Consolidated Financial Statements and Supplementary Information

Frederick Health, Inc. and Subsidiaries
Years Ended June 30, 2023 and 2022
With Report of Independent Auditors

Ernst & Young LLP

Building a better working world

Frederick Health, Inc. and Subsidiaries

Consolidated Financial Statements
and Supplementary Information

Years Ended June 30, 2023 and 2022

Contents

Ernst & Young LLP
Suite 310
1201 Wills Street
Baltimore, MD 21231

Tel: +1 410 539 7940
Fax: +1 410 783 3832
ey.com

Report of Independent Auditors

The Board of Directors
Frederick Health, Inc. and Subsidiaries

Opinion

We have audited the consolidated financial statements of Frederick Health, Inc. and Subsidiaries (the System), which comprise the consolidated balance sheets as of June 30, 2023 and 2022, and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes (collectively referred to as the financial statements).

In our opinion, based on our audits and the report of other auditors, the accompanying financial statements present fairly, in all material respects, the financial position of the System at June 30, 2023 and 2022, and the results of its operations, changes in net assets, and its cash flows for the years then ended in accordance with the accounting principles generally accepted in the United States of America.

We did not audit the financial statements of Monocacy Insurance, Ltd., a wholly owned subsidiary, which statements reflect total assets of $23,431 and $25,657 as of June 30, 2023 and 2022, respectively, and net loss after elimination of intercompany revenues of $2,052 and $3,313, respectively for the years then ended (stated in thousands). 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 Monocacy Insurance, Ltd., is based solely on the report of the other auditors.

Basis for Opinion

We have conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the System and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the System's ability to continue as a going concern for one year after the date that the financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 System's internal control. Accordingly, no such opinion is expressed.

- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.

- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the System's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal-control-related matters that we identified during the audit.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary consolidating and combining/combined 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 audits of the 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 of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Ernst + Young LLP

October 16, 2023

Frederick Health, Inc. and Subsidiaries

Consolidated Balance Sheets

(In Thousands)

	June 30	
	2023	**2022**
Assets		
Current assets:		
Cash and cash equivalents	**$ 20,414**	$ 32,267
Patient receivables	**76,459**	70,954
Other receivables	**5,154**	2,629
Inventory	**11,231**	10,993
Prepaid expenses	**6,592**	5,890
Assets limited as to use	**6,196**	6,409
Promises to give, net	**675**	730
Total current assets	**126,721**	129,872
Net property and equipment	**303,662**	287,076
Right-of-use assets, net	**27,945**	28,261
Other assets:		
Assets limited as to use	**2,853**	3,047
Investments – donor restricted	**3,416**	6,378
Promises to give, net	**3,894**	5,196
Long-term investments	**188,020**	184,844
Other investments	**19,636**	21,744
Other assets	**12,613**	9,146
Total other assets	**230,432**	230,355
Total assets	**$ 688,760**	$ 675,564

2305-4251357

	June 30	
	2023	**2022**
Liabilities and net assets		
Current liabilities:		
Current maturities of long-term debt	**$ 2,494**	$ 6,095
Accounts payable	**44,559**	33,432
Accrued expenses	**27,901**	33,715
Advances from third-party payors	**11,333**	22,189
Leases, current	**3,619**	3,258
Other current liabilities	**7,477**	8,297
Total current liabilities	**97,383**	106,986
Long-term liabilities, net of current portion:		
Long-term debt	**236,981**	196,363
Interest rate swap contract	**–**	3,515
Other long-term liabilities	**31,318**	34,763
Leases, long term	**28,321**	29,780
Total long-term liabilities, net of current portion	**296,620**	264,421
Total liabilities	**394,003**	371,407
Net assets:		
Without donor restrictions	**286,211**	291,854
With donor restrictions	**7,985**	12,303
Noncontrolling interest	**561**	–
Total net assets	**294,757**	304,157
Total liabilities and net assets	**$ 688,760**	$ 675,564

See accompanying notes.

Frederick Health, Inc. and Subsidiaries

Consolidated Statements of Operations and Changes in Net Assets

(In Thousands)

	Year Ended June 30	
	2023	**2022**
Operating revenues:		
Net patient service revenue	**$ 491,379**	$ 477,343
Other revenue	**22,501**	19,221
Total operating revenues	**513,880**	496,564
Operating expenses:		
Salaries and wages	**257,872**	238,232
Employee benefits	**51,917**	53,099
Professional fees	**10,818**	10,957
Cost of goods sold	**89,595**	81,661
Supplies	**15,507**	16,590
Contract services	**56,570**	58,187
Other	**15,954**	15,721
Utilities	**5,002**	6,294
Insurance	**5,360**	2,203
Depreciation and amortization	**32,908**	29,672
Interest	**6,285**	4,728
Total operating expenses	**547,788**	517,344
Loss from operations	**(33,908)**	(20,780)
Other income (loss), net:		
Gain on sale of assets	**3**	6
Loss on extinguishment of debt	**(268)**	–
Investment gain, net	**11,180**	8,236
Change in unrealized gains (losses) on trading securities, net	**5,088**	(31,418)
Realized losses and unrealized gains on interest rate swap contract, net	**939**	2,601
Periodic pension credit	**–**	1,829
Other nonoperating gains, net	**3,801**	6,560
Total other income (loss), net	**20,743**	(12,186)
Deficit of revenue over expenses	**(13,165)**	(32,966)
Less noncontrolling interest	**47**	–
Deficit of revenue over expenses	**$ (13,118)**	$ (32,966)

Continued on page 7.

Frederick Health, Inc. and Subsidiaries

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

	Without Donor Restrictions	With Donor Restrictions	Noncontrolling Interest	Total
Net assets, June 30, 2021	$ 319,753	$ 9,783	$ –	$ 329,536
Deficit of revenue over expenses	(32,966)	–	–	(32,966)
Pension adjustment	220	–	–	220
Released from restriction used to purchase capital	4,847	(4,847)	–	–
Assets released from restrictions	–	(4,320)	–	(4,320)
Restricted gifts, bequests, and contributions	–	11,687	–	11,687
Changes in net assets	(27,899)	2,520	–	(25,379)
Net assets, June 30, 2022	291,854	12,303	–	304,157
Deficit of revenue over expenses	**(13,165)**	**–**	**47**	**(13,118)**
Noncontrolling equity interest related to business acquisition	**4,621**	**–**	**514**	**5,135**
Released from restriction used for operations and nonoperating activities	**–**	**(4,651)**	**–**	**(4,651)**
Released from restriction used to purchase capital	**2,636**	**(2,636)**	**–**	**–**
Restricted gifts, bequests, and contributions	**–**	**2,969**	**–**	**2,969**
Other changes	**265**	**–**	**–**	**265**
Changes in net assets	**(5,643)**	**(4,318)**	**561**	**(9,400)**
Net assets, June 30, 2023	**$ 286,211**	**$ 7,985**	**$ 561**	**$ 294,757**

See accompanying notes.

