

**ST. ELIZABETH MEDICAL CENTER
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 St. Elizabeth Medical Center 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 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.

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 St. Elizabeth Medical Center 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.

Fust Charles Chambers LLP

May 22, 2017

**ST. ELIZABETH MEDICAL CENTER
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	\$ 8,200,918	5,902,557
Assets limited as to use	109,549	63,909
Investments	9,690,864	9,391,986
Patient accounts receivable, net of allowance for doubtful accounts of approximately \$5,400,000 in 2016 and \$6,300,000 in 2015	24,272,573	25,942,360
Other current assets	2,122,661	1,738,811
Inventories	5,792,039	5,590,544
Prepaid expenses	1,579,098	1,390,560
Total current assets	51,767,702	50,020,727
Assets limited as to use	3,934,345	4,003,224
Property and equipment, net	64,604,940	70,615,095
Other assets	816,347	1,260,723
Total assets	\$ 121,123,334	125,899,769
<u>Liabilities and Net Assets</u>		
Current liabilities:		
Current portion of long-term debt	1,619,248	1,550,550
Current portion of capital lease obligations	343,825	404,670
Current portion of estimated insurance liabilities	2,843,746	1,236,428
Accounts payable and accrued expenses	16,768,469	18,864,923
Accrued payroll, payroll taxes and benefits	7,868,797	7,724,790
Estimated third-party payor settlements, net	3,854,892	3,545,389
Due to affiliates, net	1,879,496	5,181,453
Other current liabilities	250,466	316,380
Total current liabilities	35,428,939	38,824,583
Accrued pension liability	46,815,314	50,183,961
Long-term portion of debt	24,936,889	26,452,589
Capital lease obligations	585,888	929,713
Estimated insurance liabilities	3,665,471	4,381,699
Other long-term liabilities	678,498	536,284
Total liabilities	112,110,999	121,308,829
Net assets:		
Unrestricted	7,596,468	3,250,882
Temporarily restricted	469,561	421,769
Permanently restricted	946,306	918,289
Total net assets	9,012,335	4,590,940
Commitments and contingencies (notes 5 and 8)		
Total liabilities and net assets	\$ 121,123,334	125,899,769

See accompanying notes to the consolidated financial statements.

**ST. ELIZABETH MEDICAL CENTER
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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)	\$ 217,633,469	205,681,545
Provision for bad debts	<u>(6,268,979)</u>	<u>(7,845,812)</u>
Net patient service revenue less provision for bad debts	211,364,490	197,835,733
Other operating revenue	6,225,037	6,701,146
Net assets released from restrictions used for operations	<u>21,250</u>	<u>40,469</u>
Total unrestricted revenues, gains and other support	<u>217,610,777</u>	<u>204,577,348</u>
Expenses:		
Salaries and wages	103,019,932	101,720,950
Employee benefits	22,809,678	21,560,839
Supplies and other	78,642,213	73,080,786
Depreciation and amortization	10,454,515	10,605,624
Interest	1,427,239	1,554,662
New York State gross receipts taxes	<u>674,428</u>	<u>614,897</u>
Total expenses	<u>217,028,005</u>	<u>209,137,758</u>
Gain (loss) from operations	<u>582,772</u>	<u>(4,560,410)</u>
Other revenue:		
Contributions and other unrestricted revenue	73,237	96,477
Investment income, net of fees	<u>355,557</u>	<u>342,288</u>
Total other income	<u>428,794</u>	<u>438,765</u>
Excess (deficiency) of revenues over expenses	1,011,566	(4,121,645)
Change in net unrealized gains and losses on investments	205,781	(261,537)
Pension related changes other than net periodic pension cost	2,672,766	270,191
Contribution from affiliate	-	450,000
Investment income (loss) on board designated net assets	261,472	(56,094)
Net assets released from restrictions used for capital purposes	<u>194,001</u>	<u>519,162</u>
Increase (decrease) in unrestricted net assets	<u>4,345,586</u>	<u>(3,199,923)</u>

**ST. ELIZABETH MEDICAL CENTER
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Consolidated Statements of Operations and Changes in Net Assets, Continued

	<u>2016</u>	<u>2015</u>
Temporarily restricted net assets:		
Contributions	227,191	409,435
Change in net unrealized gains and losses on investments	22,510	42,548
Interest income on permanently restricted net assets	13,342	14,619
Net assets released from restrictions	<u>(215,251)</u>	<u>(559,631)</u>
Increase (decrease) in temporarily restricted net assets	<u>47,792</u>	<u>(93,029)</u>
Permanently restricted net assets:		
Contributions	<u>28,017</u>	<u>34,258</u>
Increase in permanently restricted net assets	<u>28,017</u>	<u>34,258</u>
Total increase (decrease) in net assets	4,421,395	(3,258,694)
Net assets at beginning of year	<u>4,590,940</u>	<u>7,849,634</u>
Net assets at end of year	<u>\$ 9,012,335</u>	<u>4,590,940</u>

See accompanying notes to the consolidated financial statements.

**ST. ELIZABETH MEDICAL CENTER
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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	\$ 4,421,395	(3,258,694)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	10,454,515	10,605,624
Provision for bad debts	6,268,979	7,845,812
Amortization of debt issuance costs	88,441	88,441
Contribution from affiliate	-	(450,000)
Decrease in pension related changes other than net periodic pension cost	(2,672,766)	(270,191)
Change in net unrealized gains and losses on investments	(205,781)	261,537
Investment (loss) income on board designated net assets	(261,472)	56,094
(Gain) loss on sale of assets	(15,388)	22,424
Contributions received for long-term purposes	(194,001)	(443,543)
Changes in operating assets and liabilities:		
Patient accounts receivable	(4,599,192)	(5,726,271)
Inventories	(201,495)	(495,408)
Due to affiliate, net	448,043	1,594,550
Prepaid expenses	(188,538)	(486,799)
Other assets	60,526	(622,515)
Accounts payable and accrued expenses	(2,645,017)	(1,180,713)
Estimated third-party payors settlements, net	309,503	110,125
Accrued pension liability	(695,881)	(60,483)
Other liabilities	967,390	(150,986)
Net cash provided by operating activities	<u>11,339,261</u>	<u>7,439,004</u>
Cash flows from investing activities:		
Purchases of property and equipment	(3,751,790)	(5,968,754)
Proceeds from sale of property and equipment	15,388	-
Change in assets limited as to use	490,492	(314,742)
Change in investments, net	(298,878)	631,082
Net cash used in investing activities	<u>(3,544,788)</u>	<u>(5,652,414)</u>
Cash flows from financing activities:		
Short-term borrowings paid off	-	(4,000,000)
Proceeds from (payments on) affiliate advances	(3,750,000)	3,750,000
Proceeds from long-term debt	-	500,000
Principal payments of long-term debt and capital lease obligations	(1,940,113)	(1,945,900)
Contributions received for long-term purposes	194,001	443,543
Net cash used in financing activities	<u>(5,496,112)</u>	<u>(1,252,357)</u>
Net increase in cash and cash equivalents	2,298,361	534,233
Cash and cash equivalents at beginning of year	5,902,557	5,368,324
Cash and cash equivalents at end of year	<u>\$ 8,200,918</u>	<u>5,902,557</u>

