

CONSOLIDATED FINANCIAL STATEMENTS  
AND SUPPLEMENTARY INFORMATION

Peninsula Regional Health System, Inc.  
Years Ended June 30, 2016 and 2015  
With Report of Independent Auditors

Ernst & Young LLP



Building a better  
working world

Peninsula Regional Health System, Inc.

Consolidated Financial Statements and Supplementary Information

Years Ended June 30, 2016 and 2015

**Contents**

Report of Independent Auditors.....1

Consolidated Financial Statements

Consolidated Balance Sheets .....3

Consolidated Statements of Operations and Changes in Net Assets .....5

Consolidated Statements of Cash Flows.....7

Notes to Consolidated Financial Statements.....8

Supplementary Information

Consolidating Balance Sheet .....43

Consolidating Statement of Operations .....45



## Report of Independent Auditors

The Board of Trustees  
Peninsula Regional Health System, Inc.

We have audited the accompanying consolidated financial statements of Peninsula Regional Health System, Inc. and subsidiaries (the Health System), which comprise the consolidated balance sheets as of June 30, 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 financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries and joint ventures of both Peninsula Health Ventures, Inc. (Health Ventures) and Peninsula Regional Medical Center (the Hospital), both of which are wholly owned subsidiaries of the Health System. Two of the entities, Delmarva Peninsula Insurance Company (DPIC) and Delmarva Surgery Center, LLC, (Delmarva), reflect total assets constituting 2.9% in 2016 and 4.8% in 2015 and total revenues constituting 1.2% in 2016 and 1.1% in 2015 of the related consolidated totals. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for DPIC and Delmarva, is based solely on the reports of the other auditors. Additionally, we did not audit the financial statements of Peninsula Imaging, LLC (Imaging), in which the Health System has a 50% interest. In the consolidated financial statements, the Health System's investment in Imaging is stated at \$2.1 million and \$2.8 million as of June 30, 2016 and 2015, respectively, and the Health System's equity in the excess of unrestricted revenue and other support over expenses of Imaging is stated at \$1.1 million and \$1.1 million for the years ended June 30, 2016 and 2015, respectively. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Imaging, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States. 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 Health System'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, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Peninsula Regional Health System, Inc. and subsidiaries at June 30, 2016 and 2015, and the consolidated results of their operations and changes in net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

### **Supplementary Information**

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Ernst & Young LLP*

September 23, 2016

Peninsula Regional Health System, Inc.

Consolidated Balance Sheets  
(In Thousands)

	<b>June 30</b>	
	<b>2016</b>	<b>2015</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 36,755	\$ 52,976
Short-term investments	6,760	6,477
Accounts receivable, less allowance for uncollectible accounts (2016 – \$8,278; 2015 – \$7,927)	42,234	39,306
Inventories and other	10,226	10,561
Prepays	6,327	4,922
Total current assets	<u>102,302</u>	114,242
Long-term investments	226,353	226,306
Board-designated investments	23,584	23,963
Assets limited as to use:		
Construction fund	10,228	18,863
Donor-restricted fund	33,217	31,922
Self-insurance fund	19,713	19,293
	<u>63,158</u>	70,078
Property and equipment, net	224,843	206,171
Unamortized financing costs, net of accumulated amortization	1,349	1,402
Other assets	19,663	19,405
Total assets	<u>\$ 661,252</u>	<u>\$ 661,567</u>

	<b>June 30</b>	
	<b>2016</b>	<b>2015</b>
<b>Liabilities and net assets</b>		
Current liabilities:		
Current portion of long-term debt	\$ 2,068	\$ 2,005
Current portion of accrued self-insured liabilities	2,495	2,495
Accounts payable	18,088	17,941
Accrued liabilities	14,936	18,765
Advances from third-party payors	11,401	9,846
Total current liabilities	<u>48,988</u>	<u>51,052</u>
Long-term debt, net	143,319	146,494
Other liabilities	38,537	17,141
Total liabilities	<u>230,844</u>	<u>214,687</u>
Net assets:		
Unrestricted	395,287	413,327
Temporarily restricted	25,058	23,520
Permanently restricted	8,245	8,246
Peninsula Regional Health System, Inc. net assets	<u>428,590</u>	<u>445,093</u>
Minority interest	1,818	1,787
Total net assets	<u>430,408</u>	<u>446,880</u>
Total liabilities and net assets	<u><u>\$ 661,252</u></u>	<u><u>\$ 661,567</u></u>

*See accompanying notes.*

Peninsula Regional Health System, Inc.

Consolidated Statements of Operations and Changes in Net Assets  
(In Thousands)

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
Unrestricted revenue and other support:		
Net patient service revenue	\$ 418,423	\$ 405,009
Provision for bad debts	<b>(11,477)</b>	(10,785)
Net patient service revenue less provision for bad debts	<b>406,946</b>	394,224
Other operating revenue	<b>2,749</b>	3,711
Total unrestricted revenue and other support	<b>409,695</b>	397,935
Operating expenses:		
Salaries and wages	<b>165,766</b>	155,405
Supplies and other expenses	<b>184,578</b>	167,655
Employee benefits	<b>34,429</b>	32,187
Depreciation	<b>22,804</b>	22,571
Interest	<b>5,052</b>	6,186
Total operating expenses	<b>412,629</b>	384,004
(Loss) income from operations	<b>(2,934)</b>	13,931
Nonoperating income (expense):		
Investment income	<b>10,690</b>	18,945
Loss on extinguishment of debt	-	(7,309)
Total nonoperating income	<b>10,690</b>	11,636
Excess of unrestricted revenue and other support over expenses	<b>7,756</b>	25,567
Minority interest in earnings of controlled subsidiaries	<b>(31)</b>	279
Excess of unrestricted revenue and other support over expenses attributable to Peninsula Regional Health System, Inc.	<b>7,725</b>	25,846

(continued on next page)

Peninsula Regional Health System, Inc.

Consolidated Statements of Operations and Changes in Net Assets (continued)  
(In Thousands)

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
Unrestricted net assets:		
Excess of unrestricted revenue and other support over expenses attributable to Peninsula Regional Health System, Inc.	\$ 7,725	\$ 25,846
Unrealized (losses) gains on investments	(9,251)	828
Pension adjustment	(16,514)	(2,717)
(Decrease) increase in unrestricted net assets	<u>(18,040)</u>	<u>23,957</u>
Temporarily restricted net assets:		
Donations	1,673	1,313
Net realized gains on investments	1,266	1,690
Unrealized (losses) gains on investments	(1,130)	491
Net assets released from restrictions	(271)	(335)
Increase in temporarily restricted net assets	<u>1,538</u>	<u>3,159</u>
Permanently restricted net assets:		
Net realized gains on investments	2	152
Unrealized (losses) gains on investments	(3)	1
(Decrease) increase in permanently restricted net assets	<u>(1)</u>	<u>153</u>
(Decrease) increase in net assets	<u>(16,503)</u>	<u>27,269</u>
Net assets at beginning of year	<u>445,093</u>	<u>417,824</u>
Net assets at end of year	<u>\$ 428,590</u>	<u>\$ 445,093</u>

See accompanying notes.

Peninsula Regional Health System, Inc.