Frederick Health, Inc. and Subsidiaries

Consolidated Statements of Cash Flows
(In Thousands)

	Year Ended June 30	
	2023	**2022**
Operating activities		
Changes in net assets	**$ (9,400)**	$ (25,379)
Adjustments to reconcile changes in net assets to net cash used in operating activities:		
Depreciation of property and equipment	**32,908**	29,672
Loss on extinguishment of debt	**268**	–
Noncash pension adjustment	**–**	(220)
Amortization of premium and deferred financing	**(43)**	(368)
Equity in earnings of joint ventures	**(4,045)**	(6,070)
Noncash gain from acquisition	**(3,071)**	–
Unrealized losses (gains) and realized losses (gains) on unrestricted investments	**(17,334)**	28,464
Proceeds from restricted contributions	**(5,595)**	(7,530)
Change in fair value of interest rate swap, net of realized losses	**(939)**	(2,601)
Increase (decrease) in:		
Receivables, patient and other	**(7,231)**	(2,124)
Inventories and prepaids	**(443)**	(2,174)
Pledges receivable	**1,357**	(841)
Other assets	**1,251**	(340)
Accounts payable	**11,575**	3,061
Accrued expenses	**(6,042)**	(349)
Accrued pension expense	**–**	–
Advances from third-party payors	**(10,856)**	(41,851)
Other short-term liabilities	**(1,172)**	60
Other long-term liabilities	**(5,847)**	(221)
Net cash used in operating activities	**(24,659)**	(28,811)
Investing activities		
Realized losses on interest rate swap contract	**(2,576)**	(1,550)
Other investments	**3,724**	38
Acquisition, net	**(1,103)**	–
Purchases of property and equipment	**(47,194)**	(51,915)
Net sales (purchases) of long-term investments and assets limited as to use	**19,742**	(4,516)
Net cash used in investing activities	**(27,407)**	(57,943)

Frederick Health, Inc. and Subsidiaries

Consolidated Statements of Cash Flows (continued)
(In Thousands)

	Year Ended June 30	
	2023	**2022**
Fundraising and financing activities		
Proceeds from restricted contributions	**$ 5,595**	$ 7,530
Repayments of long-term debt	**(71,015)**	(4,875)
Proceeds from borrowings	**108,741**	10,000
Payments for finance leases	**(2,058)**	(1,624)
Deferred financing costs paid	**(1,263)**	(84)
Net cash provided by fundraising and financing activities	**40,000**	10,947
Net decrease in cash, cash equivalents, and restricted cash	**(12,066)**	(75,807)
Cash, cash equivalents, and restricted cash at the beginning of the year	**38,676**	114,483
Cash, cash equivalents, and restricted cash at the end of the year	**$ 26,610**	$ 38,676
Cash and cash equivalents	**$ 20,414**	$ 32,267
Restricted cash, included in assets limited as to use	**6,196**	6,409
	$ 26,610	$ 38,676
Supplemental disclosures		
Cash paid for interest	**$ 4,436**	$ 4,728

See accompanying notes.

1. Organization and Mission

Frederick Health, Inc. (the System) is a not-for-profit parent corporation formed on June 23, 2011, exempt from income tax under Section 501(a) of the Internal Revenue Code (the Code) as an organization described in Section 501(c)(3) whereby only unrelated business income as defined by Section 512(a)(1) of the Code is subject to federal income tax. The System has received a determination letter from the Internal Revenue Service (IRS) stating that it is exempt from federal income taxes under Section 501(c) of the Code.

Frederick Health Hospital, Inc. (the Hospital) is a not-for-profit hospital, exempt from federal income tax under Section 501(a) of the Code as an organization described in Section 501(c)(3) whereby only unrelated business income as defined by Section 512(a)(1) of the Code is subject to federal income tax. The Hospital is located in Frederick, Maryland, and provides health care services primarily to residents of Frederick County. The Hospital has received a determination letter from the IRS stating that it is exempt from federal income taxes under Section 501(c) of the Code.

Monocacy Insurance, Ltd. (MIL) is a Cayman Islands-domiciled single-parent captive incorporated on May 24, 2011, and holds an Unrestricted Class B insurance license issued under Section 7(2) of the Cayman Island Insurance Law. MIL directly provides primary medical professional liability, primary general liability coverage, and cyber liability coverage to the System.

Frederick Health Medical Group, LLC (the Medical Group) serves as a physician enterprise, providing governance, management, and support functions for employed physicians. The Medical Group is a not-for-profit corporation, formed on June 23, 2011, and operational as of October 1, 2013, exempt from income tax under Section 501(a) of the Code as an organization described in Section 501(c)(3) whereby only unrelated business income as defined by Section 512(a)(1) of the Code is subject to federal income tax. The Medical Group has received a determination letter from the IRS stating that it is exempt from federal income taxes under Section 501(c) of the Code.

Frederick Health Services Corporation (FHSC) is a Maryland for-profit corporation, all of the stock of which is owned by the System. FHSC is subject to federal and state income taxes.

1. Organization and Mission (continued)

On March 25, 2014, Frederick Integrated Healthcare Network, LLC (FIHN) was formed and is operated exclusively as a charitable organization for charitable, scientific, and educational purposes within the meaning of Section 501(c)(3) of the Code and the Regulations thereunder as they now exist or as they may hereafter be amended. FIHN was formed to maintain and operate a program of clinical integration and an accountable care organization among health care providers.

In October 2019, the System purchased 100% of the membership interests of Frederick View, LLC, a Maryland limited liability company. The sole asset of Frederick View, LLC was real property consisting of an approximately 94-acre parcel of land with an approximately 387,000-square-foot building, which was formerly used by an insurance company. On December 2, 2019, the Articles of Organization of Frederick View, LLC were amended for the purpose of changing the name of Frederick View, LLC to Frederick Health Village, LLC (the Village).

On December 16, 2021, Frederick Health Community Enterprises, LLC (FHCE) was formed and is operated exclusively as a charitable organization for charitable, scientific, and educational purposes within the meaning of Section 501(c)(3) of the Code and the Regulations thereunder as they now exist or as they may hereafter be amended. FHCE was formed for the benefit of, and to advance the interests of, the System.

The Obligated Group, consisting of the Hospital, Medical Group, and the System, is responsible for repayment of the Maryland Health and Higher Education Facilities Authority (MHHEFA) Series Bonds, Promissory Note 2020 and any outstanding amount on the 2013 Line of Credit. Refer to Note 9 for additional information on long-term debt.

