Atlantic General Hospital Corporation

Audited Financial Statements

Years Ended June 30, 2017 and 2016

DIXON HUGHES GOODMAN LLP

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DIXON HUGHES GOODMAN LLP

Independent Auditors' Report

Board of Trustees
Atlantic General Hospital Corporation
Berlin, Maryland

We have audited the accompanying financial statements of Atlantic General Hospital Corporation (the Corporation), which comprise the balance sheets as of June 30, 2017 and 2016, and the related statements of operations, changes in net assets, and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Atlantic General Hospital Corporation as of June 30, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

DIXON HUGHES GOODMAN LLP

Emphasis of Matter – New Accounting Pronuncment

As discussed in Note 2 to the financial statements, during the year ended June 30 2017, the Corporation implemented new accounting guidance for accounting for debt issuance cost and reporting that requires retroactive adjustments to amounts previously reported as of and for the year ended June 30, 2016. Our opinion is not modified with respect to this matter

Dixon Hughes Goodman LLP

Gaithersburg, Maryland
October 25, 2017

Atlantic General Hospital Corporation
Balance Sheets
June 30, 2017 and 2016

	2017	As Adjusted 2016
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 12,064,308**	$ 13,604,571
Investments	**8,358,835**	7,051,195
Patient accounts receivable, less uncollectible accounts of $6,021,463 and $4,306,491 for 2017 and 2016, respectively	**10,080,616**	8,785,038
Supply inventory	**2,738,539**	2,623,947
Prepaid expenses and other current assets	**3,594,126**	1,958,973
Total current assets	**36,836,424**	34,023,724
Land, buildings and equipment	**49,179,310**	48,584,152
Other assets:		
Assets whose use is limited:		
Cash and cash equivalents restricted by donor	**84,906**	69,860
Cash and cash equivalents internally designated for a future endowment	**66,913**	74,994
Investments internally designated for a future endowment	**3,529,433**	3,173,300
Noncurrent pledges receivable	**1,370,969**	30,000
Long-term investments	**27,696**	27,696
Other noncurrent assets	**4,334,515**	4,838,398
Total other assets	**9,414,432**	8,214,248
Total assets	**$ 95,430,166**	$ 90,822,124

	2017	As Adjusted 2016
LIABILITIES AND NET ASSETS		
Current liabilities:		
Accounts payable and accrued expenses	**$ 5,856,689**	$ 4,640,810
Salaries, wages, and related items	**5,915,128**	5,421,737
Interest payable	**46,318**	46,301
Advances from third party payers	**934,662**	1,009,128
Current portion of long-term debt	**2,398,737**	2,338,086
Total current liabilities	**15,151,534**	13,456,062
Noncurrent liabilities:		
Long-term debt, less current portion and unamortized debt issuance costs	**19,280,261**	22,083,964
Swap contracts	**192,373**	154,682
Other liabilities	**6,310,486**	6,640,826
Total liabilities	**40,934,654**	42,335,534
Net assets:		
Unrestricted		
General	**47,966,166**	45,120,912
Board-designated	**3,596,346**	3,248,294
Temporarily restricted	**2,933,000**	117,384
Total net assets	**54,495,512**	48,486,590
Total liabilities and net assets	**$ 95,430,166**	$ 90,822,124

Atlantic General Hospital Corporation
Statements of Operations
Years Ended June 30, 2017 and 2016

	2017	As Adjusted 2016
Operating revenue:		
Patient service revenue, net of contractual allowances and discounts	**$ 119,312,454**	$ 115,478,446
Provision for bad debts	**(4,851,375)**	(3,990,597)
Net patient service revenue, less provision for bad debts	**114,461,079**	111,487,849
Other operating revenue	**3,280,562**	3,456,714
Total operating revenue	**117,741,641**	114,944,563
Operating expenses:		
Salaries	**52,285,730**	48,475,388
Employee benefits and other related expenses	**10,343,440**	10,506,395
Professional fees and contracted services	**10,969,217**	13,120,161
Supplies and other expense	**27,144,853**	25,277,220
Utilities	**1,540,276**	1,479,646
Maintenance and repairs	**5,907,319**	5,250,009
Insurance	**1,563,567**	1,495,849
Interest	**873,994**	841,909
Depreciation	**6,622,664**	6,440,605
Amortization	**17,248**	17,248
Total operating expenses	**117,268,308**	112,904,430
Income from operations	**473,333**	2,040,133
Other income:		
Investment income	**469,878**	183,350
Net unrealized gains (losses) on trading portfolio	**1,378,017**	(519,440)
Other	**872,078**	720,076
Total other income	**2,719,973**	383,986
Revenue and gains in excess of expenses	**$ 3,193,306**	$ 2,424,119

See accompanying notes.

Atlantic General Hospital Corporation
Statements of Change in Net Assets
Years Ended June 30, 2017 and 2016

	2017		
	Unrestricted	**Temporarily Restricted**	**Total**
Nets assets, beginning of year	**$ 48,369,206**	**$ 117,384**	**$ 48,486,590**
Revenue and gains in excess of expenses	**3,193,306**	**-**	**3,193,306**
Restricted contributions	**-**	**2,948,520**	**2,948,520**
Net assets released from restrictions used for operations	**-**	**(132,904)**	**(132,904)**
Change in net assets	**3,193,306**	**2,815,616**	**6,008,922**
Net assets, end of year	**$ 51,562,512**	**$ 2,933,000**	**$ 54,495,512**

	2016		
	Unrestricted	**Temporarily Restricted**	**Total**
Net assets, beginning of year	$ 45,945,087	$ 91,914	$ 46,037,001
Revenue and gains in excess of expenses	2,424,119	-	2,424,119
Restricted contributions	-	327,394	327,394
Net assets released from restrictions used for operations	-	(301,924)	(301,924)
Change in net assets	2,424,119	25,470	2,449,589
Net assets, end of year	$ 48,369,206	$ 117,384	$ 48,486,590

See accompanying notes.

	2017	As Adjusted 2016
Cash flows from operating activities and other gains:		
Change in net assets	**$ 6,008,922**	$ 2,449,589
Adjustments to reconcile change in net assets to net cash and cash equivalents provided by operating activities and other gains:		
Depreciation and amortization expense	**6,639,912**	6,457,853
Amortization of debt issuance costs	**32,318**	32,363
Provision for bad debts	**4,851,375**	3,990,597
Recognition of change in fair value of swap contract	**37,691**	183,462
Realized losses (gains) on sale of investments	**(84,255)**	79,263
Unrealized (gains) losses on trading portfolio	**(1,378,017)**	519,440
Loss (gain) on disposal of equipment	**42,919**	(9,821)
Changes in operating assets and liabilities:		
Decrease (increase) in:		
Patient accounts receivable, net	**(6,146,953)**	(2,919,339)
Supply inventory	**(114,592)**	(276,121)
Prepaid expenses and other current assets	**(1,635,153)**	223,227
Increase (decrease) in:		
Accounts payable and accrued expenses	**1,215,879**	(4,561,322)
Salaries, wages and related items	**493,391**	518,898
Interest payable	**17**	(1,719)
Third party advances	**(74,466)**	243,403
Other liabilities	**(1,184,674)**	88,442
Net cash and cash equivalents provided by operating activities and other gains	**8,704,314**	7,018,215
Cash flows from investing activities:		
Net purchase of trading investments	**(201,501)**	(309,689)
Net purchase of land, building, and equipment	**(7,093,256)**	(4,764,017)
Net cash and cash equivalents used in investing activities	**(7,294,757)**	(5,073,706)
Cash flows from financing activities:		
Payments on long-term debt	**(2,459,000)**	(2,125,922)
Proceeds from long-term debt	**-**	452,208
Payments for debt issuance costs	**(483,855)**	-
Net cash and cash equivalents used in financing activities	**(2,942,855)**	(1,673,714)
Net change in cash and cash equivalents	**(1,533,298)**	270,795
Cash and cash equivalents at beginning of year	**13,749,425**	13,478,630
Cash and cash equivalents at end of year	**$ 12,216,127**	$ 13,749,425
Supplemental cash flow disclosure:		
Interest paid	**$ 877,766**	$ 813,318
Supplemental disclosure of noncash investing and financing activities:		
Capital lease obligations issued for equipment	**$ 167,485**	$ 1,880,519

See accompanying notes.