Consolidated Statements of Cash Flows  
(In Thousands)

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
<b>Operating activities</b>		
Change in net assets	\$ (16,503)	\$ 27,269
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation of property and equipment	22,804	22,571
Loss on advance refunding of debt	–	7,309
Amortization of original issue premium	(1,105)	(166)
Amortization of financing costs	46	78
Losses (gains) on sale of property and equipment	–	(12)
Net unrealized losses on investments	7,358	372
Net realized gains on investments	(7,251)	(15,155)
Proceeds from restricted contributions and realized gains on restricted investments	(2,939)	(3,003)
Minority interest in earnings of controlled subsidiaries	31	(279)
Changes in operating assets and liabilities:		
Accounts receivable	(2,587)	(95)
Inventories and other assets	(1,205)	1,441
Accounts payable and accrued liabilities	(4,981)	5,259
Other liabilities	18,568	2,493
Advances from third-party payors	1,555	625
Net cash provided by operating activities	<u>13,791</u>	<u>48,707</u>
<b>Investing activities</b>		
Purchase of investments	(154,630)	(167,972)
Proceeds from sales of investments	162,126	146,946
Purchases of property and equipment	(37,283)	(21,576)
Proceeds from disposal of assets	–	14
Change in assets limited to use	(1,160)	(4,395)
Net cash used in investing activities	<u>(30,947)</u>	<u>(46,983)</u>
<b>Financing activities</b>		
Proceeds from restricted contributions and realized losses on restricted investments	2,939	3,003
Proceeds from Bond Issuance	–	147,435
Deferred financing costs	–	(1,375)
Repayments of long-term debt	(2,004)	(130,404)
Net cash provided by financing activities	<u>935</u>	<u>18,659</u>
Net (decrease) increase in cash and cash equivalents	(16,221)	20,383
Cash and cash equivalents at beginning of year	52,976	32,593
Cash and cash equivalents at end of year	<u>\$ 36,755</u>	<u>\$ 52,976</u>

See accompanying notes.

# Peninsula Regional Health System, Inc.

## Notes to Consolidated Financial Statements *(Dollar Amounts in Thousands)*

June 30, 2016

### **1. Organization and Mission**

Peninsula Regional Health System, Inc. (the Health System) serves as the parent company to Peninsula Regional Medical Center (the Hospital); Peninsula Regional Medical Center Foundation, Inc. (the Foundation); Peninsula Health Ventures, Inc. (Health Ventures); Peninsula Women's Surgery Center, LLC; and Peninsula Regional Clinically Integrated Network, LLC. The Health System is a not-for-profit Maryland membership corporation established to manage the integrated delivery of health care services to the community. The Health System is the sole corporate member of the Hospital and the Foundation. In its capacity as sole corporate member, the Health System will appoint trustees, approve major expenditures, and approve long-term borrowings.

The Hospital is a not-for-profit, nonstock corporation founded in 1897 to serve the health care needs of its region. Primary service areas include the Maryland counties of Wicomico, Somerset, and Worcester; southern Delaware; and the northern Eastern Shore of Virginia. The Hospital's mission is to improve the health care of the community by providing exceptional quality primary, secondary, and selected tertiary health care services to patients in a competent and compassionate manner, designed to elicit a high degree of customer satisfaction. The Hospital provides services regardless of race, creed, sex, national origin, handicap, or age. In May 2013, Delmarva Peninsula Insurance Company (DPIC) was incorporated as a wholly owned subsidiary of the Hospital. DPIC was formed as captive insurer to provide professional and general liability (GL) insurance.

The Foundation is a not-for-profit, nonstock corporation organized to raise contributions exclusively for the benefit of charitable, educational, medical, and scientific purposes for the Hospital.

Health Ventures is a for-profit corporation organized for the purpose of owning, developing, operating, and investing in health care enterprises on the Delmarva Peninsula. The Health System owns all of the outstanding shares of common stock of Health Ventures.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

## **2. Significant Accounting Policies**

### **Principles of Consolidation**

The consolidated financial statements include the accounts of the Health System and all wholly owned subsidiaries, principally the Hospital, the Foundation, and Health Ventures. Additionally, the Health System has consolidated a 55%-owned affiliate, Delmarva Surgery Center, LLC, and recorded minority interest equal to the remaining ownership interest.

### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 amounts could differ from those estimates.

### **Fair Value of Financial Instruments**

The carrying amounts of financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, and advances from third-party payors, approximate fair value given the short-term nature of these financial instruments.

### **Cash and Cash Equivalents**

Cash and cash equivalents include surplus operating funds invested in money market funds and highly liquid corporate, U.S. government, and agency obligations, all with maturities of less than three months when purchased.

### **Investments and Investment Income**

Investments are carried at fair value. All such investments are considered available for sale and are classified as current or noncurrent assets based on management's intention as to use. Short-term investments represent investments with contractual maturities within one year and current investments in money market funds that have been designated for investment purposes. Assets limited as to use by donor restriction are recorded at fair value at the date of donation, and changes in fair value are recognized in the period in which the change occurs. Investment income

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **2. Significant Accounting Policies (continued)**

from all unrestricted investments is reported as nonoperating income. Investment income on investments of restricted assets is added to or deducted from the appropriate restricted net assets when restricted as to use by the donor.

The value of securities sold is based on the specific identification method.

The Health System periodically evaluates whether any declines in the fair value of investments are other than temporary. This evaluation consists of a review of several factors, including, but not limited to, length of time and extent that a security has been in an unrealized loss position, the existence of an event that would impair the issuer's future earnings potential, the near-term prospects for recovery of the market value of a security, and the intent and ability of the Health System to hold the security until the market value recovers. Realized gains or losses are included in nonoperating income (expense) on the accompanying consolidated statements of operations and changes in net assets. Declines in fair value below cost that are deemed to be other than temporary would be recorded as realized losses within nonoperating income (expense). Based on its evaluation, the Health System has recorded no other-than-temporary impairments for the years ended June 30, 2016 or 2015.

#### **Accounts Receivable and Contractual Allowances**

The Health System, through its member companies, provides services to patients in the Eastern Shore area of Maryland, Delaware, and Virginia, the majority of whom are covered by third-party health insurance. The Health System bills the insurer directly for services provided.

Insurance coverage and financial information is obtained from patients upon admission when available. The Health System's policy is to perform in-house collection procedures for approximately 85 days. A determination is made at that time as to which additional collection efforts to pursue. A provision for uncollectible accounts is recorded for amounts not yet written off, which are expected to become uncollectible.

Discounts ranging from 2% to 6% of charges are given to Medicare, Medicaid, and certain approved commercial health insurance and health maintenance organization programs for regulated services. Discounts in varying percentages are given for certain unregulated services. These major payors routinely review patient billings and deny payment for certain charges as medically unnecessary or as performed without appropriate preauthorization. Discounts and

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **2. Significant Accounting Policies (continued)**

denials are recorded as reductions of net patient service revenue. Revenue and accounts receivable from these third-party payors have been adjusted to reflect the difference between charges and the estimated reimbursable amounts.

Approximately 35% and 38% of accounts receivable were due from the Medicare program as of June 30, 2016 and 2015, respectively.

The Medicare and Medicaid reimbursement programs represent a substantial portion of the Health System's revenues. The Health System'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.

Over the past several years, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs, together with the imposition of fines and penalties, as well as repayments for patient services previously billed. Compliance with fraud and abuse standards and other government regulations can be subject to future government review and interpretation. Also, future changes in federal and state reimbursement funding mechanisms and related government budgeting constraints could have an adverse effect on the Health System.

#### **Inventories and Other**

Inventories and other primarily include inventories of supplies and prepaid expenses. Inventories of supplies are carried at the lower of cost or market, using the first-in, first-out method.

#### **Other Assets**

Other assets primarily include a 50% non-controlling interest in each of the following entities, which are accounted for as equity method investments: Peninsula Imaging, LLC; AHP Delmarva, LLP; Genesis Healthcare; Peninsula-NRH Regional Rehabilitation, LLC; and Peninsula Home Care, LLC. The Hospital also has a 33.3% non-controlling interest in Peninsula Home Care at Nanticoke, which is accounted for as an equity method investment. Additionally, other assets include a reinsurance receivable asset in 2016 and 2015 and a prepaid pension asset in 2015.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **2. Significant Accounting Policies (continued)**

##### **Assets Limited as to Use**

Assets limited as to use primarily include assets held by trustees under indenture agreements; assets held by trustees under irrevocable self-insurance trust agreements; and assets, including pledges receivable, whose use has been limited by the donor of the underlying funds. Amounts required to meet current liabilities have been classified on the consolidated balance sheets as current assets.