Global Pandemic

On March 11, 2020, the World Health Organization designated COVID-19 as a global pandemic. The impact of COVID-19 on operations and financial results depends upon many factors, many of which could be beyond the System's ability to control or predict.

As a result of the global pandemic, the Maryland Health Services Cost Review Commission (HSCRC or the Commission) has publicly announced its intention to support Maryland hospitals during the state of emergency and catastrophic health emergency within the state of Maryland and its collaboration with other Maryland regulatory agencies to remove licensure, regulatory, and

1. Organization and Mission (continued)

other barriers to hospitals in the provision of emergency health care services. Recognizing that hospitals experienced volume decline due to self-quarantining and canceled elective surgeries, the HSCRC permitted Maryland hospitals to increase rate corridors up to the 10% threshold or by an additional 5% from their current charging position, whichever is greater, for the years ended June 30, 2023 and 2022, to stabilize hospital revenue.

In response to COVID-19, the Coronavirus Aid, Relief, and Economic Security (CARES) Act and the American Rescue Plan Act of 2021 (ARPA) were signed into law on March 27, 2020 and March 11, 2021, respectively. The CARES Act and ARPA authorized funding to hospitals and other health care providers to be distributed through the Public Health and Social Services Emergency Fund (Relief Fund) and the Local Fiscal Recovery Fund. Payments from the Relief Fund were to be used to prevent, prepare for, and respond to coronavirus, and shall reimburse the recipient for health-care-related expenses or lost revenues attributable to coronavirus and are not required to be repaid, provided the recipients attest to and comply with the terms and conditions. In addition to the relief funding, the CARES Act provided for an expansion of the Medicare Accelerated and Advance Payment Program whereby inpatient acute care hospitals and other eligible providers were able to request accelerated payment of up to 100% of their Medicare payment amount for a six-month period to be repaid through withholding of future Medicare fee-for-service payments. The System's accounting policies for the recognition of the funding received are discussed within Note 2.

Effective May 11, 2023, the COVID-19 public health emergency ended. The System will continue to monitor COVID-19 case rates and how those cases impact the System's operations.

2. Significant Accounting Policies

Principles of Consolidation

The accompanying consolidated financial statements include the accounts and transactions of the System and its wholly owned subsidiaries: the Hospital, MIL, FHSC, the Medical Group, FIHN, FHCE, and the Village.

2. Significant Accounting Policies (continued)

The Hospital has one wholly owned subsidiary, Frederick Health Hospice, LLC (Hospice), an independent 501(c)(3) organization controlled by the Hospital, operates as a fundraising organization for the benefit of hospice services and owns the Kline Hospice House.

FHSC has two wholly owned subsidiaries: Rosehill of Frederick, LLC and Frederick Health Employer Solutions, LLC, both of which are for-profit limited liability companies that have been consolidated with FHSC into the System in the accompanying consolidated financial statements.

The accompanying consolidated financial statements include the accounts of the System and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP).

Donor-Restricted Gifts

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift becomes unconditional. Contributions are reported as net assets with donor restrictions 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, the net assets with donor restrictions are reclassified as net assets without donor restrictions and changes in net assets as net assets released from restrictions. Such amounts are classified as other revenue or transfers and additions to property and equipment. Donor-restricted contributions whose restrictions are met within the same year as received and contributions received where no restrictions were stipulated are reflected as contributions without donor restrictions. Contributed nonfinancial assets received from donors are subsequently monetized.

2. Significant Accounting Policies (continued)

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid financial instruments with an original maturity of three months or less, excluding assets limited as to use and those classified as long-term investments. Cash and cash equivalent balances may exceed amounts insured by federal agencies and, therefore, bear a risk of loss. The System has not experienced such losses on these funds.

Other Revenue

Other revenue consists primarily of other operating revenue as well as gifts, bequests, and contributions. The System follows grant accounting to recognize the stimulus funding as other operating revenue.

Inventory

Inventory, consisting primarily of drugs and medical and surgical supplies, is stated at the lower of cost or net realizable value. Cost is determined using the first-in, first-out method.

Cost of Goods Sold

Cost of goods sold consists primarily of drugs, medical supplies, and surgical implants used in the care and treatment of patients.

Investments and Assets Limited as to Use

The fair values of individual investments, excluding private equity investments and hedge funds, are based on quoted market prices of individual securities or investments or estimated amounts using quoted market prices of similar investments. Private equity investments and hedge funds are recorded based on net asset value of these investments, which is discussed further in Note 7, Fair Value Measurements. Realized and unrealized investment returns from all unrestricted investments and assets limited as to use are included on the accompanying consolidated statements of operations as part of nonoperating gains and losses.

2. Significant Accounting Policies (continued)

Long-term investments represent investments without donor restrictions and income earned on investments with and without donor restrictions. The cost of securities sold is based on the specific-identification method. Investments are classified as either current or noncurrent based on maturity dates and availability for current operations.

Substantially all of the System's investment portfolio (excluding certain assets limited as to use, private equity investments, and hedge funds) is classified as trading, with unrealized gains and losses included in (deficit) excess of revenue over expenses. Certain trusteed assets that are included in assets limited as to use are classified as other than trading. These assets primarily consist of funds held for payment of principal and interest on bonds and deferred compensation trusts.

Investment Risk and Liquidity Management

The System invests in professionally managed portfolios that contain corporate obligations, U.S. government obligations, agency securities, mortgage-backed securities, marketable equity securities, hedge funds, money market funds, and private equity investments. Such investments are exposed to various risks, such as interest rate, market, and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term would materially affect investment balances and the amounts reported in the accompanying consolidated financial statements.

As part of its liquidity management, the System's strategy is to structure its financial assets to be available to satisfy general operating expenses, current liabilities, and other obligations as they come due. The System has a committed line of credit, as discussed in Note 9, to help manage unanticipated liquidity needs.

Property and Equipment

Property and equipment are carried at cost or estimated fair value at date of contribution, less accumulated depreciation. Items acquired by gift are recorded at fair value at the time of acquisition. Depreciation is recorded using the straight-line method over the estimated useful lives of the depreciable assets. Leasehold improvements are amortized using the straight-line method over the shorter of the lease term or the estimated useful lives of the assets.

2. Significant Accounting Policies (continued)

Leases

The System enters into lease agreements for equipment, office space, and certain facilities in conducting its normal business operations. Operating leases are included in long-term right-of-use assets, current lease liability, and long-term lease liability on the accompanying consolidated balance sheets. Finance leases are included in net property and equipment, other current liabilities, and other long-term liabilities on the accompanying consolidated balance sheets.