See accompanying notes to the consolidated financial statements.

**ST. ELIZABETH MEDICAL CENTER
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Notes to Consolidated Financial Statements

December 31, 2016 and 2015

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

(a) Organization

St. Elizabeth Medical Center (the Medical Center) is a voluntary not-for-profit acute care facility located in Utica, New York. The Medical Center provides medical, surgical, and psychiatric inpatient services. In addition, the Medical Center offers outpatient general diagnostic, ambulatory care, physical therapy, and emergency care services.

St. Elizabeth Medical Center Foundation, Inc. (the Foundation) is a not-for-profit organization whose primary purpose is to solicit, collect, and invest funds on behalf of the Medical Center.

Mohawk Valley Health System (MVHS), a not-for-profit corporation, and Partners in Ministries, Inc., which is sponsored by the Sisters of St. Francis of the Neumann Communities, are co-members of the Medical Center. MVHS is also the sole corporate member of various other organizations involved in providing healthcare services to the Mohawk Valley Region.

(b) 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 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. The Medical Center 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 \$665,584 on the balance sheet for the year ended December 31, 2015, a reclassification of \$88,441 of amortization of debt issuance costs from depreciation and amortization to interest expense on the consolidated statements of operations and changes in net assets and cash flows (cash flows from operations) for the year ended December 31, 2015, but had no effect on deficiency of revenues over expenses or net assets as of or for the year ended December 31, 2015.

**ST. ELIZABETH MEDICAL CENTER
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Notes to Consolidated Financial Statements

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

(c) Basis of Accounting

The accompanying consolidated financial statements include the accounts of the Medical Center and the Foundation. The Medical Center is the sole corporate member of the Foundation. For financial reporting purposes, the Medical Center is considered the reporting entity. All significant intercompany balances and transactions have been eliminated in the consolidated financial statements.

As a member of MVHS, the Medical Center is affiliated with and transacts business with other healthcare providers in the MVHS network. Faxton-St. Luke's Healthcare (Healthcare), provides acute care. Senior Network Health, LLC (SNH), provides Medicaid managed care to seniors. St. Luke's Residential Healthcare Facility (SLH), provides long-term healthcare. Mohawk Valley Home Care, LLC (MVHC), provides nursing services. Visiting Nurse Association of Utica and Oneida County, Inc. (VNA), provides home health care services.

(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.

(e) Collective Bargaining Agreements

At December 31, 2016, the Medical Center had approximately 58% of its employees working under collective bargaining agreements. Certain agreements expire in September 2017. One agreement expires in June 2019.

(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 at date of purchase excluding amounts classified as assets limited as to use.

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Notes to Consolidated Financial Statements

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

(g) Investments and Assets Limited as to Use

Investments, assets limited as to use and pension plan assets are reported at fair value. FASB ASC No. 820, Fair Value Measurement (ASC 820), defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See note 12 for discussion on fair value measurements.

Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in the excess (deficiency) 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 (deficiency) of revenues over expenses since none of the investments are classified as trading securities.

The Medical Center 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 Medical Center's net assets.

(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, if purchased, or at fair value at the date of acquisition when acquired by gift. Property and equipment which is purchased under capital leases is stated at the lower of the present value of minimum lease payments at the beginning of the lease term or the fair market value at the inception of the lease.

Depreciation of property and equipment is calculated over the estimated useful life of each class of depreciable asset ranging from 2-40 years using the straight-line method. Property and equipment held under capital leases is amortized on the straight-line method over the lesser of the estimated useful life of the asset or the lease term. Amortization of equipment under capital leases is included in depreciation and amortization expense.

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Notes to Consolidated Financial Statements

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

(i) Property and Equipment, Continued

Gifts of long-lived assets, such as land, buildings or equipment are reported as unrestricted support and are excluded from the excess (deficiency) 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 obligations. At December 31, 2016 and 2015, the accumulated amortization on the debt issuance costs was approximately \$1,255,000 and \$1,167,000, respectively. Amortization expense amounted to approximately \$88,000 in 2016 and 2015, respectively, and is included in interest expense within the consolidated statements of operations and changes in net assets.

(k) Temporarily Restricted Net Assets

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

(l) Permanently Restricted Net Assets (Endowment Funds)

The Medical Center 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 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 \$528,864 and \$512,105 at December 31, 2016 and 2015, respectively, and are included in assets limited as to use in the consolidated balance sheets.

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Notes to Consolidated Financial Statements

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

(l) Permanently Restricted Net Assets (Endowment Funds)

The Medical Center 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.

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.

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.

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Notes to Consolidated Financial Statements

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

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

Interpretation of Relevant Law, Continued

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

Return Objectives, Strategies, Spending Policy and Investment Objectives

The Medical Center 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 Medical Center 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.

(m) Insurance Claims and Related Recoveries

The Medical Center 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. For the years ended December 31, 2016 and 2015, \$375,000 and \$708,000, respectively, has been recognized in these statements as a liability and a corresponding asset has been recorded to account for the anticipated recovery from the insurance company.