##### **Board-Designated Investments**

Board-designated investments include assets set aside by the Board of Trustees for future capital improvements and expansion. The Board of Trustees retains control of these assets and may, at its discretion, subsequently use them for other purposes.

##### **Property and Equipment**

Property and equipment consists of furniture, fixtures, equipment, and capitalized internal use software and acquired software development costs. Property acquired and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Software development costs that are incurred in the preliminary project stage for internal use software are expensed as incurred. During the development stage, direct consulting costs and payroll and payroll-related costs for employees that are directly associated with each project are capitalized and amortized over the estimated useful life of the software once the software is ready for its intended use. Capitalized software is amortized using the straight-line method over its estimated useful life, which is generally seven years. Replacements and upgrades and enhancements to existing systems that result in added functionality are capitalized, while maintenance and repairs are charged to expense as incurred.

Gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted donations. Absent explicit donor stipulations about how long those assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **2. Significant Accounting Policies (continued)**

##### **Construction Fund**

The Construction Fund was created as a result the proceeds of the 2015 Maryland Health and Higher Educational Facilities Authority (MHHEFA) Revenue Bond Offering, net of the advance refunding of the 2006 MHHEFA bond offering. The net proceeds are required to be spent on capital improvements, and used for the acquisition, renovation, or equipping of certain facilities of the Hospital.

##### **Unamortized Financing Costs**

Financing costs incurred in issuing the Maryland Health and Higher Educational Facilities Authority Project and Refunding Revenue Bonds have been capitalized and are being amortized using the straight-line method over the life of the bonds, which approximates the effective interest method. The amount amortized is recorded as an operating expense.

##### **Estimated Self-Insurance Liabilities and Workers' Compensation**

The provision for estimated professional liability claims, general liability claims, and workers' compensation claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported.

##### **Pension Benefits**

Pension benefits are recorded in accordance with Accounting Standards Codification Topic (ASC) 715, *Compensation – Retirement Benefits*, which requires the recognition of the funded status of pension plans within the accompanying consolidated balance sheets. As of June 30, 2016 and 2015, the funded status of the pension plan has been recorded within other long-term liabilities and other assets, respectively.

##### **Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are those whose use by the Health System has been limited by donors to a specific time period or purpose. Temporarily restricted net assets are to be used for capital purposes and other health care services.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**2. Significant Accounting Policies (continued)**

Permanently restricted net assets have been restricted by donors to be maintained by the Health System in perpetuity.

**Net Patient Service Revenue**

Net patient service revenue is reported at the estimated realizable amounts from patients, third-party payors, and others for services rendered. During 2016 and 2015, approximately 49% and 48%, respectively, of net patient service revenue was received under the Medicare program, 12% from CareFirst Blue Cross Blue Shield, 33% and 34%, respectively, from contracts with other third parties, and 6% from other sources.

The following table sets forth the detail of net patient service revenue:

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
Gross patient service revenue	\$ 522,069	\$ 506,851
Revenue deductions:		
Charity care	8,670	9,408
Contractual and other allowances	94,976	92,434
Patient revenue, net of deductions	418,423	405,009
Less provision for bad debts	11,477	10,785
Net patient service revenue less bad debts	\$ 406,946	\$ 394,224

The Health System employs physicians in several hospital-based specialties. The Health System bills for the services provided by these physicians. Net physician revenue is recognized when the services are provided and recorded at the estimated net realizable amount based on the contractual arrangements with third-party payors and the expected payments from the third-party payors and the patients. The difference between the billed charges and the estimated net realizable amounts is recorded as a reduction in physician revenue when the services are provided. For the years ended June 30, 2016 and 2015, the Health System recorded \$33,388 and \$29,460 of net physician revenue, respectively.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **2. Significant Accounting Policies (continued)**

Patient accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the Health System analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the Health System analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary. For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Health System records a provision for bad debts in the period of service on the basis of its past experience. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts. The Health System has not changed its charity care or uninsured discount policies during fiscal years 2016 or 2015.

#### **Other Operating Revenue**

The American Recovery and Reinvestment Act of 2009 provides for Medicare and Medicaid incentive payments for eligible hospitals and professionals that implement and achieve meaningful use of certified electronic health record (EHR) technology. For Medicare and Medicaid EHR incentive payments, the Hospital uses a gain contingency accounting method to recognize the revenues. Under this accounting policy, EHR incentive payments are recognized as revenue upon the completion of the meaningful use period and completion of the related 12-month cost report. Accordingly, the Hospital recognized approximately \$790 and \$1,974 of EHR revenues for the years ended June 30, 2016 and 2015, respectively. This is based on cost report data that is subject to audit by the Centers for Medicare & Medicaid Services (CMS) or its intermediaries, and the amounts recognized are subject to change.

These amounts are included in other operating revenue on the consolidated statements of operations. The Hospital's attestation of compliance with the meaningful use criteria is subject to audit by the federal government or its designee. The recognition of revenues is based on management's best estimate. Any subsequent changes in the recognition of revenue will impact the results of operations in the period in which they occur.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **2. Significant Accounting Policies (continued)**

##### **Charity Care**

The Health System provided care to patients who met certain criteria under its charity care policy, without charge or at amounts less than its approved rates. Because the Health System did not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The amounts written off as charity care for 2016 and 2015 were \$7,113 and \$7,402, respectively. These amounts represent direct and indirect charity care costs, which are calculated using the Health System's cost to charge ratio. The state of Maryland rate system includes components within the rates to partially compensate health systems for uncompensated care.

##### **Donor-Restricted Gifts**

Unconditional promises to give cash and other assets to the Health System are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted donations 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 the purpose of the restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported on the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

##### **Investment Income**

Investment income primarily includes income from short-term and long-term investments, board-designated investments, and investments within assets limited as to use. In addition, investment income is also recorded for certain equity method investments that are included within other assets.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued) (Dollar Amounts in Thousands)

#### 2. Significant Accounting Policies (continued)

The components of investment income are as follows:

	Year Ended June 30	
	2016	2015
Interest and dividend income	\$ 5,587	\$ 4,300
Realized gains, net	1,837	11,373
Income earned on equity method investments	3,168	3,155
Other	98	117
Total	<u>\$ 10,690</u>	<u>\$ 18,945</u>

#### Income Taxes

The Health System is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code.

#### Performance Indicator

The performance indicator for the Health System is excess of unrestricted revenue and other support over expenses, which includes all changes in unrestricted net assets except for changes in unrealized gains and losses on investments; pension adjustments in accordance with ASC 958-715, *Not-for-Profit Entities – Compensation – Retirement Benefits*; and net assets released from restrictions for property acquisitions.

#### Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued ASC 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This guidance is intended to improve and converge with international standards the financial reporting requirements for revenue from contracts with customers. It will be effective for fiscal year 2019, and early adoption is permitted beginning in fiscal year 2018. The Health System has not yet determined the impact from adoption of this new accounting pronouncement on its consolidated financial statements.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

#### 2. Significant Accounting Policies (continued)

In August 2014, the FASB issued ASU 2014-15, *Presentation of Financial Statements – Going Concern (Subtopic 205-40)*, which provides guidance in GAAP about management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. This amendment should reduce diversity in the timing and content of footnote disclosures. This ASU is effective for fiscal year 2017. The guidance is not expected to materially impact the Health System’s consolidated results of operations, net assets, or cash flows.

In April 2015, the FASB issued ASU 2015-03, *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*. The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This guidance is effective for fiscal year 2017. The guidance is not expected to materially impact the Health System’s consolidated results of operations, net assets, or cash flows.

In April 2015, the FASB issued ASU 2015-05, *Intangibles – Goodwill and Other – Internal – Use Software (Subtopic 350-40): Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement*, which provides guidance to clarify the customer’s accounting for fees paid in a cloud computing arrangement and also eliminates today’s requirement that customers analogize to the leases standard when determining the asset acquired in a software licensing arrangement. This guidance is effective for fiscal year 2017. The guidance is not expected to materially impact the Health System’s consolidated results of operations, net assets, or cash flows.