Right-of-use assets represent the System's right to use an underlying asset for the lease term and lease liabilities represent its obligation to make lease payments arising from the lease. At the inception of any contract, the System evaluates the agreement to determine whether the contract contains a lease. If the contract contains a lease, the System then evaluates the term and whether the lease is an operating or a finance lease. Most leases include one or more options to renew or may have a termination option. The System determines whether these options are reasonably certain to be exercised at the inception of the lease. The depreciable life of right-of-use assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option that is reasonably certain to be exercised at the inception of the lease. The lease expense is recognized on a straight-line basis on the accompanying consolidated statements of operations and changes in net assets over the terms of the respective leases. Leases with an initial term of 12 months or less are not recorded on the accompanying consolidated balance sheets.

Topic 842 includes an accounting policy election for nonpublic business entities to use the risk-free rate for the measurement of lease liabilities. The System elected to utilize the risk-free rate for the measurement of lease liabilities. At the commencement date, the lease liability is measured at the present value of the lease payments that are not paid at that date. The lease liability is subsequently increased by interest expense recognized and reduced by lease payments made. The System also elected the practical expedient that allows the System to treat the lease and non-lease components of a contract as a single component and account for as a lease.

2. Significant Accounting Policies (continued)

Valuation of Long-Lived Assets

The System accounts for the valuation of long-lived assets under Accounting Standards Codification (ASC) 360-10-45, *Accounting for the Impairment or Disposal of Long-Lived Assets*. This guidance requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reportable at the lower of the carrying amount or fair value, less costs to sell.

Debt Issuance Costs

Debt issuance costs related to long-term debt issuance are being deferred and amortized over the life of the related debt using the effective-interest method and are netted in long-term debt on the accompanying consolidated balance sheets.

Net Patient Service Revenue and Patient Accounts Receivable

In accordance with ASC 606, *Revenue from Contracts with Customers*, net patient service revenue, which includes hospital inpatient services, hospital outpatient services, physician services, and other patient services revenue, is recorded at the transaction price estimated by the System to reflect the total consideration due from patients and third-party payors (including commercial payers and government programs) and others. Revenue is recognized over time as performance obligations are satisfied in exchange for providing goods and services in patient care. Revenue is recorded as these goods and services are provided. The services provided to a patient during an inpatient stay or outpatient visit represent a bundle of goods and services that are distinct and accounted for as a single performance obligation.

2. Significant Accounting Policies (continued)

The System's estimate of the transaction price includes the System's standard charges for the goods and services provided with a reduction recorded related to explicit price concessions for such items as contractual allowances, charity care, potential adjustments that may arise from payment and other reviews, and implicit price concessions such as uncollectible amounts. The price concessions are determined using the portfolio approach as a practical expedient to account for patient contracts as collective groups rather than individually. Based on historical experience, a significant portion of the self-pay population will be unable or unwilling to pay for services and only the amount anticipated to be collected is recognized in the transactions price. Subsequent changes to the estimate of the transaction price are generally recorded as adjustment to net patient service revenue in the period of change.

The standard charges for goods and services for the Hospital reflect actual charges to patients based on rates established by the HSCRC in effect during the period in which the services are rendered. See Note 18 for further discussion on the HSCRC and regulated rates.

Patient receivable includes charges for amounts due from all patients less price concessions relating to allowances for the excess of established charges over the payments to be received on behalf of patients covered by Medicare, Medicaid, and other insurers. The provision for price concessions is based upon management's assessment of historical and expected net collections considering historical business and economic conditions, trends in health care coverage, and other collection indicators. Periodically throughout the year, management assesses the adequacy of the price concessions based upon historical experience of self-pay accounts receivable, including those balances after insurance payments and not covered by insurance.

The System's revenues generally relate to contracts with patients in which the System's performance obligations are to provide health care services to patients. These revenues are based upon the estimated amounts that management expects to be entitled to receive from patients and third-party payors. Refer to Note 3 for additional information regarding the recognition of revenues in accordance with generally accepted accounting principles.

2. Significant Accounting Policies (continued)

Performance Indicator

The performance indicator is the (deficit) excess of revenue over expenses. Other changes in net assets, consistent with industry practice, include contributions of long-lived assets (including assets acquired using contributions that, by donor restrictions, were to be used for the purpose of acquiring such assets) and cumulative effect of changes in accounting principles, if any.

Fair Value of Financial Instruments

The carrying amounts reported on the accompanying consolidated balance sheets for cash and cash equivalents, other receivables, accounts payable, accrued expenses, other liabilities, and advances from third-party payors approximate their fair values.

Advances From Third-Party Payors

On May 4, 2020, the System received $60,014 from the Centers for Medicare & Medicaid Services (CMS) Accelerated and Advance Payment Program, which allowed inpatient acute care hospitals to request accelerated payments of up to 100% of their Medicare payment amount for a six-month period. Consistent with the terms and conditions of the program, repayments began in April 2021. The remaining balance to repay was $0 and $13,032 as of June 30, 2023 and 2022, respectively, which represents contract liabilities as defined in ASC 606 that have been recorded within advances from third-party payors on the accompanying consolidated balance sheets.

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

2. Significant Accounting Policies (continued)

Net Assets

Net resources that are not restricted by donors are included in net assets without donor restrictions. Gifts of long-lived operating assets, such as property, plant, or equipment, are reported as net assets with donor restrictions and excluded from income. Resources restricted by donors for a specified time or purpose are reported as net assets with donor restrictions.

When the specific purposes are met, either through passage of a stipulated time period or when the purpose for restriction is accomplished, they are released to other operating revenues on the statement of operations and changes in net assets. Resources restricted by donors for additions to property, plant, and equipment are initially reported as net assets with donor restrictions and are transferred to net assets without donor restrictions when expended. Donor-imposed restrictions, which stipulate that the resources be maintained permanently, are reported as net assets with donor restrictions.

Investment income related to net assets with donor restrictions is classified as net assets without donor restrictions based on the intent of the donor.

Recent Accounting Pronouncements

In June 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. (ASU) 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. ASU 2016-13 requires financial assets measured at amortized cost to be presented at the net amount expected to be collected. The measurement of expected credit losses is based on relevant information about past events, including historical experiences, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amounts. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. ASU 2016-13 is effective for annual reporting periods beginning after December 15, 2022, including interim periods within those fiscal years, and a modified retrospective approach is required, with a cumulative-effect adjustment to net assets as of the beginning of the first reporting period in which the guidance is effective. Management is currently evaluating the impact of adopting this new accounting guidance.