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Notes to Consolidated Financial Statements

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

(n) Net Patient Service Revenue and Patient Accounts Receivable

The Medical Center has agreements with third-party payors that provide for payments at amounts different from their established rates. Inpatient acute care services rendered are paid at prospectively determined rates per discharge in accordance with the Federal Prospective Payment System (PPS) for Medicare and generally at negotiated or otherwise pre-determined amounts under the provisions of the New York Health Care Reform Act (HCRA) and related legislation for all other payors. Reimbursement rates for Medicaid, Workers' Compensation, and No-Fault are determined on a prospective basis defined by HCRA that is based on clinical, diagnostic, and other factors. Inpatient nonacute and outpatient services are paid at various rates under different arrangements with third-party payors, commercial insurance carriers and health maintenance organizations. The basis for payment under these agreements includes prospectively determined per diem and per visit rates, discounts from established charges, fee schedules, and reasonable cost. Medicare outpatient services are paid under a prospective payment system whereby services are reimbursed on a predetermined amount for each outpatient procedure, subject to various mandated modifications.

Net patient service revenue is recognized in the period services are performed, is reported at estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations.

In addition, under HCRA, all Non-Medicare payors are required to make surcharge payments for the subsidization of indigent care and other health care initiatives. The percentage amounts of the surcharge varies by payor and applies to a broader array of health care services. Also, certain payors are required to make a covered lives payment to further fund the indigent care pools and other health care initiatives for inpatient services or through voluntary election to pay a covered lives assessment directly to the New York State Department of Health (DOH). The funds are distributed to the hospitals based on each hospital's level of bad debt in relation to all other hospitals. The Medical Center recorded distributions of approximately \$1,165,000 and \$1,260,000 for the years ended December 31, 2016 and 2015, respectively, from the indigent care pool.

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Notes to Consolidated Financial Statements

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

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

Both federal and New York State regulations provide for certain adjustments to current and prior years' payment rates and indigent care pool distributions based on industry-wide and hospital-specific data. The Medical Center has established estimates based on information presently available of the amounts due to or from Medicare, Medicaid, workers' compensation and no-fault payors and amounts due from the indigent care pool for such adjustments. Those adjustments which can be reasonably estimated have been provided for in the accompanying consolidated financial statements. The Medical Center has estimated the potential impact of such adjustments based on the most recent information available.

The Medical Center is required to prepare and file various reports of actual and allowable costs annually. Provisions have been made in the consolidated financial statements for prior and current years' estimated final settlements to the Medicare program and other third-party payors. The difference between the amount provided and the actual final settlement is recorded as an adjustment to net patient service revenue in the year the final settlement is determined. The Medical Center recorded adjustments for estimated settlements with third-party payors related to either settlement of prior year issues or changes in estimates resulting in an increase of approximately \$3,640,000 and \$987,000 in net patient service revenue for the years ended December 31, 2016 and 2015, respectively. The laws and regulations governing the reimbursement for healthcare services are extremely complex and subject to interpretation. Third-party payors retain the right to review and propose adjustments to amounts requested and recorded by the Medical Center. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near future. As of December 31, 2016, all cost reports through 2015 have been filed and Medicare cost reports through 2013 have been final settled. In accordance with FASB ASC Topic 954 any amounts recognized as bad debt reduces net patient service revenue in the period in which the bad debt is recognized.

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Notes to Consolidated Financial Statements

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

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

For the years ended December 31, 2016 and 2015, revenue from the Medicare and Medicaid programs accounted for approximately 61% and 63%, respectively, of the Medical Center's net patient service revenue. 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)	\$	133,032,718	76,830,529	7,770,222	217,633,469
		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)	\$	128,793,101	70,366,060	6,522,384	205,681,545

Additions to the allowance for doubtful accounts are made by means of the provision for bad debts. Accounts written off as uncollectible are deducted from the allowance and subsequent recoveries are added. The amount of the provision for doubtful accounts is based upon management's assessment of historical expected net collections, business and economic conditions, trends in federal and state governmental health care coverage and other collection indicators. Services rendered to individuals when payment is expected and ultimately not received are written off to the allowance for doubtful accounts.

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Notes to Consolidated Financial Statements

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

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

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

	<u>2016</u>	<u>2015</u>
Medicare	49%	42%
Medicaid	14%	18%
Self-pay	12%	13%
Insurance and all others	<u>25%</u>	<u>27%</u>
	<u>100%</u>	<u>100%</u>

The Medical Center's reserve for doubtful accounts was approximately 78% of self-pay accounts receivable at December 31, 2016 and 2015. The Medical Center has not changed its charity care policy during 2016 or 2015. The Medical Center does maintain an allowance for doubtful accounts of approximately 5% at December 31, 2016 and 2015 from third-party payors.

(o) Charity Care

The Medical Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. The Medical Center's policy is not to pursue collection of amounts determined to qualify as charity care; therefore, these amounts are not reported in net patient service revenue. During 2016 and 2015, costs incurred by the Medical Center in the provision of charity care were based on the ratio of the Medical Center's costs to gross charges and approximated \$340,000 and \$225,000 for the years ended December 31, 2016 and 2015, respectively.

(p) Contributions

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, which then are treated as cost. 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.

**ST. ELIZABETH MEDICAL CENTER
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Notes to Consolidated Financial Statements

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

(q) Medicare and Medicaid Electronic Health Record Incentive Program

The American Recovery and Reinvestment Act of 2009 included provisions for implementing health information technology under the Health Information Technology for Economic and Clinical Health Act (HITECH). The provisions were designed to increase the use of electronic health record (EHR) technology and to establish the requirements for a Medicare and Medicaid incentive payment program beginning in 2011 for eligible providers that adopt and meaningfully use certified EHR technology. Eligibility for annual Medicare incentive payments is dependent on providers demonstrating meaningful use of EHR technology in each period over a four-year period. Initial Medicaid payments are available to providers that adopt, implement or upgrade certified EHR technology. Providers must demonstrate meaningful use of such technology in subsequent years to qualify for additional Medicaid incentive payments.

The Medical Center uses a grant accounting model to recognize revenue for the Medicare and Medicaid EHR incentive payments. EHR incentive payments are recognized as revenue when it is reasonably assured that the meaningful use criteria for the required period of time have been achieved and the revenue will be received. The Medical Center recognized Medicare incentive payments totalling approximately \$1,131,000 for the year ended December 31, 2015 as other operating revenue in the accompanying consolidated statements of operations and changes in net assets. The Medical Center did not recognize any incentive payments in 2016. Income from Medicare incentive payments will be subject to retrospective adjustment upon final settlement of the applicable cost report from which payments are calculated. Additionally, the Medical Center's compliance with the meaningful use criteria is subject to audit by the federal and New York State governments.

