful accounts due from affiliate	(1,665,000)	-	-	(1,665,000)	-
Change in net unrealized gains and losses on investments	3,604,758	169,024	-	3,773,782	(6,822,127)
Increase (decrease) in unrestricted net assets	<u>4,977,113</u>	<u>61,219</u>	<u>(61,219)</u>	<u>4,977,113</u>	<u>(3,976,660)</u>
Temporarily restricted net assets:					
Contributions	-	1,436,343	-	1,436,343	1,998,338
Change in value of charitable trusts	-	218,000	-	218,000	(13,000)
Net assets released from restrictions	-	(2,083,349)	-	(2,083,349)	(1,680,857)
Change in interest in temporarily restricted net assets of Foundation	(429,006)	-	429,006	-	-
Increase (decrease) in temporarily restricted net assets	<u>(429,006)</u>	<u>(429,006)</u>	<u>429,006</u>	<u>(429,006)</u>	<u>304,481</u>
Total increase (decrease) in net assets	4,548,107	(367,787)	367,787	4,548,107	(3,672,179)
Net assets at beginning of year	<u>136,678,874</u>	<u>7,006,324</u>	<u>(7,006,324)</u>	<u>136,678,874</u>	<u>140,351,053</u>
Net assets at end of year	<u>\$ 141,226,981</u>	<u>6,638,537</u>	<u>(6,638,537)</u>	<u>141,226,981</u>	<u>136,678,874</u>

See accompanying independent auditor's report.