In February 2016, the FASB issued ASU 2016-02, *Leases*. This ASU amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets. This guidance is effective for fiscal year 2020. The Health System is currently assessing the potential impact this ASU will have on the Health System’s consolidated results of operations, financial position and cash flows.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**3. Property and Equipment**

A summary of property and equipment follows:

	<b>Estimated Useful Lives (in Years)</b>	<b>June 30</b>	
		<b>2016</b>	<b>2015</b>
Land	–	\$ 11,385	\$ 11,385
Land improvements	20	11,711	13,997
Buildings and improvements	15–40	233,272	220,063
Fixed equipment	20	33,822	34,115
Movable equipment	7–10	209,822	201,143
		<b>500,012</b>	480,703
Less accumulated depreciation		<b>(301,092)</b>	(290,123)
		<b>198,920</b>	190,580
Acquired and internally developed software		17,482	–
Construction-in-progress		8,441	15,591
Property and equipment, net		<b>\$ 224,843</b>	<b>\$ 206,171</b>

As of June 30, 2016, the Hospital was committed to building and equipment purchases totaling approximately \$5,628.

**4. Other Liabilities**

The components of other liabilities are as follows:

	<b>June 30</b>	
	<b>2016</b>	<b>2015</b>
Self-insurance obligations	\$ 17,898	\$ 15,847
Long-term pension benefit obligation	16,306	–
Other	4,333	1,294
Total	<b>\$ 38,537</b>	<b>\$ 17,141</b>

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**5. Long-Term Debt**

Long-term debt consists of the following:

	<u>June 30, 2016</u>
Maryland Health and Higher Educational Facilities Authority Revenue Bonds Series 2015:	
Series 2015 serial bonds with interest rates ranging from 3.00% to 5.00% and effective rates ranging from 2.57% to 3.01% due in various annual amounts on July 1 of each year from 2016 through 2034	\$ 55,964
Series 2015 5.00% term bonds with effective rate of 3.99% due July 1, 2039	26,444
Series 2015 5.00% term bonds with effective rate of 4.13% due July 1, 2045	41,550
Building and equipment collateral loans:	
4.40% fixed rate due monthly from 2012 to 2022	1,774
	<u>125,732</u>
Less current portion of Maryland Health and Higher Educational Facilities Authority Series 2015 serial bonds	1,990
Less current portion of building and equipment collateral loans	78
	<u>123,664</u>
Original issue premium	19,655
Long-term debt, less current portion	<u><u>\$ 143,319</u></u>

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**5. Long-Term Debt (continued)**

	<u>June 30, 2015</u>
Maryland Health and Higher Educational Facilities Authority Revenue Bonds Series 2015:	
Series 2015 serial bonds with interest rates ranging from 3.00% to 5.00% and effective rates ranging from 2.57% to 3.01% due in various annual amounts on July 1 of each year from 2015 through 2034	\$ 57,895
Series 2015 5.00% term bonds with effective rate of 3.99% due July 1, 2039	26,445
Series 2015 5.00% term bonds with effective rate of 4.13% due July 1, 2045	41,550
Building and equipment collateral loans:	
4.40% fixed rate due monthly from 2012 to 2022	1,849
	<u>127,739</u>
Less current portion of Maryland Health and Higher Educational Facilities Authority Series 2015 serial bonds	1,930
Less current portion of building and equipment collateral loans	75
	<u>125,734</u>
Original issue premium	20,760
Long-term debt, less current portion	<u><u>\$ 146,494</u></u>

**Series 2015 Revenue Bonds**

On February 5, 2015, MHHEFA authorized the issuance of \$126,665 aggregate principal amount of Revenue Bonds (Series 2006 Revenue Bonds) at a premium of \$20,770. The proceeds of the issue, after payment of financing costs, were used primarily (i) to advance refund outstanding 2006 bonds and (ii) to finance \$25,000 of capital purchases.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **5. Long-Term Debt (continued)**

The Hospital is required to make semiannual payments to the trustee sufficient to meet the annual debt service requirements of the refunding bond issue for the succeeding year. Annual sinking fund installments for the term bonds range from \$3,322 on July 1, 2015, to \$8,189 on July 1, 2020. The premium on the Series 2015 Bonds is being amortized over the life of the bonds using the effective interest method.

As security for the debt service requirements of the Series 2015 Bonds, MHHEFA has a first lien and claim on all receipts of the Hospital. The terms of the indenture agreement restrict the Hospital's ability to create additional indebtedness and its use of the facilities, and require the Hospital to maintain stipulated insurance coverage and a rate structure in each year sufficient to meet certain rate covenant requirements.

#### **Series 2006 Revenue Bonds**

On February 9, 2006, MHHEFA authorized the issuance of \$142,910 aggregate principal amount of Series 2006 Revenue Bonds at a premium of \$5,333. The proceeds of the issue, after payment of financing costs, were used primarily (i) to finance and refinance a portion of the costs of construction, renovation, acquisition and equipping of the 2006 Project; (ii) to refund outstanding 1993 bonds; (iii) to pay a portion of the interest accruing on the Series 2006 Revenue Bonds for a period to extend to January 1, 2009; and (iv) to pay the Counterparty a termination payment of \$1,575 in connection with a forward starting interest rate exchange agreement entered into on August 9, 2005, and unwound on January 24, 2006.

The Series 2006 Revenue Bonds were refunded in February 2015 upon the issuance of the Series 2015 Revenue Bonds. The Health System incurred a \$7,300 loss on advance refunding of Series 2006 Revenue Bonds, which relates to advance refunding amounts in excess of principal payments and the write-off of unamortized financing costs, partially offset by the write-off of the unamortized bond premium.

#### **Delmarva Surgery Center, LLC Building Loan**

On June 1, 2012, Delmarva Surgery Center, LLC, a 55%-owned subsidiary of Health Ventures, entered into a fixed rate loan agreement with BB&T Bank in the amount of \$2,059 (\$1,774 outstanding at June 30, 2016), with fixed monthly payments through June 1, 2022.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**5. Long-Term Debt (continued)**

Scheduled principal repayments on long-term debt for the years ending June 30 are as follows:

2017	\$ 2,068
2018	2,173
2019	2,282
2020	2,396
2021	2,515
2022 and thereafter	114,298
	<u>\$ 125,732</u>

Fair values of long-term debt are estimated using discounted cash flow analyses, based on current incremental borrowing rates for similar types of borrowing arrangements.

The fair value of the Health System's long-term debt outstanding as of June 30, 2016 and 2015, was approximately \$148,928 and \$139,628, respectively.

Total interest paid for fiscal years 2016 and 2015 was \$4,999 and \$6,133, respectively.

**6. Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are available for the following purposes:

	<b>June 30</b>	
	<b>2016</b>	<b>2015</b>
Health care services:		
Capital purposes	\$ 17,390	\$ 17,208
Patient services	6,569	5,185
Educational purposes	1,099	1,127
	<u>\$ 25,058</u>	<u>\$ 23,520</u>

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**6. Temporarily and Permanently Restricted Net Assets (continued)**

Permanently restricted net assets are restricted as follows:

	<b>June 30</b>	
	<u>2016</u>	<u>2015</u>
Investments to be held in perpetuity, the income from which is expendable to support health care services	<u>\$ 8,245</u>	<u>\$ 8,246</u>

The Foundation initiated a major fundraising campaign for capital funds during fiscal year 2005 to support the Hospital's capital plans that include expansion and modernization of facilities. The Foundation has raised approximately \$14,629 as of June 30, 2016, which includes net pledges receivable presently valued at approximately \$584. The Foundation expects to receive payment on the majority of the pledges by 2020 and all payments by 2025. Additionally, during 2011, the Foundation launched a fundraising campaign to support the operating room expansion. This campaign has raised \$2,894 as of June 30, 2016, which includes net pledges receivable presently valued at \$123. Additionally during 2015, the Foundation initiated a behavioral health campaign that has raised \$1,511 as of June 30, 2016, and includes net pledges receivable presently valued at \$558. Pledges receivable are included in assets limited as to use in the accompanying balance sheets.