(r) Excess (Deficiency) of Revenues Over Expenses

The consolidated statements of operations and changes in net assets include excess (deficiency) of revenues over expenses. Changes in unrestricted net assets which are excluded from excess (deficiency) of revenues over expenses, consistent with industry practice, include unrealized gains and losses on investments other than trading securities, permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets), and pension liability adjustments in accordance with FASB ASC Subtopic 715-30, Compensation-Retirement Benefits, Defined Benefit Plans - Pension.

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Notes to Consolidated Financial Statements

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

(s) Income Taxes

The Medical Center and the Foundation have been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code. As of December 31, 2016 and 2015, the Medical Center 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. The Medical Center does not anticipate the total unrecognized tax benefits will change in the next twelve months.

(t) Concentration of Credit Risk

The Medical Center 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 Medical Center's financial position.

(u) Reclassifications

Certain 2015 amounts have been reclassified to conform to the 2016 consolidated financial statement presentation.

(v) Subsequent Events

Subsequent events have been evaluated through May 22, 2017, which is the date consolidated financial statements were available to be issued.

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 the Medical Center 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.

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Notes to Consolidated Financial Statements

(2) Assets Limited as to Use and Investments

The composition of assets limited as to use and investments, at fair value, at December 31, 2016 and 2015 is set forth in the tables below:

	<u>2016</u>	<u>2015</u>
Under bond indenture agreements:		
Cash and cash equivalents	\$ -	62,320
Commercial paper	2,532,239	2,502,954
	<u>2,532,239</u>	<u>2,565,274</u>
Less current portion for bond interest fund	<u>109,549</u>	<u>63,909</u>
Debt service reserve fund	<u>2,422,690</u>	<u>2,501,365</u>
Restricted by donors:		
Cash and cash equivalents	565,744	585,191
Common stock	240,065	202,529
Domestic equity mutual funds	215,921	214,521
U.S. government and agency debt securities	<u>37,938</u>	<u>48,670</u>
Total restricted by donors	<u>1,059,668</u>	<u>1,050,911</u>
Held in escrow - cash and cash equivalents	<u>451,987</u>	<u>450,948</u>
Total assets limited as to use - long-term	<u>\$ 3,934,345</u>	<u>4,003,224</u>
Investments:		
Cash and cash equivalents	\$ 89,811	122,128
Certificates of deposit	140,135	199,601
Common stock	3,641,024	3,415,134
Exchange traded funds	402,870	341,339
Mutual funds	2,152,960	1,758,290
U.S. government and agency debt securities	25,353	581,091
Domestic corporate bonds	2,830,340	2,420,615
Municipal bonds	<u>408,371</u>	<u>553,788</u>
Total investments	<u>\$ 9,690,864</u>	<u>9,391,986</u>

**ST. ELIZABETH MEDICAL CENTER
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Notes to Consolidated Financial Statements

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

Investment income, excluding temporarily restricted, is as follows for the years ended December 31:

	<u>2016</u>	<u>2015</u>
Investment income:		
Interest and dividends, net of fees	\$ 326,893	345,620
Realized gain (loss) on sale of investments	<u>28,664</u>	<u>(3,332)</u>
	355,557	342,288
Change in net unrealized gains and losses and investments	<u>205,981</u>	<u>(261,537)</u>
	<u>\$ 561,538</u>	<u>80,751</u>

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

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Notes to Consolidated Financial Statements

(3) Property and Equipment

Property and equipment at December 31 are as follows:

	<u>2016</u>	<u>2015</u>
Land	\$ 768,605	768,605
Land improvements	6,014,329	5,964,923
Buildings	75,731,932	74,610,510
Fixed equipment	55,732,449	55,518,219
Moveable equipment	65,948,782	63,151,979
Property and equipment under capitalized leases	<u>3,717,904</u>	<u>3,717,904</u>
	207,914,001	203,732,140
Less accumulated depreciation and amortization	<u>144,244,469</u>	<u>133,840,376</u>
	63,669,532	69,891,764
Construction-in-progress	<u>935,408</u>	<u>723,331</u>
Property and equipment, net	<u>\$ 64,604,940</u>	<u>70,615,095</u>

Depreciation and amortization expense for 2016 and 2015 was approximately \$10,455,000 and \$10,606,000, respectively.

Construction-in-progress at December 31, 2016 consists of various infrastructure and information technology projects at the Medical Center.

(4) Short-Term Borrowings

The Medical Center maintains a line of credit with a lender which provides for borrowings up to \$6,000,000 at December 31, 2016 secured by the Medical Center's College of Nursing building and up to \$7,000,000 of eligible accounts receivable, as defined. Borrowings against this line of credit are payable on demand and bear interest at the lender's prime rate. There were no borrowings on the line as of December 31, 2016 and 2015.

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Notes to Consolidated Financial Statements

(5) Long-Term Debt and Lease Obligations

Long-term debt at December 31 is as follows:

	<u>2016</u>	<u>2015</u>
Series 1999-A Bonds (\$11,540,000 and \$12,080,000 principal amount less unamortized discount of \$64,686 and \$71,983 at December 31, 2016 and 2015, respectively)(a)	\$ 11,475,314	12,008,017
Series 1999-B Bonds (\$5,720,000 and \$6,220,000 principal amount less unamortized discount of \$73,236 and \$80,636 at December 31, 2016 and 2015, respectively) (b)	5,646,764	6,139,364
Series 2006-A Bonds (c)	8,000,000	8,000,000
Term loan (d)	632,062	844,807
Loans payable to Sisters (e)	<u>1,379,140</u>	<u>1,676,535</u>
	27,133,281	28,668,723
Less unamortized debt issuance costs	577,143	665,584
Less current portion	<u>1,619,248</u>	<u>1,550,550</u>
Long-term debt, net	<u>\$ 24,936,889</u>	<u>26,452,589</u>

- (a) In April 1999, the Medical Center obtained financing of \$15,000,000 through the placement of Oneida County Industrial Development Agency Civic Facility Revenue Bonds, Series 1999-A (the Series 1999-A Bonds). The Series 1999-A Bonds mature as follows: \$1,965,000 through December 2019 with interest payable semiannually at an annual rate of 5.750%; and an additional \$9,575,000 through December 2029 with interest payable semiannually at an annual rate of 5.875%. The Medical Center is required to make annual sinking fund payments to be used for mandatory redemption of the Series 1999-A Bonds ranging from \$620,000 to \$1,220,000 through December 2029. The Medical Center is also required to maintain certain covenants under the Bond agreement including minimum debt service coverage. The Medical Center is in compliance with its covenants at December 31, 2016 and 2015.