Notes to Financial Statements

1. Organization and Nature of Activities

Atlantic General Hospital Corporation (the Corporation) is a non-stock, non-profit Maryland corporation organized on April 4, 1989, primarily for the purpose of constructing, owning and operating Atlantic General Hospital (the Hospital) in Worcester County, Maryland. On May 21, 1993, the Hospital commenced operations as a full-service acute care inpatient and outpatient health care facility. Admitting physicians are primarily practitioners in the local area. Prior to May 21, 1993, the Corporation's primary activity was the planning and development of the Hospital.

2. Summary of Significant Accounting Policies

Use of estimates

The preparation of 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Basis of presentation

The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America.

Board-designated unrestricted net assets

Board-designated unrestricted net assets represent assets whose use by the Hospital has been designated by the Board of Trustees for a particular purpose. The Board of Trustees may remove or modify the designations at any time. The board-designated assets were a result of the Hospital being named beneficiary in a portion of an estate pursuant to a will in 2001. Board-designated unrestricted net assets as of June 30, 2017 and 2016 are reported as cash and cash equivalents and investments internally designated for a future endowment in the accompanying balance sheets and are comprised of the following:

	2017	2016
Cash and cash equivalents	**$ 66,913**	$ 74,994
Investments	**3,529,433**	3,173,300
	$ 3,596,346	$ 3,248,294

The Board of Trustees has determined that any investment income on the future endowment will be internally designated by using a three year rolling average market value method, of which 3% annually can be used to fund physician practice development.

Temporarily restricted net assets

Temporarily restricted net assets are those whose use by the Hospital has been limited by donors or grantors to a specific time period or purpose. Temporarily restricted net assets as of June 30 are restricted for community and education programs and operations.

Donor-restricted gifts

Unconditional promises to give cash and other assets to the Corporation 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 on the earlier of the date the condition is satisfied or the gift is received. The gifts 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 statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted revenue and support in the accompanying financial statements.

Risk factors

The Corporation’s ability to maintain and/or increase future revenues could be adversely affected by: (1) the growth of managed care organizations promoting alternative methods for health care delivery and payment of services such as discounted fee-for-service networks and capitated fee arrangements (the rate setting process in the State of Maryland prohibits hospitals from entering into discounted fee arrangements, however, managed care contracts may provide for exclusive service arrangements); (2) proposed and/or future changes in the laws, rules, regulations, and policies relating to the definition, activities, and/or taxation of not-for-profit tax-exempt entities; (3) the outcome of the federal budget debate, and the enactment into law of all or any part of the current budget resolutions under consideration by Congress related to Medicare and Medicaid reimbursement methodology and/or further reductions in payments to hospitals and other health care providers; (4) the ultimate impact of the federal health care reform legislation (5) the future of Maryland’s certificate of need program, where future deregulation could result in the entrance of new competitors, or future additional regulation may eliminate the Hospital’s ability to expand or add new services; and (6) the future of the Maryland Health Services Cost Review Commission’s authority to regulate rates, where future changes could result in reductions to revenues since payers would be allowed to negotiate discounts not currently allowed.

The Joint Commission, a non-governmental privately owned entity, provides accreditation status to hospitals and other health care organizations in the United States of America. Such accreditation is based upon a number of requirements including undergoing periodic surveys conducted by Joint Commission personnel. Certain managed care payers require hospitals to have appropriate Joint Commission accreditation in order to participate in those programs. In addition, the Center for Medicare and Medicaid Services of the U.S. Department of Health and Human Services (CMS), the agency with oversight of the Medicare and Medicaid programs, provides “deemed status” for facilities having Joint Commission accreditation. In other words, by being Joint Commission accredited, facilities are “deemed” to be in compliance with the Medicare and Medicaid conditions of participation. Termination as a Medicare provider or exclusion from any or all of these programs/payers would have a materially negative impact on the future financial position, operating results and cash flows of the Hospital. The Hospital has been accredited by the Joint Commission through September 19, 2018.

The Medicare and Medicaid reimbursement programs represent a substantial portion of the Hospital’s revenues. The Corporation’s operations are subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse.

Cash and cash equivalents

The Corporation invests excess cash in financial instruments, which are converted into cash as needed to meet the Corporation’s obligations. Cash equivalents are highly liquid financial instruments with original maturities of less than three months or containing provisions for early redemption without penalty. The Corporation has cash holding in commercial banks that routinely exceed the Federal Deposit Insurance Corporation maximum insurance limit of $250,000.

The composition of cash and cash equivalents at June 30 is as follows:

	2017	2016
Cash and cash equivalents, classified as a current asset	**$ 12,064,308**	$ 13,604,571
Amounts restricted by donor	**84,906**	69,860
Amounts internally designated for a future endowment	**66,913**	74,994
Total cash and cash equivalents (as reported in the accompanying statements of cash flows)	**$ 12,216,127**	$ 13,749,425

Investments

Investments in equity securities with readily determinable fair values are measured at fair value in the accompanying balance sheets based on quoted market prices. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in other income, unless the income or loss is restricted by donor or law. Long-term investments represent charitable gift annuities recorded at the present value of the expected gift and investment in a captive insurance company.

The composition of investments at June 30 is as follows:

	2017	2016
Investments:		
Common stock	**$ 2,374,443**	$ 2,969,534
Mutual funds - equities	**8,153,443**	5,666,195
Mutual funds - fixed maturity	**1,388,078**	1,616,462
	11,915,964	10,252,191
Less investments internally designated for a future endowment	**3,529,433**	3,173,300
Less long-term investments	**27,696**	27,696
Undesignated investments	**$ 8,358,835**	$ 7,051,195

Investment income for the years ended June 30 consists of:

	2017	2016
Interest and dividends	**$ 385,623**	$ 262,613
Realized gains (losses)	**84,255**	(79,263)
	$ 469,878	$ 183,350

During 2008, the Corporation joined Maryland e-Care, LLC, a joint venture formed by six Maryland hospitals to provide remote monitoring technology with clinical decision support and physician/nursing services for their use in the intensive care units and other clinical areas within their respective hospitals. Currently, the Corporation maintains an 8.11% interest ($20,000) in this joint venture, which is reported using the cost method of accounting in the accompanying financial statements.