(Dollars in Thousands)

3. Patient Receivables and Patient Service Revenue

Patient receivables consist of the following at June 30:

	2023	2022
Gross patient receivables	**$ 124,583**	$ 107,266
Less estimated uncollectible accounts and contractual allowances	**(48,124)**	(36,312)
Net patient receivables	**$ 76,459**	$ 70,954

Patient service revenue consists of the following for the years ended June 30:

	2023	2022
Inpatient charges	**$ 252,926**	$ 256,061
Outpatient charges	**447,692**	380,206
Gross charges	**700,618**	636,267
Less contractual and other allowances	**(209,239)**	(158,924)
Net patient service revenue	**$ 491,379**	$ 477,343

The System has elected to apply the optional exemption in ASC 606-10-50-14A as all performance obligations relate to contracts with a duration of less than one year. Under this exemption, the System was not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. Any unsatisfied or partially unsatisfied performance obligations at the end of the year are completed within days or weeks of the end of the year.

The System has also elected the practical expedient utilizing the portfolio approach and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the System's expectation that the period between the time the service is provided to a patient and the time that the patient or third-party payor pays for that service will be one year or less.

(Dollars in Thousands)

3. Patient Receivables and Patient Service Revenue (continued)

The System does not pursue collection of amounts determined to qualify as charity care; therefore, these revenues are not reported as net patient service revenue. Using the cost to charge ratio to approximate cost, charity care provided for the years ended June 30, 2023 and 2022, was $7,021 and $8,758, respectively. The state of Maryland rate system includes components within the rates to partially compensate hospitals for uncompensated care.

4. Assets Limited as to Use

A summary of assets that are limited as to use substantially for debt service and deferred compensation trusts at June 30 is as follows:

	2023	2022
Current:		
Principal, interest, and other – bonds	**$ 1,229**	$ 2,612
Construction funds	**4,912**	–
Other	**55**	3,797
	$ 6,196	$ 6,409
Noncurrent:		
Deferred compensation trusts	**$ 2,853**	$ 3,047
	$ 2,853	$ 3,047

The assets that are limited as to use consist of the following at June 30:

	2023	2022
Current:		
Cash and money market accounts	**$ 6,196**	$ 6,409
	$ 6,196	$ 6,409
Noncurrent:		
Mutual funds	**$ 2,853**	$ 3,047
	$ 2,853	$ 3,047

The noncurrent assets limited as to use mutual funds are primarily invested in equities and bonds chosen by deferred compensation plan participants.

(Dollars in Thousands)

5. Promises to Give

Promises to give are discounted and are due as follows at June 30:

	2023	2022
Less than one year	**$ 794**	$ 859
One to five years	**2,682**	2,839
More than five years	**2,649**	3,859
	6,125	7,557
Less discounting and allowance for uncollectible promises	**1,556**	1,631
Total promises to give, net	**4,569**	5,926
Less current portion of promises to give, net	**675**	730
	$ 3,894	$ 5,196

Promises to give include $1,320 and $2,491 for the years ended June 30, 2023 and 2022, respectively, related to charitable remainder trusts. This net amount represents the excess of the fair value of the related trust accounts over the net present value of the annuities to be paid out of the trust to the named beneficiaries over their estimated life expectancy.

6. Investments

Investments reported as a component of other long-term assets are summarized as follows:

	2023	2022
Investments – donor restricted	**$ 3,416**	$ 6,378
Long-term investments	**188,020**	184,844
	$ 191,436	$ 191,222

Long-term investments represent investments without donor restrictions and income earned on investments with and without donor restrictions.

Investments with donor restrictions are designated by the donors for expenses relating to capital projects or replacement or improvement of existing assets, or to cover the cost of services rendered as charity care and other programs.

(Dollars in Thousands)

6. Investments (continued)

To satisfy its long-term rate-of-return objectives, the System relies on a balanced investment strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The System targets a diversified asset allocation that places a greater emphasis on mutual fund and equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Long-term investments with and without donor restrictions recorded at fair value consist of the following at June 30:

	2023		2022	
	Cost	**Fair Value/ NAV***	**Cost**	**Fair Value/ NAV***
Cash and cash equivalents	**$ 3,282**	**$ 3,282**	$ 7,779	$ 7,779
U.S. government obligations	**4,156**	**3,957**	4,464	4,447
Agency securities	**1,311**	**1,269**	189	182
Corporate obligations	**6,950**	**6,526**	6,583	6,562
Mortgage-backed securities	**5,530**	**5,046**	4,434	4,070
Equity securities	**55,803**	**66,807**	42,780	54,818
Mutual funds	**65,089**	**60,443**	66,292	69,495
Private equity investments	**13,115**	**18,322**	9,702	16,550
Hedge funds	**18,690**	**25,784**	21,425	27,319
	$ 173,926	**$ 191,436**	$ 163,648	$ 191,222

*Private equity investments and hedge funds are recorded net asset values (NAVs), which is discussed further in Note 7, Fair Value Measurements.

Investment gain, net for the years ended June 30 is as follows:

	2023	2022
Unrestricted:		
Net realized gains	**$ 7,684**	$ 6,795
Interest and dividends, net of investment expense	**3,180**	3,406
Gains from joint ventures	**316**	626
	$ 11,180	$ 10,827

(Dollars in Thousands)

6. Investments (continued)

Investment expense was $302 and $399 for the years ended June 30, 2023 and 2022, respectively.

Other investments consist of the following at June 30:

	Carrying Value		Income (Loss)	
	2023	**2022**	**2023**	**2022**
Joint ventures	**$ 19,636**	$ 19,064	**$ 4,045**	$ 1,341
Other	**–**	2,680	**–**	–
	$ 19,636	$ 21,744	**$ 4,045**	$ 1,341

Investments in joint ventures are accounted for using the equity method at June 30 and are as follows:

	Entity	Interest %	2023	2022
Mt. Airy Health Services, LLC	Hospital	50	**$ 1,031**	$ 1,209
Frederick County Radiology, LLC	Hospital	35	**13,006**	11,398
Emmitsburg Wellness Pavilion, LLC	FH	50	**700**	700
Mt. Airy Med-Services, LLC	FHSC	50	**3,131**	3,402
Frederick Surgical Center, LLC	FHSC	40.6	**–**	936
MNR of Frederick, LLC	FHSC	22.5	**565**	1,062
Other	Multiple	6–50	**1,203**	357
			$ 19,636	$ 19,064

The fair value of these joint ventures is not readily determinable.

7. Fair Value Measurements

Assets and liabilities recorded at fair value on the accompanying consolidated balance sheets are categorized based upon the level of judgment associated with the inputs used to measure their fair value.

7. Fair Value Measurements (continued)

FASB guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability (i.e., the exit price) in an orderly transaction between market participants at the measurement date, emphasizing that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, the FASB establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

The level inputs, as defined by FASB guidance for fair value measurements and disclosures, are as follows:

- Level 1 – Inputs utilize unadjusted quoted prices in active markets for identical assets or liabilities that the System has the ability to access at the measurement date.