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Notes to Consolidated Financial Statements

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

- (b) In June 1999, the Medical Center obtained additional financing of \$15,000,000 through the placement of Oneida County Industrial Development Agency Civic Facility Revenue Bonds, Series 1999-B (the Series 1999-B Bonds). The Series 1999-B Bonds mature as follows: \$465,000 through December 2019 with interest payable semiannually at an annual rate of 6.00%; and an additional \$5,255,000 through December 2029 with interest payable semiannually at an annual rate of 6.00%. The Medical Center is required to make annual sinking fund payments to be used for mandatory redemption of the Series 1999-B Bonds ranging from \$190,000 to \$770,000 through December 2029. The Medical Center is also required to maintain certain covenants under the Bond agreement including minimum debt service coverage. The Medical Center is in compliance with its covenants at December 31, 2016 and 2015.
- (c) In June 2006, the Medical Center obtained additional financing of \$14,000,000 through the placement of Oneida County Industrial Development Agency Multi-Mode Variable Rate Civic Facility Revenue Bonds Series 2006-A (the Series 2006-A Bonds). The 2006-A Bonds were issued on a parity basis with the 1999-A and 1999-B bonds. The Series 2006-A bonds mature in June 2026. Interest is paid monthly based on the Securities Industry and Financial Markets Association Municipal Swap Index. The average rate was 0.77% and 0.09% at December 31, 2016 and 2015, respectively. The Medical Center is required to make sinking fund payments to provide for the redemption of the Series 2006-A Bonds ranging from \$740,000 to \$1,020,000 through 2026. Using both philanthropic funds raised through the Foundation and proceeds from the sale of a building, the Medical Center has made early sinking fund payments. As further security for the Bonds, the Medical Center has entered into a Reimbursement Agreement with HSBC Bank USA, pursuant to which the Bank has issued an irrevocable direct-pay letter of credit aggregating the principal amount. The letter of credit will expire on June 21, 2018. The Medical Center is also required to maintain certain covenants under the Bond agreement including minimum debt service coverage and minimum day's cash on hand. The Medical Center is in compliance with its covenants at December 31, 2016 and 2015.
- (d) In September 2014, the Medical Center obtained financing through a term note, for equipment, with a bank in the amount of \$1,100,000. The note is collateralized by the related equipment. The term note is payable in monthly installments including interest fixed at 3.95%. The term note matures in September 2019. The Medical Center is also required to maintain certain covenants including minimum debt service coverage. The Medical Center is in compliance with its covenants at December 31, 2016 and 2015.

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Notes to Consolidated Financial Statements

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

- (e) The Medical Center has loans outstanding with the Sisters of St. Francis of the Neumann Communities. All loans are interest free through 2022. Expected principal payments are approximately \$297,000 for 2017, \$350,000 for 2018 and \$183,000 for 2019 through terms of agreements. In the event that timely principal payments are not made, the Medical Center will be charged interest at 5%.

Under the indenture of Trust for the Series 1999-A, Series 1999-B, and Series 2006-A Bonds, the Medical Center is required to maintain certain levels of reserve accounts with the trustee. Amounts under this agreement have been classified as either current or noncurrent based upon the anticipated release date of such funds or contractual obligation. The Series 1999-A Bonds, Series 1999-B Bonds, and Series 2006-A Bonds, described in (a), (b) and (c), respectively, are secured by a mortgage lien on the property and equipment of the Medical Center, as a security interest in assets limited as to use.

Future annual principal payments on long-term debt are summarized as follows:

2017	\$ 1,619,248
2018	2,365,591
2019	2,397,360
2020	2,323,016
2021	2,433,016
Thereafter	<u>15,995,050</u>
	<u>\$ 27,133,281</u>

The Medical Center leases various buildings and equipment from vendors with renewable lease options. The leases were determined to be capital type leases, pursuant to generally accepted accounting principles. The leases have expiration dates from 2017 through 2022 and interest rates ranging from 1.63% - 10.72%.

The net book value of the equipment capitalized under lease agreements at December 31, 2016 and 2015 amounted to approximately \$1,424,000 and \$1,756,000, respectively. Total future principal and interest payments on these obligations amount to approximately \$1,170,000 of which approximately \$240,000 represents interest at December 31, 2016.

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Notes to Consolidated Financial Statements

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

Future minimum lease principal payments under noncancellable operating leases (with initial or remaining lease terms in excess of one year) and future minimum capital lease payments as of December 31, 2016 are:

	<u>Capital leases</u>	<u>Operating leases</u>
2017	\$ 343,825	748,850
2018	96,848	363,994
2019	107,633	273,504
2020	119,619	273,504
2021	132,940	273,504
Thereafter	<u>128,848</u>	<u>660,968</u>
Total minimum lease payments	929,713	\$ <u><u>2,594,324</u></u>
Less current portion	<u>343,825</u>	
	<u>\$ 585,888</u>	

Total rental expense for the years ended December 31, 2016 and 2015 for all operating leases was approximately \$988,000 and \$1,067,000, respectively.

(6) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets, consisting of cash and cash equivalents and short-term investments at December 31 are available for the following purposes:

	<u>2016</u>	<u>2015</u>
Capital improvements and other	\$ 209,178	237,225
Scholarships	128,751	110,310
Donor-restricted endowments	<u>131,632</u>	<u>74,234</u>
	<u>\$ 469,561</u>	<u>421,769</u>

Permanently restricted net assets, consisting of cash and cash equivalents and long-term investments at December 31 are available for the following purposes:

	<u>2016</u>	<u>2015</u>
Endowments for scholarships	\$ 417,442	406,184
Foundation endowment funds	<u>528,864</u>	<u>512,105</u>
	<u>\$ 946,306</u>	<u>918,289</u>

**ST. ELIZABETH MEDICAL CENTER
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Notes to Consolidated Financial Statements

(7) Pension Plans

The Medical Center has a noncontributory defined benefit plan which covers substantially all employees. Benefits are based on compensation and years of service. In 2003, the Medical Center applied for and received a favorable determination that its defined benefit plan is that of a nonselecting church plan under Section 410(d) of the Internal Revenue Code. Under status as a church plan, the Medical Center has elected to contribute the minimum amounts calculated as if the plan were subject to ERISA funding requirements.