Fair value measurements

Current accounting standards define 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, and establish a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

Level 1: Quoted prices in active markets for identical assets or liabilities such as debt and equity securities, mutual funds, and money market accounts that are traded in an active market, and other cash equivalents. Level one investments include common stocks, equity mutual funds and money market funds that are traded in an active market.

Level 2: Observable inputs other than level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level two investments include corporate bonds, U.S. government obligations, and asset and mortgage backed securities. A third party pricing service may be used to determine the fair value of each of these investment securities. Because quoted prices in active markets for identical assets are not available, these prices are determined using observable market information such as quotes from less active markets and/or quoted prices of securities with similar characteristics.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. Level three investments can include limited liability partnerships and limited liability companies. The fair value for these investments are determined by applying the ownership percentage to the net asset value of the investment fund. Underlying investments of the funds can include hedge funds, real estate funds, mortgage backed securities, asset backed securities, and global equity fund of funds.

The following discussion describes the valuation methodologies used for financial assets measured at fair value. The techniques utilized in estimating the fair values are affected by the assumptions used, including discount rates, and estimates of the amount and timing of future cash flows. Care should be exercised in deriving conclusions about the Corporation’s business, its value, or financial position based on the fair value information of financial assets presented below.

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial asset, including estimates of the timing, amount of expected future cash flows, and the credit standing of the issuer. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair value may not be realized in the immediate settlement of the financial asset.

Fair values of common stock and mutual funds have been determined by the Corporation from observable market quotations, when available. Private placement securities and other equity securities where a public quotation is not available are valued by using broker quotes.

The fair value of the Corporation’s interest rate swap contracts are based on the proprietary model of a third party valuation specialist. The fair value takes into consideration the prevailing interest rate environment and the specific terms and conditions of the swap, and considers the credit risk of the Corporation and the counterparty. The method used to determine the fair value calculates the estimated future payments required by the swap and discounts these payments using an appropriate discount rate. The value represents the estimated exit price that the Corporation would pay to terminate the agreement.

The following table presents the Corporation's fair value hierarchy for assets and liabilities measured at fair value on a recurring basis as of June 30, 2017:

	Level 1	Level 2	Total Fair Value
Assets			
Mutual funds:			
Fixed maturity:			
High Yield Bond	$ 291,456	$ -	$ 291,456
Inflation-Protected Bond	176,951	-	176,951
Intermediate-term Bond	919,671	-	919,671
Equities:			
Bank Loan	49,771	-	49,771
Commodities Broad Basket	75,000	-	75,000
Diversified Emerging Markets	911,420	-	911,420
Equity Energy	74,496	-	74,496
Foreign Large Blend	824,465	-	824,465
Foreign Large Growth	1,056,915	-	1,056,915
Foreign Large Value	179,638	-	179,638
Foreign Small/Mid Growth	49,325	-	49,325
Large Blend	131,936	-	131,936
Large Growth	1,335,307	-	1,335,307
Large Value	1,246,110	-	1,246,110
Mid-Cap Growth	385,375	-	385,375
Mid-Cap Value	434,722	-	434,722
Option Writing	310,100	-	310,100
Real Estate	303,234	-	303,234
Small Blend	785,629	-	785,629
Common stocks:			
Basic Materials	62,768	-	62,768
Consumer Goods	90,779	-	90,779
Financial	627,814	728,540	1,356,354
Healthcare	426,643	-	426,643
Industrial Goods	84,955	-	84,955
Services	98,325	-	98,325
Technology	209,030	-	209,030
Utilities	25,589	-	25,589
Total	$ 11,167,424	$ 728,540	$ 11,895,964
Liabilities			
Interest rate swaps	$ -	$ (192,373)	$ (192,373)
	$ -	$ (192,373)	$ (192,373)

The following table presents the Corporation's fair value hierarchy for assets and liabilities measured at fair value on a recurring basis as of June 30, 2016:

	Level 1	Level 2	Total Fair Value
Assets			
Mutual funds:			
Fixed maturity:			
High Yield Bond	$ 325,816	$ -	$ 325,816
Inflation-Protected Bond	336,698	-	336,698
Intermediate-term Bond	953,947	-	953,947
Equities:			
Diversified Emerging Markets	520,679	-	520,679
Equity Energy	77,544	-	77,544
Foreign Large Blend	943,279	-	943,279
Foreign Large Growth	20,149	-	20,149
Large Blend	104,508	-	104,508
Large Growth	1,036,780	-	1,036,780
Large Value	1,049,384	-	1,049,384
Mid-Cap Growth	214,960	-	214,960
Mid-Cap Value	310,698	-	310,698
Multialternative	200,592	-	200,592
Real Estate	303,924	-	303,924
Small Blend	784,379	-	784,379
Small Value	99,319	-	99,319
Common stocks:			
Basic Materials	157,027	-	157,027
Consumer Goods	177,571	-	177,571
Financial	595,897	728,540	1,324,437
Healthcare	500,362	-	500,362
Industrial Goods	132,561	-	132,561
OTC Markets	14,612	-	14,612
Services	192,983	-	192,983
Technology	413,967	-	413,967
Utilities	36,015	-	36,015
Total	$ 9,503,651	$ 728,540	$ 10,232,191
Liabilities			
Interest rate swaps	$ -	$ (154,682)	$ (154,682)
	$ -	$ (154,682)	$ (152,682)

There were no significant transfers between fair value hierarchy levels for the years ended June 30, 2017 and 2016.

Supply inventory

Supply inventory is stated at the lower of cost or market, with cost determined principally by the first-in, first-out method.

Land, buildings, and equipment

Land, buildings, and equipment are carried at cost, including net interest on related borrowings capitalized during periods of construction. Donated items are recorded at fair value at the date of the donation. Capital leases are carried at the lower of the present value of their net minimum lease payments or the fair value of the leased properties at the inception of the lease less accumulated amortization. Expenditures that materially increase values, change capacities, or extend useful lives are capitalized. The carrying amounts of significant assets sold, retired, or otherwise disposed of and the related allowances for depreciation are eliminated from the accounts.

Depreciation, which includes amortization of equipment under capital leases, is recorded on the straight-line basis using the half-year convention over the estimated useful lives (or lease term if shorter) of 10 to 40 years for buildings and improvements and 5 to 10 years for equipment. Any acquisitions from July 1, 1999 and forward that are in excess of $100,000 are depreciated on the straight-line basis without using the half-year convention.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support, and are excluded from revenue and gains in excess of expenses and losses. 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.

Net patient service revenue and patient accounts receivable

Net patient service revenue is reported at estimated net realizable amounts from patients, third party payers, and others for services rendered.

The following table presents the detail of net patient service revenue:

	2017	2016
Gross charges for patient service	**$ 162,112,254**	$ 156,123,842
Deductions from gross charges		
Charity care	**2,569,515**	3,277,821
Contractual and other allowances	**40,230,285**	37,367,575
Net patient service revenue	**119,312,454**	115,478,446
Less: provision for bad debts	**4,851,375**	3,990,597
	$ 114,461,079	$ 111,487,849

Patient accounts receivable include Hospital and physician charges for accounts due from Medicare, Maryland Medical Assistance (Medicaid), CareFirst, commercial and managed care insurers, and self-paying patients. Deducted from patient accounts receivable are estimates of allowances for the excess of charges over the payments on patient accounts to be received from third party payers and uncollectible amounts related to self-paying patients. These estimates are calculated by management based on historical collection experience and analysis of financial class and age of groups of accounts receivable. The allowance for doubtful accounts compared to gross patient accounts receivable was 27% and 24% as of June 30, 2017 and 2016, respectively. The increase in the allowance for doubtful accounts in 2017 was due to a decline in collection experience.