- Level 2 – Inputs are inputs other than quoted prices included in Level 1 that are observable for the assets or liabilities, either directly or indirectly. Level 2 inputs may include quoted prices for similar assets and liabilities in active markets, as well as inputs that are observable for the assets or liabilities (other than quoted prices), such as interest rates, foreign exchange rates, and yield curves that are observable at commonly quoted intervals.

- Level 3 – Inputs are unobservable inputs for the assets or liabilities, which are typically based on an entity's own assumptions, as there is little, if any, related market activity. Inputs to determine the fair value of Level 3 assets and liabilities require management judgment and estimation.

In addition to amounts recorded at fair value, certain investments are recorded at net asset value.

Net Asset Value – Values are based on the calculated net asset value. The calculated NAV for underlying investments are fair value estimates determined by an external fund manager and other sources based on quoted market prices, operating results, and other business and market sector factors.

(Dollars in Thousands)

7. Fair Value Measurements (continued)

The determination of the fair value level within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The System's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the assets or liabilities.

The following tables present the System's assets and liabilities measured at fair value on a recurring basis and those recorded at NAV, aggregated by the level in the fair value hierarchy within which those measurements fall:

		Fair Value Measurements at Reporting Date Using			
	Total at June 30, 2023	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Other Unobservable Inputs (Level 3)**	**NAV**
Assets					
Cash and cash equivalents	**$ 29,892**	**$ 29,892**	**$ –**	**$ –**	**$ –**
Equity securities	**66,807**	**66,807**	**–**	**–**	**–**
U.S. government obligations	**3,957**	**–**	**3,957**	**–**	**–**
Agency securities	**1,269**	**–**	**1,269**	**–**	**–**
Corporate and other bonds	**6,526**	**–**	**6,526**	**–**	**–**
Mutual funds	**63,296**	**63,296**	**–**	**–**	**–**
Mortgage-backed securities	**5,046**	**–**	**5,046**	**–**	**–**
Private equity investments	**18,322**	**–**	**–**	**–**	**18,322**
Hedge funds	**25,784**	**–**	**–**	**–**	**25,784**
Total assets	**$ 220,899**	**$ 159,995**	**$ 16,798**	**$ –**	**$ 44,106**

(Dollars in Thousands)

7. Fair Value Measurements (continued)

	Total at June 30, 2022	Fair Value Measurements at Reporting Date Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)	NAV
Assets					
Cash and cash equivalents	$ 46,419	$ 46,419	$ –	$ –	$ –
Equity securities	54,818	54,818	–	–	–
U.S. government obligations	4,448	–	4,448	–	–
Agency securities	182	–	182	–	–
Corporate and other bonds	6,562	–	6,562	–	–
Mutual funds	72,578	72,578	–	–	–
Mortgage-backed securities	4,070	–	4,070	–	–
Private equity investments	16,550	–	–	–	16,550
Hedge funds	27,319	–	–	–	27,319
Total assets	$ 232,946	$ 173,815	$ 15,262	$ –	$ 43,869
Liabilities					
Interest rate swap liability	$ (3,515)	$ –	$ –	$ (3,515)	$ –
Total liabilities	$ (3,515)	$ –	$ –	$ (3,515)	$ –

The fair value of the System's trading securities is 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 (LIBOR) 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.

7. Fair Value Measurements (continued)

Private equity investments and hedge funds are recorded at NAV. These amounts are not required to be categorized in the fair value hierarchy. The recorded value is based on the proportionate share of the NAV based on the most recent partners' capital statements received from the general partners, which is generally as of the balance sheet date. It is expected that NAV approximates fair value.

The System had approximately $7,818 of unfunded commitments in private equity investments and hedge funds as of June 30, 2023.

Interest Rate Swap

The System entered into an interest rate swap agreement in conjunction with the issuance of variable rate bonds. The swap contract is valued using models based on readily observable market parameters for all substantial terms of the contract. The change in the fair market value of the swap agreement is included in (deficit) excess of revenue over expenses as the swap is not designated as an effective hedge.

Credit exposure associated with nonperformance by the counterparty to the derivative instrument is generally limited to the uncollateralized fair value of the asset related to instruments recognized on the balance sheets.

The swap contract was terminated on June 29, 2023; see Note 10.

(Dollars in Thousands)

8. Property and Equipment

Property and equipment consist of the following at June 30:

	Estimated Useful Lives	2023	2022
Land	–	**$ 10,967**	$ 10,967
Land improvements	8–20 years	**4,625**	4,625
Buildings	20–40 years	**331,664**	290,705
Fixed equipment	10–20 years	**29,485**	29,452
Movable equipment	3–20 years	**301,691**	288,928
Leasehold improvements	5–20 years	**24,291**	22,886
		702,723	647,563
Less accumulated depreciation		**438,672**	406,103
		264,051	241,460
Construction-in-process, renovations, and deposits		**39,611**	45,616
		$ 303,662	$ 287,076

Construction-in-progress consists of the System's building construction and renovations. As these projects are completed, the related assets are transferred out of construction-in-progress and into the appropriate asset category and are depreciated over the applicable useful lives.

Capitalized computer software, net of accumulated amortization, as of June 30, 2023 and 2022, was $8,571 and $10,258, respectively. Amortization of computer software was $3,933 and $3,469 for fiscal years 2023 and 2022, respectively.

The net book value of assets under financing lease arrangements totaled $8,297 and $10,420 as of June 30, 2023 and 2022, respectively. Depreciation expense related to assets under financing lease arrangements was $2,123 and $1,194 for the years ended June 30, 2023 and 2022, respectively.

(Dollars in Thousands)

9. Long-Term Debt

Long-term debt consists of the following:

		June 30	
	Interest Rate	**2023**	**2022**
MHHEFA Series 2023 Bonds	3.49% to 5.00%	**$ 69,975**	$ –
2013 Line of Credit	Variable	**10,000**	–
MHHEFA Series 2020 Bonds	3.25% to 4.00%	**62,645**	62,645
Promissory Note 2020 converted	1.82%	**92,585**	93,550
MHHEFA Series 2017B Bonds	Variable	**–**	43,535
MHHEFA Series 2012 Bonds	3.00% to 5.00%	**–**	1,295
FSC Line of Credit	Variable	**109**	–
		235,314	201,025
Less current maturities		**(2,494)**	(6,095)
Plus unamortized premiums, net		**6,831**	3,178
Less deferred financing costs, net		**(2,670)**	(1,745)
		$ 236,981	$ 196,363

Series 2023 MHHEFA Revenue Bonds

On June 29, 2023, the System obtained a loan of $69,975 in MHHEFA Revenue Bonds, Frederick Health Issue, Series 2023. The MHHEFA Series 2023 Bonds were issued to refund $35,685 of MHHEFA Series 2017B, refinance $22,463 of outstanding 2013 Line of Credit, pay financing costs, and finance a portion of certain construction and equipment costs of the System.