Effective December 31, 2010, the Plan was amended to freeze benefit accruals for non-bargaining unit members. Effective January 1, 2012, the Plan was amended to freeze benefit accruals for the employees of one of the collective bargaining units. Effective April 1, 2013, the Plan was amended to freeze benefit accruals for the final collective bargaining unit.

The following tables present the changes in the Medical Center's benefit obligation and plan assets and funded status as of December 31:

	<u>2016</u>	<u>2015</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 106,440,336	108,603,253
Interest cost	5,556,747	5,314,583
Actuarial gain	(672,053)	(4,604,055)
Benefits paid	<u>(3,184,420)</u>	<u>(2,873,445)</u>
Benefit obligation at end of year	<u>\$ 108,140,610</u>	<u>106,440,336</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	55,999,375	58,088,618
Actual return on plan assets, net	5,271,936	(1,905,835)
Employer contributions	3,372,500	2,817,000
Benefits and administrative expenses paid	<u>(3,318,515)</u>	<u>(3,000,408)</u>
Fair value of plan assets at end of year	<u>61,325,296</u>	<u>55,999,375</u>
Funded status and accrued pension liability	<u>\$ (46,815,314)</u>	<u>(50,440,961)</u>

The Medical Center made a contribution to the Plan in the amount of \$257,000, which was in-transit as of December 31, 2015 and has been recorded as a reduction of the accrued pension liability.

**ST. ELIZABETH MEDICAL CENTER
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Notes to Consolidated Financial Statements

(7) Pension Plans. Continued

The Medical Center had \$31,346,378 and \$34,336,144 of actuarial net losses in unrestricted net assets as of December 31, 2016 and 2015, respectively, which have not yet been recognized as a component of net periodic pension cost. The estimated net loss expected to be amortized from unrestricted net assets into net periodic pension cost over the next fiscal year is \$1,774,038.

The components of net periodic pension cost for the years ended December 31:

	<u>2016</u>	<u>2015</u>
Administrative costs	\$ 127,000	86,000
Interest cost	5,556,747	5,314,583
Expected return on plan assets	(4,921,117)	(4,718,516)
Amortization of unrecognized net loss	<u>1,973,989</u>	<u>2,331,450</u>
Net periodic pension cost	<u>\$ 2,736,619</u>	<u>3,013,517</u>

The weighted average assumptions used to determine projected benefit obligations at December 31 are as follows:

	<u>2016</u>	<u>2015</u>
Discount rate	5.24%	5.31%
Expected long-term return on plan assets	7.50%	8.00%

The weighted average assumptions used to determine net periodic benefit cost for the years ended December 31 are as follows:

	<u>2016</u>	<u>2015</u>
Discount rate	5.31%	4.97%
Expected long-term return on plan assets	8.00%	8.00%

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Notes to Consolidated Financial Statements

(7) Pension Plans, Continued

The Medical Center's defined benefit plan's investment objectives are to emphasize total return specifically through long-term growth of capital while avoiding excessive risk, and to achieve a balanced return of current income and modest growth of principal. In order to achieve these objectives, the Medical Center has established the following asset allocation guidelines:

<u>Asset Class</u>	<u>Minimum</u>	<u>Maximum</u>	<u>Preferred</u>
Large cap equity	30%	50%	41%
Small cap equity	-	15%	5%
Mid cap equity	-	15%	6%
International equity	-	25%	16%
Fixed income	20%	80%	32%
Cash and cash equivalents	-	5%	-

The expected long-term rate of return on plan assets is reviewed annually, taking into consideration the asset allocation, historical returns on the types of assets held, and the current economic environment. Based on these factors, it is expected that the pension assets will earn an average of 7.50% per annum.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2016 or 2015.

Money market fund: Valued at amortized cost which approximates fair value.

Common stocks: Valued at the closing price reported on the active market on which the individual securities are traded.

Mutual funds: Valued at the daily closing price as reported by the fund. Mutual funds held by the Plan are open-end and closed-end mutual funds that are registered with the U.S. Securities and Exchange Commission. These funds are required to publish their daily net asset value (NAV) and to transact at that price. The mutual funds held by the Plan are deemed to be actively traded.

Common trust: Valued based on the NAV per unit, without further adjustment. NAV is based upon the fair value of the underlying investments.

Alternative investments: The investments consist of partnership and hedge funds. These securities are estimated using current information obtained from the general partner or investment manager for the respective funds. Investments in private equity partnerships are generally estimated using partner's capital balances, and their fair value of investments are generally estimated using the NAV.

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Notes to Consolidated Financial Statements

(7) Pension Plans. Continued

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the plan believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table presents by level, within the fair value hierarchy, the Plan's assets as of December 31:

Assets at fair value as of December 31, 2016					
		Level 1	Level 2	Level 3	Total
Money market fund	\$	-	943,520	-	943,520
Mutual funds		43,722,769	-	-	43,722,769
Common trust		-	4,886,311	-	4,886,311
Alternative investments		-	7,612,313	4,160,383	11,772,696
	\$	43,722,769	13,442,144	4,160,383	61,325,296
Assets at fair value as of December 31, 2015					
		Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$	2,000,000	-	-	2,000,000
Money market fund		-	478,559	-	478,559
Common stocks		893,767	-	-	893,767
Mutual funds		33,063,571	-	-	33,063,571
Common trust		-	5,000,000	-	5,000,000
Alternative investments		-	10,479,778	4,083,700	14,563,478
	\$	35,957,338	15,958,337	4,083,700	55,999,375

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Notes to Consolidated Financial Statements

(7) Pension Plans. Continued

The following table sets forth a summary of changes in the fair value of the Plan's level 3 assets for the years ended December 31:

	<u>Alternative investments</u>	
	<u>2016</u>	<u>2015</u>
Fair value at January 1	\$ 4,083,700	4,059,197
Unrealized gain, net	76,683	24,503
Fair value at December 31	\$ 4,160,383	4,083,700

The Medical Center expects to contribute \$3,948,000 to its defined benefit plan in 2017.