Charity care

The Hospital provides care to patients who meet certain criteria under its financial assistance policy without charge or at amounts less than its established rates. Such patients are identified based on financial information obtained from the patient (or their guarantor) and subsequent analysis, and use of the federal poverty limits as guidelines. Since the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as a component of net patient service revenue or net patient accounts receivable.

Under current accounting standards, the Hospital is required to report the cost of providing charity care. The cost of charity care provided by the Hospital totaled $1,970,963 and $2,472,431 for the years ended June 30, 2017 and 2016, respectively. Rates charged by the Hospital for regulated services are determined based on an assessment of direct and indirect cost calculated pursuant to the methodology established by the Maryland Health Services Cost Review Commission (the Commission). For any charity services rendered by the Corporation, the cost of charity care is calculated by applying the estimated total cost-to-charge ratio for the Hospital services to the total amount of charges for services provided to patients benefitting from the charity care policies of the Hospital.

A Maryland hospital either receives payments from or makes payments to the Commission with respect to an Uncompensated Care Fund (UCC) established for rate-regulated hospitals in Maryland. The UCC is intended to provide Maryland hospitals with funds to support the provision of uncompensated care at those hospitals. The Hospital received net payments from the UCC of $512,458 and $1,201,716 for the years ended June 30 2017 and 2016, respectively.

Revenue and gains in excess of expenses

The statements of operations include revenue and gains in excess of expenses. Changes in unrestricted net assets, which are excluded from revenue and gains in excess of expenses, consistent with industry practice, include contributions of (and assets released from donor restrictions related to) long-lived assets and other items that are required by accounting principles generally accepted in the United States of America to be reported separately.

Maryland Health Services Cost Review Commission (the Commission)

Certain of the Hospital’s charges are subject to review and approval by the Commission. The Hospital has filed the required reports with the Commission and believes it is in compliance with the Commission’s requirements. The rate of reimbursement for principally all inpatient services and certain other services to patients under the Medicare and Medicaid programs prior to January 1, 2014 was based on a 36-year-old agreement between the Centers for Medicare and Medicaid Services (CMS) and the Commission. This agreement was based upon a waiver from the Medicare prospective payment system reimbursement principles granted to the State of Maryland under Section 1814(b) of the Social Security Act. In January 2014, CMS approved a new waiver to modernize Maryland’s unique all-payer rate-setting system for hospital services. The current waiver consists of a five-year performance period. Maryland hospitals will commit to achieving significant quality improvements including reductions in 30-day readmissions and hospital acquired conditions. Maryland will also limit the annual Medicare per capita hospital cost growth to a rate lower than the national annual per capita growth rate per year for 2015 to 2018. Under this model, Medicare is estimated to save at least $330 million over the next five years. Under the waiver, Maryland will shift virtually all of its hospital revenue over the five year performance period into global payment models. The Hospital elected to participate in this new global budget revenue program.

Patient service revenue is recorded at rates established by the Commission. The Hospital entered into a Global Budget Revenue (GBR) agreement with the Commission. The GBR agreement will renew each year for a one-year period unless it is cancelled by the Commission or by the Hospital. The GBR agreement provides the Hospital with a fixed revenue amount (CAP) under which it must operate each year. The CAP is adjusted annually for inflation, change in the Hospital’s payer mix and uncompensated care, change in population and quality incentives.

The Commission's rate-setting methodology for service centers that provide both inpatient and outpatient services or only outpatient services consists of establishing an acceptable unit rate for these centers within the applicable facility. The actual average unit charge for each service center is compared to the approved rate on a monthly basis. The rate variances, plus penalties where applicable, are applied to decrease (in the case of overcharges) or increase (in the case of undercharges) future approved rates on an annual basis. The timing of the Commission's rate adjustments for the Hospital could result in an increase or reduction due to the variances and penalties described above in a year subsequent to the year in which such items occur. The Hospital’s policy is to accrue revenue based on actual rates charged for services to patients in the year in which the services are performed and are billable.

Other operating revenue

The Hospital met compliance requirements to receive incentives to upgrade and implement certified electronic health record systems and become meaningful users under the provisions of the American Recovery and Reinvestment Act of 2009. The Corporation recognized $0 and $653,618 of meaningful use incentives for fiscal years ended June 30, 2017 and 2016, respectively, and reported this amount as other operating revenue in the accompanying statements of operations. The meaningful use incentive amounts received are subject to audit and future settlement by CMS.

Advertising and marketing costs

The Corporation expenses advertising and marketing costs as they are incurred. Advertising and marketing expenses were approximately $1,534,000 and $1,302,000 for the fiscal years ended June 30, 2017 and 2016, respectively, and are reported as supplies and other expense in the accompanying statements of operations. No advertising or marketing costs have been capitalized in the accompanying balance sheets.

Income taxes

The Corporation is exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code as a public charity. Federal tax law requires that the Corporation be operated in a manner consistent with its initial exemption application in order to maintain its exempt status. Management has analyzed the operations of the Corporation and concluded that it remains in compliance with the requirements for exemption.

The state in which the Corporation operates also provides general exemption from state income taxation for organizations that are exempt from federal income taxation. However, the Corporation is subject to both federal and state income taxation at corporate tax rates on its unrelated business income. Exemption from other state taxes, such as real and personal property taxes, is separately determined.

Current accounting standards define the threshold for recognizing uncertain income tax return positions in the financial statements as “more likely than not” that the position is sustainable, based on technical merits, and also provide guidance on the measurement, classification, and disclosure of tax return positions in the financial statements. Management believes there is no impact on the Corporation’s accompanying financial statements related to uncertain income tax provisions.

Recent accounting pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*, which provides a principles–based standard for recognizing revenue through a five-step process. The guidance in ASU 2014-09 is effective for the Corporation beginning July 1, 2018, with early adoption permitted. At the present time, management has not yet determined what the effects of adopting this ASU will be on its financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The amendments in this ASU revise the accounting related to lessee accounting. Under the new guidance, lessees will be required to recognize a lease liability and a right-of-use asset for all leases. The amendments in this ASU are effective for the Corporation beginning on July 1, 2019, with early adoption permitted, and should be applied through a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. Management has not yet determined what the effects of adopting this ASU will be on its financial statements.

In August 2016, FASB issued ASU 2016-14, *Not-For-Profit Entities (Topic 958), Presentation of Financial Statements of Not-for Profit Entities.* The amendments in this ASU make certain improvements that address many, but not all, of the identified issues about the current financial reporting for Not-for-Profit (NFP) entities. Under the new guidance, financial statements and noted disclosures requirements for NFP entities include the following:

1. Present on the face of the statement of financial position net assets with and without donor restrictions
2. Present on the statement of activities additional operation measures.
3. Continue to present on the face of the statement of cash flows the net amount for operating cash flows using either the direct or indirect method of reporting but no longer require the presentation or disclosure of the indirect method (reconciliation) if using the direct method.
4. Enhanced disclosures that provide quantitative and qualitative information about liquidity management.