Scheduled payments on pledges receivable for the years ending June 30 are as follows:

2017	\$ 445
2018–2021	739
2022 and thereafter	<u>355</u>
	1,539
Less:	
Impact of discounting of pledges receivable to net present value	112
Allowance for uncollectible pledges	<u>163</u>
Net pledges receivable, capital campaign	<u>\$ 1,264</u>

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**7. Functional Expenses**

The Health System considers health care services and management and general to be its primary functional categories for purposes of expense classification. Depreciation and interest costs are included in health care services. The Health System's operating expenses by functional classification are as follows:

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
Health care services	\$ 353,874	\$ 345,559
Management and general	58,755	38,445
	<u>\$ 412,629</u>	<u>\$ 384,004</u>

**8. Malpractice Insurance Costs, Self-Insured Professional Liability, and Workers' Compensation**

Effective July 1, 2013, Delmarva Peninsula Insurance Captive (DPIC) was formed as a captive insurer to provide professional liability insurance. DPIC is a wholly owned subsidiary of the Hospital. The primary layer of professional and GL insurance coverage is self-insured through DPIC, and the secondary layer is fully insured through a commercial carrier.

Effective July 1, 2013, under a loss portfolio transfer agreement, DPIC assumed the medical professional liability (MPL) and GL coverage previously included under PRMC's self-insurance plan for incidents occurring between March 1, 1986 and June 30, 2013, for MPL and for occurrences between March 1, 2004 and June 30, 2013, for GL that were reported to the Hospital prior to June 30, 2013. The policy provides MPL coverage limits varying from \$1,000 to \$2,000 for each and every medical incident, with policy aggregates varying from \$3,000 to \$8,000. The policy provides GL coverage limits of \$1,000 per occurrence and \$3,000 policy aggregates. This policy is retrospectively rated.

DPIC is fully insured by commercial carriers in excess of the coverage limits discussed above up to \$25,000 per claim and in the aggregate. As of June 30, 2016 and 2015, the accrued self-insured professional liability losses have been undiscounted for both years. As of June 30, 2016 and 2015, \$16,646 and \$14,146, respectively, has been reserved for professional liability loss contingencies, including excess coverage. A related reinsurance receivable of \$5,100 and \$4,010 has been recorded in other assets as of June 30, 2016 and 2015, respectively.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

**8. Malpractice Insurance Costs, Self-Insured Professional Liability, and Workers' Compensation (continued)**

Effective July 1, 2013, DPIC provides excess umbrella liability coverage on a mature claims-made basis with a retroactive date of March 1, 2005. The excess MPL tower follows the form of the underlying primary MPL coverage providing a total of \$25,000 limits of liability. The umbrella liability coverage provides \$25,000 limits of liability excess of scheduled underlying coverages including the primary GL coverage. The excess umbrella liability coverage is 100% reinsured with Darwin for the first \$10,000 limit and OneBeacon for the second \$15,000 limit.

The Hospital is also self-insured for workers' compensation up to an annual limit of \$500 per occurrence. The Hospital carries an excess liability insurance policy for workers' compensation claims above this limit. As of June 30, 2016 and 2015, \$3,701 and \$4,200, respectively, has been reserved for workers' compensation loss contingencies.

**9. Investments**

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

Fair values of all investments, including short-term investments, long-term investments, board-designated investments, and assets limited as to use are based on quoted market prices and/or prices obtained from a third party using other market data for the same or comparable instruments and transactions in establishing the prices. Certain long-term pledges receivable have been discounted.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)  
*(Dollar Amounts in Thousands)*

**9. Investments (continued)**

Fair value of investments and certain assets limited as to use held by the Health System is summarized as follows:

	<b>June 30</b>	
	<b>2016</b>	<b>2015</b>
Investments:		
Cash and cash equivalents	\$ 22,692	\$ 19,149
U.S. Treasury securities	16,592	12,789
Corporate bonds	58,267	54,843
Mortgage-backed securities	25,879	39,909
Equity securities	194,893	198,168
Other (including pledges receivable held at the Foundation)	1,533	1,966
Total	<u>\$ 319,856</u>	<u>\$ 326,824</u>

ASC 320, *Investments – Debt and Equity Securities*, provides guidance on the recognition and presentation of other-than-temporary impairments. If a debt security is in an unrealized loss position and the Health System has the intent to sell the debt security, or it is more likely than not that the Health System will have to sell the debt security before recovery of its amortized cost basis, the decline in value is deemed to be other than temporary and is recorded to other-than-temporary impairment losses recognized in the performance indicator on the consolidated statements of operations and changes in net assets. For impaired debt securities that the Health System does not intend to sell or it is more likely than not that the Health System will not have to sell such securities, but the Health System expects that it will not fully recover the amortized cost basis, the credit component of the other-than-temporary impairment is recognized in other-than-temporary impairment losses recognized in income on the consolidated statements of operations and changes in net assets and the non-credit component of the other-than-temporary impairment is recognized as a change in unrestricted net assets.

The credit component of other-than-temporary impairment is determined by comparing the net present value of projected future cash flows with the amortized cost basis of the debt security. The net present value is calculated by discounting the best estimate of projected future cash flows at the effective interest rate implicit in the debt security at the date of acquisition. Cash flow estimates are driven by assumptions regarding probability of default, including changes in credit ratings, and estimates regarding timing and amount of recoveries associated with a default.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)  
*(Dollar Amounts in Thousands)*

**9. Investments (continued)**

Furthermore, unrealized losses entirely caused by non-credit-related factors related to debt securities for which the Health System expects to fully recover the amortized cost basis continue to be recognized as an unrealized loss on investments within the changes in unrestricted net assets.

The following table shows the gross unrealized losses and fair value of the Health System's investments with unrealized losses that are not deemed to be other than temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

	<b>Fair Value &lt; 1 Year</b>	<b>Unrealized Losses &lt; 1 Year</b>	<b>Fair Value &gt; 1 Year</b>	<b>Unrealized Losses &gt; 1 Year</b>	<b>Total Unrealized Losses</b>
<b>June 30, 2016</b>					
U.S. Treasury	\$ -	\$ -	\$ 3,255	\$ 213	\$ 213
Mortgage-backed securities	542	23	1,486	55	78
Corporate bonds	5,154	65	8,041	488	553
Equity securities	37,776	3,215	2,664	206	3,421
Total investments	<u>\$ 43,472</u>	<u>\$ 3,303</u>	<u>\$ 15,446</u>	<u>\$ 962</u>	<u>\$ 4,265</u>
<b>June 30, 2015</b>					
U.S. Treasury	\$ 4,334	\$ 63	\$ 3,869	\$ 218	\$ 281
Mortgage-backed securities	2,690	25	4,869	235	260
Corporate bonds	20,204	299	7,000	408	707
Equity securities	33,149	1,910	204	19	1,929
Total investments	<u>\$ 60,377</u>	<u>\$ 2,297</u>	<u>\$ 15,942</u>	<u>\$ 880</u>	<u>\$ 3,177</u>

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **10. Fair Value Measurements**

ASC 820, *Fair Value Measurement*, establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described below.