The following approximate benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	<u>Benefit payments</u>
2017	\$ 3,948,000
2018	4,275,000
2019	4,603,000
2020	4,899,000
2021	5,237,000
2022 - 2026	30,814,000

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Notes to Consolidated Financial Statements

(7) Pension Plans. Continued

The Medical Center also offers a 401(k) defined contribution retirement plan to substantially all of its non-union employees. Members of UFCW collective bargaining unit received contributions equal to other participants, however their plan assets are administered by representatives selected by UFCW. Effective March 3, 2013, members of the New York State Nurses Association were admitted to the plan in conjunction with the freezing of the defined benefit plan as discussed above. Each year participants may contribute up to 75% of eligible pre-tax compensation, as defined in the Plan, subject to maximum annual additions allowed by law. Employees that are not covered by UFCW collective bargaining unit are eligible to receive a safe harbor contribution equal to 3% of compensation. Further, for 2016 and 2015 non-union employees are eligible for a discretionary match on their contributions based on years of service as detailed below:

<u>Years of service</u>	<u>% of employer contribution (up to 4%)</u>
1 - 9	50% (or 2% in most cases)
10 - 19	75% (or 3% in most cases)
20+	100% (or 4% in most cases)

Contributions to this plan approximated \$4,141,000 and \$4,196,000 for the years ended December 31, 2016 and 2015, respectively.

The Medical Center also offers a 457(b) plan covering certain highly compensated employees. Participants may contribute amounts up to statutory limits on an annual basis. Under the plan the Medical Center contributes between 2% and 4% of earnings over the 401(k) annual maximum amount depending on the employee's years of service. The Medical Center's contributions to the plan approximated \$27,000 for the year ended December 31, 2016. There were no contributions made by the Medical Center for the year ended December 31, 2015. An asset and liability representing the total amount invested in the 457(b) plan totalling approximately \$560,000 and \$388,000 has been recorded as an other long-term asset and other long-term liability at December 31, 2016 and 2015, respectively.

(8) Contingencies

Professional Liability Insurance

Since 1986, the Medical Center's exposure for medical malpractice risk has been insured under a claims-made policy, which provides for \$1,000,000 coverage for each claim, not to exceed \$3,000,000 in aggregate annual coverage. In addition, the Medical Center has purchased excess insurance policies. If the claims-made policy is not renewed or replaced with equivalent insurance, claims based on occurrences during the claims-made coverage period but reported subsequent to such a change will be uninsured. The Medical Center has a right under its present policy to acquire extended coverage if it decides to terminate its claims-made coverage, nor does it expect any difficulty in renewing the policies as they become due.

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Notes to Consolidated Financial Statements

(8) Contingencies, Continued

Professional Liability Insurance, Continued

In the ordinary course of operations, the Medical Center is named as a defendant in various lawsuits, or events occur which could lead to litigation, claims, or assessments. Although the outcome of such matters cannot be predicted with certainty, management believes that insurance coverage is sufficient to cover current or potential claims, or that the final outcomes of such matters will not have a material adverse effect on the financial position of the Medical Center.

Workers' Compensation Insurance

Prior to January 1, 2012, the Medical Center obtained coverage for workers compensation insurance through the Healthcare Underwriters Mutual Risk Management Group (Group). The Medical Center is one of four members of the Group. The Group is an unincorporated association of healthcare providers in the upstate region of New York State and was organized under a trust agreement for the purpose of establishing a workers' compensation self-insurance group. The Group is governed by a board of trustees consisting of one trustee for each member. Members of the Trust are jointly and severally liable for Group activities and liabilities. The Group is no longer active and has been in the process of settling outstanding claims since December 31, 2011. At December 31, 2016 and 2015, the Medical Center has not been notified of any assessments resulting from participation in the Trust however has accrued approximately \$1,083,000 and \$587,000, respectively, in long-term portion of estimated insurance liabilities to cover any future assessments.

Since January 1, 2012, the Medical Center has been self-insured for these liabilities. Losses from asserted and unasserted workers compensation claims are accrued based on actuarial estimates that incorporate the Medical Center's past experience, the nature of each claim or incident, relevant trend factors, and estimated recoveries, if any, on unsettled claims. The Medical Center has accrued approximately \$3,996,000 and \$3,368,000 for the years ended December 31, 2016 and 2015, respectively. These accruals are part of estimated insurance liabilities on the consolidated balance sheet. In conjunction with the self-insurance program, the Medical Center is required to post a letter of credit with the State of New York Workers Compensation Board. This letter of credit totalled \$1,542,515 as of December 31, 2016 and 2015.

Health Insurance

Effective January 1, 2015, the Medical Center is self-insured for medical benefits. Based on claims experience, the Medical Center has accrued approximately \$762,000 and \$600,000, respectively, in current portion of estimate insurance liabilities as December 31, 2016 and 2015, respectively, to cover non-domestic claims to be paid after year end.

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Notes to Consolidated Financial Statements

(9) Affiliated Entities

Faxton-St. Luke's Healthcare

During 2016 and 2015, Healthcare advanced funds to the Medical Center to pay down the outstanding balance on their short-term borrowing arrangement. As of December 31, 2015, there was \$3,750,000 outstanding on this advance which is included within current portion of due to 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.

The Medical Center and Healthcare have contracted with each other to provide certain operational services, including shared employment, provider coverage, patient care, rental of office space, and other shared services. In 2016 and 2015, the Medical Center purchased services totalling approximately \$3,968,000 and \$2,115,000, respectively, from Healthcare and sold services totalling approximately \$2,609,000 and \$1,420,000, 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 contribution from affiliate for the year ended December 31, 2015.

Net receivables (payables) at December 31 from (to) affiliates for services performed and billing of other pass through expenses to and from the Medical Center are as follows:

	<u>2016</u>	<u>2015</u>
Due to affiliates:		
Healthcare (advance)	\$ -	(3,750,000)
Healthcare	(9,023,436)	(4,508,620)
Other	(13,913)	(64,457)
	<u>(9,037,349)</u>	<u>(8,323,077)</u>
Due from affiliates:		
Healthcare	7,085,001	3,139,916
Other	72,852	1,708
	<u>7,157,853</u>	<u>3,141,624</u>
	<u>\$ (1,879,496)</u>	<u>(5,181,453)</u>

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(9) Affiliated Entities, Continued

Mohawk Valley EC, LLC

The Medical Center, Healthcare 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. The Medical Center will maintain a 20% interest and sharing ratio in MVEC. The amount recognized as income based on the Medical Center's share is approximately \$219,000 and \$210,000 for the years ended December 31, 2016 and 2015, respectively.