The amendments in ASU 2016-14 are effective for the Corporation beginning on July 1, 2018, with early adoption permitted. Management has not yet determined what the effects of adopting this ASU will be on its consolidated financial statements.

Presentation of debt issuance costs

Effective July 1, 2017 the Corporation adopted ASU 2015-03, *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, which amends presentation guidance by requiring debt issuance costs related to a recognized debt obligation be presented in the balance sheet as a direct deduction from the carrying amount of that debt obligation, consistent with the presentation of debt discounts. ASU 2015-03 does not change the recognition and measurement requirements for debt issuance costs. Prior to the issuance of this ASU, an entity would present debt issuance costs as an asset. Accordingly, the amounts in the 2016 financial statements described below have been reclassified for comparative purposes to conform to the presentation in the 2017 financial statements. Such reclassifications did not impact the 2016 change in net assets.

	As of June 30, 2016		
	As Previously Reported	**Retrospective Adjustment**	**As Adjusted**
Balance sheets:			
Assets			
Debt issuance costs, net of accumulated amortization	$ 322,775	$ (322,775)	$ -
Total assets	91,144,899	(322,775)	90,822,124
Liabilities and members' equity			
Long–term debt, less current portion, net of unamortized debt issuance costs	$ 22,406,739	$ (322,775)	$ 22,083,964
Total liabilities and members' equity	91,144,889	(322,775)	90,822,124
Statement of operations:			
Amortization	$ 49,611	$ (32,363)	$ 17,248
Interest	809,546	32,363	841,909
Statement of cash flows:			
Depreciation and amortization	$ 6,490,216	$ (32,363)	$ 6,457,853
Amortization of debt issuance costs	-	32,363	32,363

3. Land, Buildings, and Equipment

Land, buildings, and equipment are comprised of the following as of June 30:

	2017	2016
Land, buildings, and improvements	**$ 46,838,265**	$ 45,640,801
Fixed equipment	**20,490,255**	19,641,983
Movable equipment	**37,143,417**	35,645,535
Capital lease equipment	**2,978,185**	2,242,205
	107,450,122	103,170,524
Less accumulated depreciation	**63,912,394**	57,340,792
	43,537,728	45,829,732
Construction in process	**5,641,582**	2,754,420
	$ 49,179,310	$ 48,584,152

Accumulated amortization on leased equipment totaling $1,399,997 and $1,038,505 is included in the balance of accumulated depreciation as of June 30, 2017 and 2016, respectively. Amortization expense associated with capital lease equipment was $355,257 and $159,534 for the years ended June 30, 2017 and 2016, and is included in the balance of depreciation expense in the accompanying statements of operations.

4. Pledges Receivable

Unconditional promises to give cash and others assets are recorded at fair value in the year that they are made net of allowance for uncollectible accounts and discounted to their present value. As of June 30, 2017, promises to give that are expected to be received in less than one year total $1,162,554, one to five years total $1,396,824, and more than five years total $75,355. The promises to give in future years are discounted in the amount of $101,210 at a rate of 2.8% at June 30, 2017. Conditional promises to give are recorded at the time they become unconditional and are reported in prepaid expenses and other current assets and noncurrent pledges receivable of the accompanying balance sheet.

5. Non-Current Liabilities

Long-term debt as of June 30 is comprised of the following:

	2017	2016
$9,978,700 Berlin, Maryland Hospital Refunding Revenue Bonds (Atlantic General Hospital Facility), Series 2001; interest is determined by taking the weighted BMA index plus 1.65% per annum; principal and interest payments are due monthly commencing December 20, 2001 through December 1, 2026.	**$ 5,630,963**	$ 6,054,083
$5,000,000 Berlin, Maryland Hospital Revenue Bond (Atlantic General Hospital Facility), Series 2002; interest is currently the weighted BMA index plus 1.65% per annum, with an option to change quarterly to 65% of the prime rate; payable in monthly principal and interest installments of $11,111 commencing October 1, 2008; matures September 1, 2027.	**1,366,667**	1,500,000

$2,200,000 Series A Bond payable to M&T Bank with a fixed interest rate of 5.19%, which was based on the 10 year point on the S43 MUNI Swaps Curve + 2.44% until June 30, 2020. Beginning July 1, 2020 to and including its maturity or prepayment in full, the loan will bear interest at a rate equal to the Weighted SIFMA Calculation + 1.65%. Principal and interest payments are due monthly commencing August 1, 2010 through July 1, 2025.	**1,185,556**	1,332,222
$2,600,000 Series B Bond payable to M&T Bank with a fixed interest rate of 5.08% through June 30, 2020 and a variable rate equal to the weighted SIFMA Calculation + 1.65%. Principal and interest payments are due monthly commencing January 1, 2011 through July 1, 2025.	**1,449,425**	1,628,736
$7,400,000 Series C Bond payable to M&T Bank with a variable interest rate equal to the Weighted SIFMA Calculation through December 31, 2012 and a fixed rate calculated as the 7-year point on the S43 Muni Swaps Curve + 2.44% from January 1, 2013 through June 30, 2020; thereafter, a variable rate equal to the SIFMA rate. Principal and interest payments are due monthly commencing August 1, 2011 through July 1, 2025. This loan converted to a fixed rate of 3.48% on January 1, 2013.	**4,062,935**	4,617,648
$4,154,850 loan payable to M&T Bank with an interest rate of M&T 10 year swap rate; payable in monthly principal installments of $17,312 maturing on April 9, 2023. The Corporation entered into an interest rate swap that effectively fixes the interest rate at 4.02%. The interest rate swap expires April 9, 2023.	**3,306,560**	3,514,302
$1,750,000 loan payable from Bank of Ocean City, secured by real property, with interest of 3.99%; payable in monthly principal and interest installments of $10,599 commencing May 11, 2014; due April 11, 2034.	**1,557,060**	1,637,541
$1,950,000 loan payable from Bank of Ocean City, secured by real property, interest of 3.99%; payable in monthly principal and interest installments of $11,810 commencing June 23, 2014; due May 23, 2034.	**965,787**	1,087,487
$680,000 loan payable from Bank of Ocean City, secured by real property, with interest of 3.99%; payable in monthly principal and interest installments of $4,118 commencing July 30, 2015; due June 30, 2035.	**633,777**	652,412
$452,208 loan payable from Bethesda Leasing, LLC for tenant improvements, with interest of 5.00%; payable in monthly principal and interest installments of $4,796 commencing April 1, 2016; due March 1, 2026.	**407,228**	446,435
$633,753 loans payable for financing of Allscripts Perks Inpatient Clinical System with fixed interest rate of 2.00% secured by the associated equipment. Principal and interest payments are due monthly beginning October 1, 2011 through July 1, 2019.	**83,229**	286,693

$208,522 loan payable for financing of Allscripts Sunrise Mobile MD Software and Sunrise EPSi Software with a fixed interest rate of 3.99% secured by the associated equipment. Principal and interest payments are due annually beginning December 31, 2015 through December 31, 2023.	**190,260**	190,260
Capital leases payable, with interest ranging from 3.54% to 5.44%, secured by selected equipment.	**1,613,863**	1,797,006
Total long-term debt	**22,453,310**	24,744,825
Less – net unamortized debt issuance costs.	**(774,312)**	(322,775)
Less – current portion	**(2,398,737)**	(2,338,086)
	$ 19,280,261	$ 22,083,964