- Level 1 – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Health System has the ability to access.
- Level 2 – Inputs to the valuation methodology include:
  - Quoted prices for similar assets or liabilities in active markets
  - Quoted prices for identical or similar assets or liabilities in inactive markets
  - Inputs other than quoted prices that are observable for the asset or liability
  - Inputs that are derived principally from or corroborated by observable market data by correlation or other means
- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)  
*(Dollar Amounts in Thousands)*

**10. Fair Value Measurements (continued)**

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Health System 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 the Health System's assets and liabilities measured at fair value, aggregated by level in the fair value hierarchy within which those measurements fall:

	<b>Assets at Fair Value as of June 30, 2016</b>			
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 22,692	\$ –	\$ –	\$ 22,692
U.S. government securities	16,592	–	–	16,592
Corporate bonds	–	58,267	–	58,267
Government-sponsored mortgage-backed securities	–	25,879	–	25,879
Equity securities	194,893	–	–	194,893
Other	269	–	1,264	1,533
<b>Total assets</b>	<b>\$ 234,447</b>	<b>\$ 84,146</b>	<b>\$ 1,264</b>	<b>\$ 319,856</b>

	<b>Assets at Fair Value as of June 30, 2015</b>			
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 19,149	\$ –	\$ –	\$ 19,149
U.S. government securities	12,789	–	–	12,789
Corporate bonds	–	54,843	–	54,843
Government-sponsored mortgage-backed securities	–	39,909	–	39,909
Equity securities	198,168	–	–	198,168
Other	853	–	1,113	1,966
<b>Total assets</b>	<b>\$ 230,959</b>	<b>\$ 94,752</b>	<b>\$ 1,113</b>	<b>\$ 326,824</b>

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)  
*(Dollar Amounts in Thousands)*

**10. Fair Value Measurements (continued)**

The fair values of securities are determined by third-party service providers utilizing various methods dependent upon the specific type of investment. Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Where significant inputs, including benchmark yields, broker-dealer quotes, issuer spreads, bids, offers, the London Interbank Offered Rate curve, and measures of volatility, are used by these third-party dealers or independent pricing services to determine fair values, the securities are classified within Level 2.

Long-term pledges receivable, which are measured at fair value on a nonrecurring basis, are discounted to net present value upon receipt using an appropriate risk-free discount rate based on the term of the receivable. Pledges receivable are recorded net of an allowance for uncollectible pledges. The following table provides a reconciliation of the beginning and ending balances of pledges receivable at fair value that used significant unobservable inputs (Level 3):

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
<b>Pledges receivable</b>		
Balance at July 1	\$ 1,113	\$ 1,503
New pledges	725	257
Collections on pledges	(601)	(726)
Write-off of pledges	-	(1)
Changes in reserves	27	80
Balance at June 30	<u>\$ 1,264</u>	<u>\$ 1,113</u>

**11. Pension Plan**

The Health System has a cash balance-type defined benefit pension plan covering substantially all of its employees. Plan benefits are based on years of service and the employees' compensation during the last five years of covered employment. The Health System's funding policy is to make sufficient contributions to the plan to comply with the minimum funding provisions of the Employee Retirement Income Security Act of 1974. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

**11. Pension Plan (continued)**

The Peninsula Regional Medical Center Pension Plus Plan (the Plan) provides annual allocations to a participant's hypothetical account. When a participant retires, the participant has the choice to receive a lump-sum distribution equal to the value of the hypothetical account or to receive an annuity based on the value of the hypothetical account.

Prior to January 1, 2009, the Plan provided three different allocations: (i) a service-related allocation, (ii) an age-related allocation, and (iii) a matching allocation. Both the service-related allocation and the age-related allocation were determined by multiplying a participant's annual compensation by a certain percentage. The matching allocation operated to provide an annual allocation in the Plan based on the participant's contribution to the Health System's 403(b) plan.

The Internal Revenue Service issued new regulations that were effective as of January 1, 2009. The new regulations prohibited a pension plan from providing a matching allocation based on a participant's contributions to a different plan. The Plan provided a matching allocation based on a participant's contribution to a 403(b) plan. In order to comply with the new tax law requirements, the Plan was amended effective as of December 31, 2008, to eliminate future matching allocations in the Plan. At the same time, the Health System adopted a 403(b) plan effective as of January 1, 2009, and provided a replacement matching contribution in the 403(b) plan.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**11. Pension Plan (continued)**

The following provides a reconciliation of the changes in fair value of the Plan's assets and projected benefit obligations, and the Plan's funded status:

	<b>June 30</b>	
	<b>2016</b>	<b>2015</b>
Accumulated benefit obligation	<b>\$ 121,840</b>	\$ 108,280
Projected benefit obligation, beginning of year	<b>\$ 117,330</b>	\$ 106,976
Service cost	<b>5,825</b>	5,126
Interest cost	<b>4,584</b>	3,587
Actuarial loss	<b>9,819</b>	6,318
Benefits paid	<b>(3,127)</b>	(4,677)
Projected benefit obligation, end of year	<b>134,431</b>	117,330
Fair value of plan assets, beginning of year	<b>119,411</b>	113,002
Actual gain on plan assets	<b>(1,159)</b>	8,086
Employer contributions	<b>3,000</b>	3,000
Benefits paid	<b>(3,127)</b>	(4,677)
Fair value of plan assets, end of year	<b>118,125</b>	119,411
Fair value of plan assets (less) greater than the projected benefit obligation	<b>\$ (16,306)</b>	\$ 2,081
(Pension liability) prepaid pension cost recorded on the consolidated balance sheet	<b>\$ (16,306)</b>	\$ 2,081

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**11. Pension Plan (continued)**

Components of net periodic benefit cost are as follows:

	<b>Year Ended June 30</b>	
	<b>2016</b>	<b>2015</b>
Service cost	\$ 5,825	\$ 5,126
Interest cost	4,584	3,587
Expected return on plan assets	(7,725)	(7,088)
Amortization of prior service credit	(126)	(126)
Recognized net actuarial loss	2,314	2,729
Net periodic benefit cost	<u>\$ 4,872</u>	<u>\$ 4,228</u>

Net amounts recognized in unrestricted net assets that have not been recognized in net periodic benefit cost are as follows:

	<b>2016</b>	<b>2015</b>
Net actuarial loss	\$ 45,808	\$ 29,420
Prior service credit	(63)	(189)
Total recognized in unrestricted net assets	<u>\$ 45,745</u>	<u>\$ 29,231</u>

The estimated net actuarial loss and prior service credit for the Plan that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are \$2,796 and \$(63), respectively.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**11. Pension Plan (continued)**

Weighted average assumptions used to determine projected benefit obligations and net periodic benefit costs at June 30 were as follows:

	<u>2016</u>	<u>2015</u>
<b>Projected benefit obligation</b>		
Discount rate	<b>3.15%</b>	4.00%
Rates of increase in compensation levels:		
Service:		
<11	<b>8.00</b>	8.00
11<21	<b>5.00</b>	5.00
21=<	<b>3.00</b>	3.00
<b>Net periodic benefit cost</b>		
Discount rate	<b>4.00</b>	3.50
Expected long-term return on plan assets	<b>7.00%</b>	7.00%
Rate of increase in compensation levels:		
Service:		
<11	<b>8.00</b>	8.00
11<21	<b>5.00</b>	5.00
21=<	<b>3.00</b>	3.00

The defined benefit pension plan asset allocation as of the measurement date and the target asset allocation, presented as a percentage of total plan assets, were as follows:

	<u>2016</u>	<u>2015</u>	<u>Target Allocation</u>
Debt securities	<b>27%</b>	27%	25%–40%
Equity securities	<b>70</b>	70	45%–75%
Cash and cash equivalents	<b>3</b>	3	1%–10%
Total	<b>100%</b>	100%	

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **11. Pension Plan (continued)**

The Health System's defined benefit plan invests in a diversified mix of traditional asset classes. Investments in U.S. equity securities and fixed income securities are made to maximize long-term results while recognizing the need for adequate liquidity to meet ongoing benefit and administrative obligations. Risk tolerance of unexpected investment and actuarial outcomes is continually evaluated by understanding the pension plan's liability characteristics. This is performed through forecasting and assessing ranges of investment outcomes over short-term and long-term horizons, and by assessing the Health System's financial condition and its future potential obligations from both the pension and general operational requirements. Complementary investment styles, such as growth and value equity investing techniques, are utilized by the Health System's investment advisors to further improve portfolio and operational risk characteristics. Equity investments, both actively and passively managed, are used primarily to increase overall plan returns. Fixed income investments provide diversification benefits and liability hedging attributes that are desirable, especially in falling interest rate environments.