Interest is payable semiannually on each January 1 and July 1, through July 1, 2053.

The Series 2023 Bonds were issued with a premium of $3,766 and resulted in the incurrence of $1,263 of deferred finance costs as June 30, 2023, to be amortized over the 30-year life of the bonds.

Series 2023 Bonds are subject to redemption prior to maturity beginning at the option of the authority at the principal amount of the Series 2023 Bonds to be redeemed plus accrued interest thereon to the date set for redemption.

9. Long-Term Debt (continued)

The bond agreement contains certain financial covenants, all of which the System was in compliance with as of June 30, 2023.

Series 2020 MHHEFA Revenue Bonds

On June 25, 2020, the System obtained a loan of $62,645 in MHHEFA Revenue Bonds, Frederick Health System Issue, Series 2020. The MHHEFA Series 2020 Bonds were issued to refund all of the outstanding MHHEFA Series 2017A Bonds, pay financing costs, and finance a portion of certain construction and equipment costs of the System.

Interest is payable semiannually on each January 1 and July 1, through July 1, 2050.

The Series 2020 Bonds were issued with a premium of $3,405 and resulted in the incurrence of $877 of deferred finance costs to be amortized over the 30-year life of the bonds.

Series 2020 Bonds are subject to redemption prior to maturity beginning at the option of the authority at the principal amount of the Series 2020 Bonds to be redeemed plus accrued interest thereon to the date set for redemption.

Under the provisions of the bond agreement, the System has granted a security interest in all receipts now owned and hereafter acquired. The bonds are also secured with a deed of trust and security agreement applicable to the main hospital campus of the System. The Series 2020 Bonds are secured ratably with the Series 2012A Bonds, Series 2017B Bonds, Promissory Note 2020, and any outstanding amounts on the 2013 Line of Credit.

The bond agreement contains certain financial covenants, all of which the System was in compliance with as of June 30, 2023.

Promissory Note 2020

On June 25, 2020, the System's Obligated Group issued a promissory note in favor of a lending institution in the amount of $93,875 facilitating legal defeasance of $86,290 of the Series 2012A MHHEFA Revenue Bonds, to pay related finance costs and fund an escrow account to provide for future Series 2012A interest and principal payments. In conjunction with the issuance of this note,

9. Long-Term Debt (continued)

MHHEFA issued a tax exempt bond on July 1, 2022, in the principal amount of the remaining balance on this promissory note, in what is often referred to as a Cinderella bond. The transaction resulted in the incurrence of $386 of deferred finance costs to be amortized over the life of the promissory note of 18 years.

The interest rate on the Promissory Note 2020 is a fixed rate of 2.32% until the tax exempt bond is issued and is payable monthly. There is no debt service reserve requirement associated with the Promissory Note 2020.

Under the provisions of the loan agreement, the System has granted a security interest in all receipts now owned and hereafter acquired. The Promissory Note 2020 is also secured with a deed of trust and security agreement applicable to the main hospital campus of the System. The Promissory Note 2020 is secured ratably with the Series 2012A Bonds, Series 2017B Bonds, Series 2020 Bonds, and any outstanding amounts on the 2013 Line of Credit.

The Promissory Note 2020 contains certain financial covenants, all of which the System was in compliance with as of June 30, 2023.

Series 2017B MHHEFA Revenue Bonds

In June 2017, the System obtained a loan of $60,645 in MHHEFA Revenue Bonds, Frederick Memorial Hospital Issue, Series 2017B. Upon settlement of the bonds, MHHEFA and the Obligated Group entered into a financing agreement with BB&T whereby BB&T became the initial purchaser of the Series 2017B Bonds. The interest rate on the bonds is based on an index floating rate determined by BB&T equal to the applicable percentage of LIBOR plus the applicable spread plus the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) adjustment, if any. The average interest rate on the bond loan was 3.84% for the year ended June 30, 2023. The carrying value of the 2017B Bonds approximates fair value.

The proceeds of the Series 2017B Bonds were used to pay financing costs and for the refunding of the Series 2012B Bonds.

The 2017B MHHEFA Revenue Bonds were paid in full during the fiscal year ended June 30, 2023; $35,685 was refinanced using 2023 MHHEFA Revenue Bonds and the remainder paid by the System.

9. Long-Term Debt (continued)

Series 2012A MHHEFA Revenue Bonds

On June 25, 2020, the Obligated Group members of the System issued a promissory note in favor of a lending institution in the amount of $93,875, facilitating legal defeasance of $86,290 of the Series 2012A MHHEFA Revenue Bonds.

The 2012A MHHEFA Revenue Bonds were paid in full by the System during the fiscal year ended June 30, 2023.

2013 Line of Credit

On September 9, 2013, the System entered into a $20,000 revolving line of credit with a lending institution for the purpose of funding short-term working capital needs. The line of credit bears a variable interest rate of one-month LIBOR plus 1.50% per annum, adjusted and payable monthly.

Under the provisions of this revolving line of credit, the System has granted a security interest in all receipts now owned and hereafter acquired. Any outstanding amounts on this line of credit are secured with a deed of trust and security agreement applicable to the main hospital campus of the System and are secured ratably with the Series 2012A Bonds, Series 2017B Bonds, Promissory Note 2020, and Series 2020 Bonds. All outstanding principal and interest must be repaid on the maturity date.

This agreement contains certain financial covenants, all of which the System was in compliance with as of June 30, 2023.

This line-of-credit agreement was amended on November 4, 2015, extending the maturity date to December 1, 2017, and decreased the revolving loan commitment from $20,000 to $15,000. A second amendment was made on January 1, 2017, reducing the variable interest rate to one-month LIBOR plus 1.25% per annum. A third amendment was made on November 30, 2017, extending the maturity date to January 31, 2020. A fourth amendment was made on October 29, 2019, reducing the variable interest rate to one-month LIBOR plus 1.05% and extending the maturity date to January 31, 2022. A fifth amendment was made on March 7, 2022, changing the interest rate to the Secured Overnight Financing Rate (SOFR) + 1.08% instead of LIBOR and extending the maturity date to January 31, 2024. A sixth amendment was made on January 1, 2023, extending the maturity date to January 31, 2025, and increasing the loan commitment to $50,000.

(Dollars in Thousands)

9. Long-Term Debt (continued)

A $15,000 draw was made during July 2022 and a $20,000 draw was made during January 2023. Repayment in the amount of $25,000 was made during June 2023 with $22,467 and $2,533 coming from 2023 Series MHHEFA Revenue Bonds and System equity, respectively. The outstanding balance on this line of credit was $10,000 and $0 as of June 30, 2023 and 2022, respectively. The average interest rate on the 2013 Line of Credit was 4.91% for the year ended June 30, 2023.