Maturities of long-term debt, including capital leases, for years ending June 30 are as follows:

	2018	2019	2020	2021	2022	After 2022
Future minimum lease payments	$ 462,221	$ 468,395	$ 472,869	$ 335,403	$ 35,528	$ 6,044
Less interest	77,429	54,980	26,337	6,925	899	27
	384,792	413,415	446,532	328,478	34,629	6,017
Notes/loans payable	566,145	474,366	477,636	487,660	505,929	4,632,165
Bonds payable	1,436,891	1,489,481	1,519,225	1,550,829	1,584,411	6,114,709
	$ 2,387,828	$ 2,377,262	$ 2,443,393	$ 2,366,967	$ 2,124,969	$10,752,891

2001 Series refunding revenue bond

On December 20, 2001, pursuant to a loan and financing agreement (the Financing Agreement) between the Corporation, the Mayor and Council of Berlin, Maryland (the Issuer), and M&T Bank (formerly Wilmington Trust Company (the Lender), the Town of Berlin issued a $9,978,700 Hospital Refunding Revenue Bond (Atlantic General Hospital Facility), 2001 Series (the 2001 Bond) dated December 1, 2001, to refund the then-existing 1992 Series Revenue Bonds (the Prior Bonds), provide for the payment of accrued and unpaid interest and premium on the Prior Bonds, and provide for the payment of a portion of the costs of issuance of the 2001 Bond. The Financing Agreement requires monthly payments by the Corporation sufficient to meet the principal and interest requirements of the 2001 Bond through its maturity on December 1, 2026. There is no trustee for the 2001 Bond; the Corporation makes all payments of principal and interest on the 2001 Bond directly to the Lender.

In accordance with the terms of the Financing Agreement, the Corporation has entered into various covenants imposing restrictions on the transfer or disposition of property and incurrence of additional indebtedness, restrictions on the acquisition of real property and equipment beyond specified limits, the achievement of certain pre-established financial indicators, monthly reporting of financial information, and the granting of a security interest in all property and unrestricted revenues of the Corporation.

The Corporation's obligations are evidenced by the Financing Agreement, a deed of trust, and other documents executed and delivered for the purpose of securing the loan. The Corporation has assigned a continuing security interest in its receipts, equipment collateral, personal property, any judgments or awards, any insurance settlements, all rents, and all right and title and interest in property leases and subleases. Upon the occurrence of an event of default under the Financing Agreement, the interest on the outstanding principal balance will be increased 2% per annum in excess of the tax-exempt rate or the taxable rate, as applicable, until such time that the default is cured.

The 2001 Bond is subject to redemption prior to the scheduled December 1, 2026 maturity in different ways:

1. Mandatory redemption in whole but not in part, at the sole option of the Lender, at a redemption price equal to the unpaid principal amount together with unpaid interest through redemption. Redemption without premium or penalty is available on December 1, 2021. The lender must give 180 days' notice for mandatory redemption and they can only do so in the fiscal year 2022.

2. Special mandatory redemption given certain circumstances, in whole or in part as the case may be, at redemption price equal to the principal amount together with all unpaid interest through redemption plus applicable penalties.

2002 Series revenue bond

On September 18, 2002, pursuant to a loan and financing agreement (Second Financing) between the Corporation, the Issuer, and the Lender, the Town of Berlin issued a qualified tax-exempt $5,000,000 Berlin, Maryland Corporation Revenue Bond (Atlantic General Hospital Facility), 2002 Series (the 2002 Bond) dated September 1, 2002. Its proceeds were used to finance a portion of the cost of the acquisition, construction and equipping of an expansion of the existing hospital facility for additional emergency, surgical, and outpatient service capacity. The Second Financing requires monthly payments by the Corporation directly to the Lender sufficient to meet the principal and interest requirements of the 2002 Bond through its maturity on September 1, 2027. Initially, interest was paid at 65% of the prime rate; however, from January 1, 2003 until such time that the Corporation enters into a swap arrangement, the Corporation has the option to direct a change in the interest rate between the initial rate and the weighted BMA calculation plus 165 basis points on any quarterly conversion date.

The Bond is subject to redemption prior to the September 18, 2027 maturity in different ways:

1. Mandatory redemption in whole but not in part, at the sole option of the Lender, at a redemption price equal to the unpaid principal amount together with unpaid interest through redemption. Redemption without premium or penalty is available on September 1, 2022.

2. Special mandatory redemption given certain circumstances, in whole or in part as the case may be, at redemption price equal to the principal amount together with all unpaid interest through redemption plus applicable penalties.

The 2002 Bond is collateralized by the pledged receipts, property, and revenues of the Hospital. The 2002 Bond also imposes certain restrictive covenants on the Corporation, for which noncompliance could cause accelerated demand for payment.

In July 2009, the Corporation received written notification from the Lender agreeing to waive the put options for the 2001 Series Refunding Revenue Bond and 2002 Series Revenue Bond.

2008 Commercial mortgage loan

During 2008, the Corporation obtained a $5.172 million commercial mortgage loan from a commercial bank for the purposes of paying pre-existing debt and completing construction on a medical office building. The loan is collateralized by a mortgage lien against the Hospital property as well as certain units in the medical office building. During 2013, the outstanding balance of $4,154,850 was refinanced over a 20-year term, maturing April 11, 2023. At that time the Corporation entered into a 10-year interest rate swap agreement effectively fixing the interest rate at 4.02%.

Swap agreements

In connection with the issuance of the 2008 term loan and commercial loan, the Corporation entered into an ISDA Master Agreement with the Lender to reduce the Corporation's exposure to future variable cash flows caused by fluctuations in the interest rate (the 2008 Swap Agreement). Under the terms of the 2008 Swap Agreement, the Corporation paid a fixed rate of 5.30% and 5.15% on the outstanding principal balance of the 2008 Commercial mortgage loan and the 2008 term loan, respectively, during the period April 2008 to March 2013. The 2008 Swap Agreement expired on April 9, 2013. With the refinancing of the 2008 term loan during 2013, the Corporation entered into an interest rate swap agreement with the Lender expiring April 2023 (the 2013 Swap Agreement). Under the 2013 Swap Agreement, the fixed rate is 1.77% and the variable rate is the 30-day LIBOR rate. In connection with the issuance of new tax-exempt financing subsequent to June 30, 2017 (Note 11), the Corporation entered into forward contracts to lock fixed interest rates ranging from 1.46% to 1.82% on a notional amount of approximately $30 million.

The fair value of the swap agreements as of June 30, 2017 and 2016 (as determined in consultation with investment hedging consultants), based on the present value of cash flow differences over the life of the swap agreement between the interest rate calculated on the swap agreements at inception and rates available on similar swap agreements as of June 30 is ($192,373) and ($154,682), respectively. Payments made to the counterparty to the Swap Agreement were $37,691 and $183,462 for the years ended June 30, 2017 and 2016, respectively. The Corporation is exposed to credit loss in the event of nonperformance by the counterparty on the swap agreements, but does not anticipate nonperformance by the counterparty.