Asset allocations and investment performance are formally reviewed at regularly scheduled meetings of the Health System's Financial Resources Committee.

The overall rate of expected return on assets assumption was based on historical returns, with adjustments made to reflect expectations of future returns. The extent to which the future expectations were recognized included the target rates of return for the future, which have not historically changed.

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)  
*(Dollar Amounts in Thousands)*

**11. Pension Plan (continued)**

The fair values of the Health System's pension plan assets as of June 30, by asset category (see Note 10, *Fair Value Measurements*, for a description of the asset categories), are as follows:

	2016			
	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Investments at fair value:				
Cash and cash equivalents	\$ 3,621	\$ —	\$ —	\$ 3,621
U.S. Treasuries	7,021	—	—	7,021
Government-sponsored mortgage-backed securities	—	8,875	—	8,875
Corporate debt securities	—	16,419	—	16,419
Publicly traded equity securities	81,870	—	—	81,870
Other	319	—	—	319
Total investments	<u>\$ 92,831</u>	<u>\$ 25,294</u>	<u>\$ —</u>	<u>\$ 118,125</u>
	2015			
	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Investments at fair value:				
Cash and cash equivalents	\$ 4,057	\$ —	\$ —	\$ 4,057
U.S. Treasuries	6,746	—	—	6,746
Government-sponsored mortgage-backed securities	—	9,253	—	9,253
Corporate debt securities	—	15,523	—	15,523
Publicly traded equity securities	83,491	—	—	83,491
Other	341	—	—	341
Total investments	<u>\$ 94,635</u>	<u>\$ 24,776</u>	<u>\$ —</u>	<u>\$ 119,411</u>

Peninsula Regional Health System, Inc.

Notes to Consolidated Financial Statements (continued)

(Dollar Amounts in Thousands)

**11. Pension Plan (continued)**

The following methods and assumptions were used to estimate fair value of each class of financial instrument:

*U.S. Treasuries:* The fair value is determined by an active price for an identical security in an observable market.

*Corporate debt securities and government-sponsored mortgage-backed securities:* The fair value is estimated using quoted prices for similar assets in active markets or quoted prices for identical or similar assets in non-active markets (few transactions, limited information, noncurrent prices, and high variability over time).

*Money market funds:* The carrying value of these money market funds approximates fair value as the maturities are less than three months.

*Publicly traded equity securities:* The fair value is determined by market quotes for an identical security in an observable market.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Health System 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.

**Cash Flows**

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows for the years ending June 30:

2017	\$	6,701
2018		8,032
2019		8,044
2020		8,254
2021		9,179
2022–2026		48,868

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **11. Pension Plan (continued)**

The Health System intends to make voluntary contributions to the defined benefit pension plan of \$3,000 for the year ending June 30, 2017. This funding level exceeds any regulatory requirements for 2017.

#### **12. Commitments and Contingencies**

##### **Agreement With the Office of Inspector General**

The Health System received several subpoenas from the Office of Inspector General of the U.S. Department of Health and Human Services (OIG), requiring the production of certain documents related to claims for physician health care services provided by a former medical staff member. These subpoenas were issued in connection with a civil investigation being conducted by the U.S. Attorney's Office for the District of Maryland. In January 2011, the Health System reached a tentative agreement in principle, which was ultimately approved by the U.S. Department of Justice, the OIG, the Office of Personnel Management, and the state of Maryland in August 2011, to resolve all remaining potential civil claims arising out of the Health System's medical services to patients of the physician. The Health System reached this agreement without admitting liability in order to avoid the expense and uncertainty of litigation and to allow the Health System to move forward. In this regard and consistent with the settlement, an amount of \$1,800 was paid in June 2011. The settlement also includes a five-year Corporate Integrity Agreement that will require the Health System to establish and/or enhance various compliance processes and also have several independent peer review reports completed on an annual basis.

##### **Other**

The Health System has been named as a defendant in various lawsuits arising from the performance of its normal activities. In the opinion of the Health System's management, after discussion with legal counsel, the amount, if any, of the Health System's ultimate liability under these lawsuits will not have a material adverse effect on the consolidated financial position of the Health System.

A portion of the Health System's revenues is received from health maintenance organizations and other managed care payors. Managed care payors generally use case management activities to control utilization. These payors also have the ability to select providers offering the most cost-effective care. Management does not believe that the organization has undue exposure to any one managed care payor.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **12. Commitments and Contingencies (continued)**

The Health System's revenues may be subject to adjustment as a result of examination by government agencies or contractors based upon differing interpretation of government regulations, medical diagnosis, charge coding, medical necessity, or other contract terms. The resolution of these matters, if any, often is not finalized until subsequent to the period during which the services were rendered. Section 302 of the Tax Relief and Health Care Act of 2006 authorized a permanent program involving the use of third-party recovery audit contractors (RACs) to identify Medicare overpayments and underpayments made to providers. The Health System has established protocols to respond to RAC requests and payment denials. Payment recoveries resulting from RAC reviews are appealable through administrative and judicial processes, and the Health System intends to pursue the reversal of adverse determinations where appropriate. In addition to overpayments that are not reversed on appeal, the Health System will incur additional costs to respond to requests for records and pursue the reversal of payment denials. As of June 30, 2016 and 2015, the Health System has recorded an estimated reserve regarding the Medicare overpayments. In the opinion of the Health System's management, the ultimate settlement of this matter will not have a material adverse effect on the consolidated financial position of the Health System.

As part of a national investigation, the Health System has been working with the Department of Justice (DOJ) regarding the Medicare programs' coverage guidelines for the implantation of implantable cardioverter defibrillators. On June 15, 2015, the Health System executed a settlement agreement with the DOJ for \$2,910. Upon settlement, the Health System accrued the settlement balance as accrued liabilities. Payment was made in July 2015.

On June 22, 2012, the Health System filed a self-disclosure to CMS, reporting technical violations of the self-referral regulations (referred to as Stark). As of June 30, 2016, the Health System does not believe the settlement of this issue will have a material adverse effect on its consolidated financial statements.

#### **Operating Leases**

The Health System leases certain of its operating facilities and equipment. These leases, which expire through 2028, generally require the Health System to pay all maintenance, property tax, and insurance costs.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **12. Commitments and Contingencies (continued)**

At June 30, 2016, aggregate amounts of future minimum payments under operating leases were as follows:

2017	\$	2,219
2018		2,041
2019		1,705
2020		1,333
2021 and thereafter		7,567

Rent expense is recognized on a straight-line basis over the terms of the leases. Rent expense was \$2,695 and \$2,400 for the years ended June 30, 2016 and 2015, respectively.

#### **13. Maryland Health Services Cost Review Commission**

Certain hospital charges are subject to review and approval by the Maryland Health Services Cost Review Commission (the Commission). Hospital management has filed the required forms with the Commission and believes the Hospital to be in compliance with Commission requirements.

The current rate of reimbursement for principally all inpatient services and certain other services to patients under the Medicare and Medicaid programs is based on an agreement between CMS and the Commission. This agreement is based upon a waiver from Medicare prospective payment system reimbursement principles granted to the state of Maryland under Section 1814(b) of the Social Security Act. As of January 2014, the CMS approved a modernized waiver that will be in place as long as Maryland hospitals commit to achieving significant quality improvements, limits on all-payer capita hospital growth, and limits on annual Medicare per capita hospital cost growth to a rate lower than the national annual per capita growth rate. This model is projected to save Medicare at least \$330,000 over the next five years.

Beginning in fiscal year 2014, the Hospital entered into an agreement with the Commission to participate in the Global Budgeted Revenue (GBR) program. GBR methodology encourages hospitals to focus on population health strategies by establishing a fixed annual revenue cap for each GBR hospital. The agreement is evergreen in nature and covers both regulated inpatient and outpatient revenues.