(10) Statement of Cash Flow Supplemental Disclosures

The Medical Center's cash payments for interest and noncash investing and financing activities for the years ended December 31 were as follows:

	<u>2016</u>	<u>2015</u>
Cash paid during the year for interest	\$ 1,327,756	1,444,941
Property and equipment acquisitions included in accounts payable	692,570	656,967

(11) Functional Expenses

The Medical Center provides general health care services to residents of Utica, New York. Expenses related to providing these services are as follows:

	<u>2016</u>	<u>2015</u>
Healthcare services	\$ 195,587,790	188,272,676
General and administrative	<u>21,440,215</u>	<u>20,865,082</u>
	<u>\$ 217,028,005</u>	<u>209,137,758</u>

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(12) 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 Medical Center in estimating the fair value of its financial instruments:

Cash and cash equivalents: consists of money market funds that are valued at the net asset value (NAV) reported by the financial institution.

Certificates of deposit: consists of fixed-maturity certificates of deposit that are valued based on discounted future cash flows using the rates currently offered for deposits of similar remaining maturities.

Common stock, exchange traded funds and mutual funds: consists of actively traded equity securities and the Medical Center's investment in publicly traded mutual funds. Actively traded equity securities are valued on a continuous basis and mutual funds are valued at the closing price reported on an active market on which the individual securities are traded.

U.S. Government and agency debt securities, domestic corporate bonds, and municipal bonds: Consists of the Medical Center's directly owned securities and the Medical Center's investment in securities that are issued by the U.S. government or publicly owned government-sponsored enterprises. Securities owned directly by the Medical Center and securities issued by the U.S. government or publicly owned government-sponsored enterprises are valued based on quoted market prices or dealer quotes where available (Level 1 measurements). If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments or, if necessary, matrix pricing from a third party pricing vendor to determine fair value (Level 2 measurements). Matrix prices are based on quoted prices for securities with similar coupons, ratings, and maturities, rather than on specific bids and offers for the designated security.

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(12) Fair Value of Financial Instruments. Continued

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 Medical Center 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.

The Medical Center's financial assets recognized at fair value in the consolidated financial statements on a recurring basis consist of investments and assets limited as to use. The Medical Center's consolidated financial statements do not contain financial liabilities or nonfinancial assets and liabilities that are recognized at fair value on a recurring basis. In general, and where applicable, management used quoted prices in active markets for identical assets to determine fair value.

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Notes to Consolidated Financial Statements

(12) Fair Value of Financial Instruments, Continued

	Fair value measurements at December 31, 2016			
	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Assets:				
Assets limited as to use:				
Under bond indenture agreements:				
Commercial paper	\$ 2,532,239	2,532,239	-	-
Restricted by donors:				
Cash and cash equivalents	565,744	565,744	-	-
Exchange traded funds	240,065	240,065	-	-
Domestic equity mutual funds	215,921	215,921	-	-
U.S. government and agency debt securities	37,938	-	37,938	-
Total assets limited as to use	3,591,907	3,553,969	37,938	-
Investments:				
Cash and cash equivalents	89,811	89,811	-	-
Certificates of deposit	140,135	-	140,135	-
Common stock	3,641,024	3,641,024	-	-
Exchange traded funds	402,870	402,870	-	-
Mutual funds:				
Domestic equity	1,445,508	1,445,508	-	-
Internationally developed equity	474,082	474,082	-	-
Emerging markets equity	223,528	223,528	-	-
Real estate fund	9,842	9,842	-	-
Total mutual funds	2,152,960	2,152,960	-	-
U.S. government and agency debt securities	25,353	-	25,353	-
Domestic corporate bonds	2,830,340	-	2,830,340	-
Municipal bonds	408,371	-	408,371	-
Total investments	9,690,864	6,286,665	3,404,199	-
Total assets	\$ 13,282,771	9,840,634	3,442,137	-

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(12) Fair Value of Financial Instruments, Continued

	Fair value measurements at December 31, 2015			
	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Assets:				
Assets whose use is limited:				
Under bond indenture agreements:				
Cash and cash equivalents	\$ 62,320	62,320	-	-
Exchange traded funds	2,502,954	2,502,954	-	-
Restricted by donors:				
Cash and cash equivalents	585,191	585,191	-	-
Common stock	202,529	202,529	-	-
Domestic equity mutual funds	214,521	214,521	-	-
U.S. government and agency debt securities	48,670	-	48,670	-
Total assets limited as to use	<u>3,616,185</u>	<u>3,567,515</u>	<u>48,670</u>	<u>-</u>
Investments:				
Cash and cash equivalents	122,128	122,128	-	-
Certificates of deposit	199,601	-	199,601	-
Common stock	3,415,134	3,415,134	-	-
Exchange traded funds	341,339	341,339	-	-
Mutual funds:				
Domestic equity	1,241,380	1,241,380	-	-
Internationally developed equity	350,611	350,611	-	-
Emerging markets equity	137,509	137,509	-	-
Real estate fund	28,790	28,790	-	-
Total mutual funds	<u>1,758,290</u>	<u>1,758,290</u>	<u>-</u>	<u>-</u>
U.S. government and agency debt securities	581,091	-	581,091	-
Domestic corporate bonds	2,420,615	-	2,420,615	-
Municipal bonds	553,788	-	553,788	-
Total investments	<u>9,391,986</u>	<u>5,636,891</u>	<u>3,755,095</u>	<u>-</u>
Total assets	<u>\$ 13,008,171</u>	<u>9,204,406</u>	<u>3,803,765</u>	<u>-</u>

The Medical Center's accounting policy is to recognize transfers between levels of the fair value hierarchy on the date of the event or change in circumstances that caused the transfer. There were no significant transfers into or out of Level 1 or Level 2 for the year ended December 31, 2016.

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Notes to Consolidated Financial Statements

(12) Fair Value of Financial Instruments, Continued

Various assets and liabilities are not required to be measured at fair value on a recurring basis. The fair value of the Medical Center's long-term debt approximates carrying value at December 31, 2016 and 2015. These fair values are estimated using discounted cash flow analysis, based on the Medical Center's current incremental borrowing rate for similar types of borrowing arrangements. The carrying value of all remaining financial assets and liabilities not required to be measured at fair value on a recurring basis approximate fair value at December 31, 2016 and 2015.