2010 Series revenue bonds

Pursuant to a Commitment Letter dated June 21, 2010, M&T Bank approved financing in the aggregate principal amount not to exceed $12,200,000 for the Corporation by the issuance of three series of bonds (Series A, Series B and Series C), collectively, the 2010 Series Revenue Bonds issued by the Mayor and Council of Berlin (the Issuer). On June 29, 2010, pursuant to a loan and financing agreement (the 2010 Loan and Financing Agreement) between the Corporation, the Issuer, and M&T Bank (the Lender), the Issuer issued the Hospital Revenue Bonds (Atlantic General Hospital Facility) 2010 Series A in the amount of $2,200,000. The Series B Bond and Series C Bond were issued on December 13, 2010 in the amounts of $2,600,000 and $7,400,000, respectively. Proceeds of each Series of the Bonds have been used to finance a portion of cost of the acquisition, installation and improvement of various facilities, equipment and furnishings at the main Hospital campus, equipment at the billing office, and equipment at the Atlantic Health Center.

The financing requires monthly payments by the Corporation directly to the Lender sufficient to meet the principal and interest requirements of the 2010 Bonds through their maturity on July 1, 2025. Repayment began on August 1, 2010 for Series A Bond and February 1, 2011 for Series B Bond and August 1, 2011 for the Series C Bond.

The Series A and B Bonds bear interest from the date of their issuance to and including June 30, 2020 at a fixed rate which is equal to the rate of 10-year point on the S43 MUNI Swaps Curve plus 244 basis points. For the Series A Bond and B Bond, the interest rate is 5.19% and 5.08%, respectively. Beginning July 1, 2020 to and including their maturity or repayment in full, the Bonds shall bear interest at a rate which is equal to the Weighted SIFMA Calculation plus 165 basis points. The Series C Bond incurred interest from the date of its issuance to and including December 31, 2012 at a variable rate which was equal to the Weighted SIFMA Calculation plus 165 basis points. From and after January 1, 2013 to and including June 30, 2020, the Series C Bond bears interest at the fixed rate of 7-year point on the S43 MUNI Swaps Curve plus 244 basis points, which was 3.48%. From and after July 1, 2020 to and including its maturity or repayment in full, the Series C Bond shall bear interest at a variable rate which is equal to the Weighted SIFMA Calculation plus 165 basis points. The 2010 Loan and Financing Agreement precludes any additional interest rate swaps or other interest rate hedging arrangement with respect to any Series of the Bonds.

The Bonds are subject to redemption prior to the July 1, 2025 maturity in different ways:

1. Optional redemption in whole or in part, at the direction of the Corporation and if approved by the Issuer, with partial redemptions applied to unpaid interest, premiums, and then principal installments in the inverse order of the installment payment dates:

Redemption Period	Redemption Price (on principal)
July 1, 2017 – June 30, 2018	102%
July 1, 2018 – June 30, 2019	101%
July 1, 2019 – June 30, 2020 and thereafter	100%

2. Mandatory redemption prior to maturity from Receipts Requiring Mandatory Redemption.

3. Mandatory redemption prior to maturity at the option of the Holder.

4. Mandatory redemption prior to maturity upon the occurrence of a Determination of Taxability.

The 2010 Bonds are collateralized by the pledged receipts, property, and the revenues of the Hospital. The 2010 Bonds also impose certain restrictive covenants on the Corporation, for which noncompliance could cause accelerated demand for payment.

The Bonds are also subject to a put option which can be exercised with at least 270 days prior written notice to the Borrower, whereby the Lender at its sole option may put any one or more of the Bonds to the Borrower as of July 1, 2020, and be paid the unpaid principal balance of such Bond or Bonds selected for such put option, plus interest accrued thereon to such put date.

2015 Commercial Mortgage Loan

During 2015, the Corporation obtained a $680,000 commercial mortgage from a commercial bank for the purposes of purchasing a condominium unit in the medical office building. The loan is collateralized by a mortgage lien against the condominium. Principal and interest payments of $4,118 are made monthly and the loan matures on June 30, 2035.

6. Professional Liability Insurance Coverage

The Corporation is presently exposed to asserted and unasserted potential legal claims encountered in the ordinary course of business. In the opinion of management, the resolution of such matters will not have a material adverse impact on the Corporation's June 30, 2017 financial position or the results of operations for the year then ended.

Prior to 2005, the Corporation had claims-made professional liability insurance through a commercial insurance carrier covering claims arising from the performance of professional services and brought against the Corporation while the policy was in force. Insurable limits under this policy were $1 million per claim and $3 million annual aggregate shared limit basis. In addition, the Corporation maintained an umbrella policy of $15,000,000 per occurrence and aggregate.

During 2005, the Hospital, in conjunction with eight other Maryland hospitals, (Shareholders) formed Freestate Healthcare Insurance Company, Ltd. (Captive), a Cayman Islands company, to provide claims-made professional and general liability coverage for the risks of the Shareholders, their controlled affiliates, and their respective employees. Each of the Shareholders is a Maryland nonprofit corporation, exempt from federal income taxation under Section 501(a) of the Internal Revenue Code of 1986, as amended (Code or IRC), as an organization described in Section 501(c)(3) of the Code. The Shareholders are not affiliated with one another through common ownership or control. As of June 30, 2017, the Captive had five Shareholders.

The Captive provides primary coverage to the Shareholders and their affiliates with limits of liability of $1,000,000 for each and every claim (Retained Layer), and provides an excess policy with various limits of liability which is fully reinsured through commercial carriers. The Corporation has $10,000,000 of additional reinsurance in the aggregate through such reinsurance arrangements. The estimated unpaid loss liability reserved by the captive for the Hospital was $4,287,692 and $4,774,327 at June 30, 2017 and 2016, respectively. In accordance with current accounting standards, the June 30, 2017 and 2016 unpaid loss liability is recorded as a noncurrent liability, and the related insurance recovery was reported as a noncurrent asset, in the accompanying balance sheets. An estimated liability for incurred but not reported professional liability claims has also been recorded in the amount of approximately $2,023,000 and $1,866,000 as a noncurrent liability as of June 30,2017 and 2016, respectively.

Premiums are calculated by an actuary under a retrospectively rated policy and are based primarily on the experience of the Shareholders. The total premium is allocated to each of the Shareholders based on their experience. Premiums for the Corporation’s professional and general liability insurance of approximately $1,077,000 and $1,038,000 were charged to operations during fiscal years 2017 and 2016. Retrospective premium assessments and credits are calculated based on the aggregate experience of all named insureds under the policy. Each named insured’s assessment or credit is based on the percentage of their actual exposure to the actual exposure of all named insureds. In management's opinion, the assets of the Captive are sufficient to meet its obligations as of June 30, 2017. If the financial condition of the Captive were to materially deteriorate in the future, and the Captive was unable to pay its claim obligations, the responsibility to pay those claims would return to the member hospitals.

7. Commitments

Employment agreements

The Corporation has entered into various employee agreements with certain physicians whereby the Corporation has agreed to pay reasonable expenses of the physicians’ practices in addition to compensation for services rendered. These agreements are generally for a period of two years.

Lease agreements

The Corporation has entered into various lease agreements for equipment and facilities. Most lease arrangements contain a renewal option. Total rent expense for the years ended June 30, 2017 and 2016 was approximately $1,258,000 and $1,140,000 respectively. Future minimum payments on noncancelable office and equipment leases, with initial or remaining terms of one year or more, for years ending June 30 are as follows:

2018	$ 1,161,449
2019	1,091,889
2020	952,092
2021	818,942
2022	467,406
Thereafter	598,895
	$ 5,090,673

Retirement plans

The Corporation sponsors a 403(b) retirement covering substantially all employees of the Corporation. Participants may elect to contribute a percentage of their pretax annual compensation, as defined by the Plan, not to exceed the maximum allowable contributions under the Internal Revenue Code (IRC). The Corporation matches 50% of the first 5% of participants' elective deferrals and participants become 100% vested in employer contributions after three years of continuous service. Plan expenses were approximately $635,000 and $630,000 for the years ended June 30, 2017 and 2016, respectively.