## Peninsula Regional Health System, Inc.

### Notes to Consolidated Financial Statements (continued)

*(Dollar Amounts in Thousands)*

#### **13. Maryland Health Services Cost Review Commission (continued)**

Under GBR, hospital revenue is known at the beginning of each fiscal year. Annual revenue is calculated from a base year and is adjusted annually for inflation, infrastructure requirements, population changes, performance in quality-based programs, and changes in levels of uncompensated care. Revenue may also be adjusted annually for market levels and shifts of services to unregulated services.

The Commission's rate-setting methodology for hospital service centers that provide both inpatient and outpatient services or only outpatient services consists of establishing an acceptable unit rate for defined inpatient and outpatient service centers within a hospital. The actual average unit charge for each service center is compared to the approved rate monthly and annually. Overcharges and undercharges due to either patient volume or price variances, adjusted for 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 Hospital undercharged by \$122 as of June 30, 2016, which is within the allowable corridor as specified in the GBR Agreement.

The timing of the Commission's rate adjustments for the Hospital could result in an increase or reduction in rates due to the variances and penalties described above in a year subsequent to the year in which such items occur, and there is at least a possibility that the amounts may be material. The Hospital's policy is to record revenue based on actual charges for services to patients in the year in which the services are performed. The Hospital recognizes unbilled revenue for in-house patient services.

#### **14. Subsequent Events**

The Health System has evaluated subsequent events through September 23, 2016, the date the accompanying consolidated financial statements were issued.

# Supplementary Information

Peninsula Regional Health System, Inc.

Consolidating Balance Sheet

(In Thousands)

June 30, 2016

	Peninsula Regional Medical Center	Peninsula Regional Medical Center Foundation, Inc.	Peninsula Health Ventures, Inc.	Peninsula Regional Clinically Integrated Network	Peninsula Surgery Center	Peninsula Regional Health System, Inc.	Eliminations	Consolidated
<b>Assets</b>								
Current assets:								
Cash and cash equivalents	\$ 29,256	\$ 1,166	\$ 6,316	\$ 1	\$ 1	\$ 15	\$ -	\$ 36,755
Short-term investments	6,760	-	-	-	-	-	-	6,760
Intercompany receivables	341	-	-	-	-	-	(341)	-
Accounts receivable, less allowance for uncollectible accounts	41,520	-	714	-	-	-	-	42,234
Inventories and other	9,888	-	338	-	-	-	-	10,226
Prepays	6,276	-	51	-	-	-	-	6,327
Total current assets	94,041	1,166	7,419	1	1	15	(341)	102,302
Long-term investments	226,353	-	-	-	-	-	-	226,353
Investment in subsidiaries	-	-	-	-	-	435,743	(435,743)	-
Board-designated investments	23,584	-	-	-	-	-	-	23,584
Assets limited as to use:								
Construction fund	10,228	-	-	-	-	-	-	10,228
Donor-restricted fund	33,217	7,000	-	-	-	-	(7,000)	33,217
Self-insurance fund	19,713	-	-	-	-	-	-	19,713
Total assets limited as to use	63,158	7,000	-	-	-	-	(7,000)	63,158
Property and equipment, net	220,671	-	3,708	-	464	-	-	224,843
Unamortized financing costs, net of accumulated amortization	1,310	-	39	-	-	-	-	1,349
Other assets	10,145	-	9,414	-	-	104	-	19,663
Total assets	\$ 639,262	\$ 8,166	\$ 20,580	\$ 1	\$ 465	\$ 435,862	\$ (443,084)	\$ 661,252

Peninsula Regional Health System, Inc.

Consolidating Balance Sheet (continued)

(In Thousands)

June 30, 2016

	Peninsula Regional Medical Center	Peninsula Regional Medical Center Foundation, Inc.	Peninsula Health Ventures, Inc.	Peninsula Regional Clinically Integrated Network	Peninsula Surgery Center	Peninsula Regional Health System, Inc.	Eliminations	Consolidated
<b>Liabilities and net assets</b>								
Current liabilities:								
Current portion of long-term debt	\$ 1,990	\$ -	\$ 78	\$ -	\$ -	\$ -	\$ -	\$ 2,068
Current portion of accrued self-insured liabilities	2,495	-	-	-	-	-	-	2,495
Intercompany payables	-	-	9	39	20	273	(341)	-
Accounts payable	17,724	-	364	-	-	-	-	18,088
Accrued liabilities	14,936	-	-	-	-	-	-	14,936
Advances from third-party payors	11,401	-	-	-	-	-	-	11,401
Total current liabilities	48,546	-	451	39	20	273	(341)	48,988
Long-term debt, net	141,624	-	1,695	-	-	-	-	143,319
Other liabilities	38,537	-	-	-	-	-	-	38,537
Total liabilities	228,707	-	2,146	39	20	273	(341)	230,844
Net assets:								
Unrestricted	377,252	1,166	16,616	(38)	445	395,285	(395,439)	395,287
Temporarily restricted	25,058	7,000	-	-	-	32,059	(39,059)	25,058
Permanently restricted	8,245	-	-	-	-	8,245	(8,245)	8,245
Peninsula Regional Health System, Inc. net assets	410,555	8,166	16,616	(38)	445	435,589	(442,743)	428,590
Minority interest	-	-	1,818	-	-	-	-	1,818
Total net assets	410,555	8,166	18,434	(38)	445	435,589	(442,743)	430,408
Total liabilities and net assets	\$ 639,262	\$ 8,166	\$ 20,580	\$ 1	\$ 465	\$ 435,862	\$ (443,084)	\$ 661,252

Peninsula Regional Health System, Inc.

Consolidating Statement of Operations

(In Thousands)

Year Ended June 30, 2016

	Peninsula Regional Medical Center	Peninsula Regional Medical Center Foundation, Inc.	Peninsula Health Ventures, Inc.	Peninsula Regional Clinically Integrated Network	Peninsula Surgery Center	Peninsula Regional Health System, Inc.	Eliminations	Consolidated
Unrestricted revenue and other support:								
Net patient service revenue	\$ 413,532	\$ –	\$ 4,891	\$ –	\$ –	\$ –	\$ –	\$ 418,423
Provision for bad debts	(11,449)	–	(28)	–	–	–	–	(11,477)
Net patient service revenue less provision for bad debts	402,083	–	4,863	–	–	–	–	406,946
Other operating revenue	2,739	–	10	–	–	–	–	2,749
Net assets released from restrictions	–	271	–	–	–	–	(271)	–
Total unrestricted revenue and other support	404,822	271	4,873	–	–	–	(271)	409,695
Operating expenses:								
Salaries and wages	165,766	–	–	–	–	–	–	165,766
Supplies and other expenses	177,927	4	5,909	451	287	–	–	184,578
Employee benefits	34,429	–	–	–	–	–	–	34,429
Depreciation	22,554	–	250	–	–	–	–	22,804
Interest	4,964	–	88	–	–	–	–	5,052
Contributions to Hospital	–	271	–	–	–	–	(271)	–
Total operating expenses	405,640	275	6,247	451	287	–	(271)	412,629
Loss from operations	(818)	(4)	(1,374)	(451)	(287)	–	–	(2,934)
Nonoperating income (expense):								
Investment income	7,655	3	3,201	–	–	(169)	–	10,690
Loss on extinguishment of debt	–	–	–	–	–	–	–	–
Total nonoperating income	7,655	3	3,201	–	–	(169)	–	10,690
Excess (deficit) of unrestricted revenue and other support over expenses	6,837	(1)	1,827	(451)	(287)	(169)	–	7,756
Minority interest in earnings of controlled subsidiaries	–	–	(31)	–	–	–	–	(31)
Excess (deficit) of unrestricted revenue and other support over expenses attributable to PRHS	\$ 6,837	\$ (1)	\$ 1,796	\$ (451)	\$ (287)	\$ (169)	\$ –	\$ 7,725

**About EY**

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit [ey.com](http://ey.com).

© 2016 Ernst & Young LLP.  
All Rights Reserved.

**[ey.com](http://ey.com)**