Effective January 31, 2003, the Corporation entered into an agreement to sponsor a Section 457 deferred compensation plan. All contributions to the Section 457 plan are from participating employees; however, all assets of the Section 457 plan are the sole property of the Corporation and are fully subject to claims by the Corporation's general creditors.

Self-insured plans

Effective May 1, 2002, the Corporation joined the Maryland Hospital Association (MHA) Workers' Compensation Self-Insurance Group to self-insure for worker's compensation benefits. The annual premium for worker's compensation is calculated based on the Corporation's payroll estimate and MHA rates per payroll classification. The MHA rates are determined based on past experience. Amounts charged to operations for workers' compensation expense were $468,738 and $414,062 for the years ended June 30, 2017 and 2016, respectively.

In lieu of paying unemployment tax premiums to the State of Maryland, the Corporation secured a letter of credit with M&T Bank, effective May 21, 2004. As of June 30, 2017 the letter of credit was in the amount of $410,020. Additionally, the Corporation paid actual Maryland unemployment claims in the amount of $56,132 and $69,657 for the years ended June 30, 2017 and 2016, respectively.

The Corporation maintains an agreement with a third party to administer a self-insured health plan that benefits Hospital associates and their dependents. On behalf of participating associates, the Corporation pays the cost of health claims and an administration fee for each subscriber associate. The participating associates share in the cost by remitting a pre-established premium through payroll deductions. Additionally, the Hospital obtains stop loss insurance to cover possible claims in excess of expected claims. The stop loss insurance agreements are annual agreements, subject to annual renewals. The Corporation submits a claim for reimbursement of stop loss insurance when claims exceed a pre-established ceiling. The Corporation's net health benefit expense for the fiscal years ended June 30, 2017 and 2016, net of premiums received from associates during the fiscal years, ($1,051,963 and $905,560 respectively), was $5,460,084 and $5,898,830, respectively.

The Corporation maintains an agreement with a third party to coordinate the administration of dental health benefits to Hospital employees and their dependents. This is an annual agreement, subject to annual renewals. On behalf of participating employees, the Hospital pays the cost of claims and a fee for each subscriber employee, and the participating employees remit a portion of the Corporation's cost through a pre-established schedule of payroll deductions.

Allscripts Perks inpatient clinical system

In September 2011, the Corporation entered into a seven-year agreement for an electronic medical records system and support services for approximately $8.8 million. As of June 30, 2017, approximately $7.6 million has been paid. In December, 2014, the Corporation entered into a nine-year agreement for additional system and support services for approximately $5.8 million. The 2014 agreement also extended the support and remote hosting services of the 2011 agreement (to begin upon expiration of the 2011 agreement) for an additional time period to continue coterminous with the 2014 agreement for approximately $6.2 million. As of June 30, 2017, approximately $3.5 million has been paid. In September 2015, the Corporation entered into 5 year agreement for annual upgrades for approximately $820,000 in total. Expenditures will be expensed or capitalized in the year they are disbursed. As of June 30, 2017, approximately $468,000 has been incurred and capitalized.

Regional Cancer Center

In December 2016, with the consent of the Board of Directors, the Corporation entered into an agreement for the construction of a new regional cancer facility for approximately $9 million. It is expected that the construction of the facility will be completed near December 2017 and will cost approximately $15 million to build, equip, and furnish the cancer center. Subsequent to year-end, the Corporation has obtained financing for the project and has begun construction.

8. Functional expenses

The Corporation provides general health care services to residents within its geographic area. Expenses related to providing these services are as follows for the years ended June 30:

	2017	2016
Health care services	**$ 93,181,395**	$ 80,496,219
General and administrative	**24,086,913**	32,408,211
	$ 117,268,308	$ 112,904,430

9. Business and Credit Concentrations

The Corporation grants credit to patients, many of whom are local residents. The Corporation generally does not require collateral or other security in extending credit; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits receivable under their health insurance programs, plans or policies.

At June 30, the Corporation had gross accounts receivable from third-party payers and others as follows:

	2017	2016
Medicare	**$ 6,295,489**	$ 4,932,045
Medicaid	**632,806**	762,570
Commercial insurance and HMOs	**4,427,853**	3,793,459
CareFirst	**2,789,868**	2,142,296
Self-pay and others	**7,781,213**	6,423,375
	$ 21,927,229	$ 18,053,745

Gross patient charges, by payer class, consisted of the following for the years ended June 30:

	2017	2016
Medicare	50%	50%
Medicaid	13%	12%
Commercial insurance and HMOs	14%	14%
CareFirst	18%	18%
Self-pay and others	5%	6%
	100%	100%

10. Grant Awards

In January 2002, the Hospital received notice indicating it was a recipient of a conditional award of up to $750,000 through the Perdue Kresge Challenge for the Community, an endowment challenge grant program for nonprofit organizations serving the Lower Eastern Shore of Maryland. This grant was contingent upon the Hospital's ability to raise, at a minimum, slightly more than two-thirds of the $750,000 match ($502,500) in qualified gifts in the Hospital's named agency-restricted endowment fund (the Fund). During 2005, the Hospital met the full challenge and Purdue Kresge matched the $750,000. By Board designation, all of the income distributed from the Perdue Kresge Challenge endowment will be used to fund physician practice development in the community.

On January 15, 2002, an endowment fund (the Fund) was established in the Hospital's name in order for the Hospital to participate in the Perdue Kresge Challenge for the Community. The Fund is held by and accounted for in the financial statements of the Community Foundation of the Eastern Shore. An unrelated third party actively manages the investments, which are invested currently in various bonds, mutual funds, and equities. All realized gains and losses are reinvested in the Fund. The Fund has no minimum value requirement. All gifts to the Fund will be invested in perpetuity. The Hospital, as sole beneficiary to any interest earned on the Fund, will receive income distributions earned on the assets of the Fund with no external restrictions regarding use; however, the Board of Trustees has designated all investment income from this endowment fund for funding physician practice development in the community. Income distributions will be made on an annual basis. Fund activity is presented below for the years ended June 30:

	2017	2016
Beginning fund balance	**$ 1,833,937**	$ 1,961,652
Interest and dividends	**66,954**	64,464
Net realized and unrealized losses	**171,496**	(79,688)
Administrative and management fees	**(19,536)**	(19,483)
Annual income distributions	**(94,720)**	(93,008)
Ending fund balance	**$ 1,958,131**	$ 1,833,937

11. Subsequent Events

In preparing these financial statements, the Corporation has considered events have been evaluated by management through October 25, 2017, which is the date the financial statements were issued. In September 2017, the Corporation entered into new tax-exempt financing of $30 million (including forward contracts to synthetically fix interest rates on variable rate indebtedness; see Note 5) and bank qualified bonds of $10 million that will be used to refund existing debt and fund the building and equipping of a new cancer center, WOC Women's Imaging and the Master Facility Plan.