FSC Line of Credit

FSC has a line of credit with a lending institution in the amount of $750 with a maturity date of June 5, 2024. The interest rate is variable at one-month SOFR + 2.32% and the balance outstanding as of June 30, 2023 was $109. The applicable interest rate on June 30, 2023 was 7.38%.

Debt service requirements on long-term debt, excluding original issue premium and deferred financing costs at June 30, 2023, of $6,831 and $2,670, respectively, are as follows:

	Principal
Year ending June 30:	
2024	$ 2,494
2025	12,485
2026	5,380
2027	5,745
2028	5,945
Thereafter	203,265
	$ 235,314

10. Interest Rate Swap Contract

The System records its derivatives as assets or liabilities at fair value. A derivative is typically defined as an instrument whose value is derived from an underlying instrument, index, or rate; has a notional amount; requires little or no initial investment; and can be net settled. The System participates in an interest rate swap contract that is considered a derivative financial instrument.

10. Interest Rate Swap Contract (continued)

The System had an interest rate swap contract with a third party, which was terminated on June 29, 2023, with a payment to the counterparty of $2,165. The System was exposed to credit loss in the event of nonperformance by the counterparty to the interest rate swap contract. However, the System did not anticipate nonperformance by the counterparty. Under the swap contract, the System paid interest at a fixed rate of 3.804% per annum and received interest at a variable rate equal to 67.000% of the one-month LIBOR. The swap contract required payments to be made or received monthly. The fair value of the swap contract was a liability of $0 and $3,515 at June 30, 2023 and 2022, respectively.

The System accrued net payments under its interest rate swap program of $2,576 and $1,550 during fiscal years 2023 and 2022, respectively, including $2,165 for termination on June 29, 2023. These amounts are included within realized and unrealized losses on interest rate swap contract, net, on the accompanying consolidated statements of operations and investing activities on the accompanying consolidated statements of cash flows.

The interest rate swap contract was not designated as an effective cash flow hedge. The System's objectives of entering into the interest rate swap contract included limiting or hedging variable interest rate payments to achieve lower overall borrowing costs than a comparable unhedged fixed rate borrowing, to alter the pattern of debt service payments, and to improve asset/liability matching. Changes in the fair value of the derivative financial instrument were recognized in realized and unrealized losses on interest rate swap contract, net on the accompanying consolidated statements of operations and investing activities on the accompanying consolidated statements of cash flows. The carrying value of the System's derivative financial instrument approximates fair value. The interest rate swap contract was valued using models based on readily observable market parameters for all substantial terms of the contract.

Credit exposure associated with nonperformance by the counterparties to derivative instruments is generally limited to the uncollateralized fair value of the asset related to instruments recognized on the consolidated balance sheets. The System attempted to mitigate the risk of nonperformance by selecting counterparties with high credit ratings and monitoring their creditworthiness.

The System's derivative agreements did not contain any credit support provisions that require it to post collateral if there are declines in the derivative value or its credit rating.

(Dollars in Thousands)

11. Employee Benefit Plans

The System had a defined benefit pension plan (the Plan) that was curtailed on June 30, 2007. The System used a measurement date of June 30 to determine plan assets and benefit obligations. The curtailment was such that participants would no longer accrue benefits under the Plan and no new participants would be accepted. Participant accounts would not receive any service credits or increases in benefits for post-curtailment compensation increases beyond June 30, 2007; however, the System would make annual contributions to the Plan in accordance with actuarially determined amounts to meet future accumulated benefit obligations under the frozen Plan.

The Hospital's Board of Directors approved a plan for terminating the Plan on August 26, 2020, and the System had notified participants of their options. In June 2022, the System completed its termination of the Plan, which converted remaining participants' benefit interests into an annuity or lump-sum distributions.

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 based on a June 30 measurement date:

	2022
Accumulated benefit obligation	$ N/A
Change in projected benefit obligation:	
Projected benefit obligation at beginning of year	$ 53,278
Interest cost	1,440
Actuarial gain	(1,393)
Benefits paid and settlement	(53,325)
Projected benefit obligation at end of year	–
Change in plan assets:	
Fair value of plan assets at beginning of year	52,918
Actual return on plan assets	2,107
Employer contribution (receipt)	(1,700)
Benefits paid and settlement	(53,325)
Fair value of plan assets at end of year	–
Net amount recognized – funded status	$ –

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

Net amounts recognized in net assets without donor restrictions that have not been recognized in net periodic cost are as follows at June 30:

	2022
Net actuarial loss	$ N/A
Total recognized in unrestricted net assets	$ N/A

The following table sets forth the weighted average assumptions used to determine benefit obligations:

	June 30, 2022
Discount rate	N/A
Interest crediting rate	N/A
Rate of compensation increase	N/A

The following table sets forth the weighted average assumptions used to determine net periodic benefit cost:

	Year Ended June 30, 2022
Discount rate	2.75%
Expected return on plan assets	3.50
Interest crediting rate	4.00
Rate of compensation increase	N/A

(Dollars in Thousands)

11. Employee Benefit Plans (continued)

Net periodic pension cost included the following components:

	2022
Interest cost	$ 1,440
Return on plan assets	(1,604)
Amortization of net loss	–
Effect of settlement	(1,665)
Net periodic pension (credit) cost	$ (1,829)

The Plan's assets were recorded at fair value.

The System also has a tax-deferred annuity savings (403(b)) plan available to substantially all employees. In conjunction with the curtailment of the defined benefit pension plan, the System modified the 403(b) plan effective July 1, 2007. Effective January 1, 2018, the 403(b) plan was amended such that all new hires will be automatically enrolled in the 403(b) plan at 3% of employee earnings, which will be automatically increased 1% annually up to 10%. Employees can opt out of this automatic enrollment and annual increase. The System will match 100.0% on employee contributions up to 5.0% of employee earnings. Base contributions continue for employees with five to ten years of service at 0.5% and 1.0% for employees with more than ten years of service. The System's contribution for base matching and transition credits totaled $9,106 and $8,988 for fiscal years 2023 and 2022, respectively.

In December 2005, the System adopted two nonqualified deferred compensation plans with an effective date of December 15, 2004, for certain members of executive management. Under these plans, participating employees may contribute amounts from their compensation to the plan and may receive a discretionary employer contribution. Employees are fully vested in all employee contributions to the plans. Vesting in employer contributions occurs in accordance with the underlying plan documents. All assets of the plans are held in separate trusts. Total contributions by the System to the plans were $423 and $498 for the years ended June 30, 2023 and 2022, respectively.

(Dollars in Thousands)

12. Concentration of Credit Risk

The System has funds on deposit with financial institutions in excess of amounts insured by the Federal Deposit Insurance Corporation. The System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements.

The mix of receivables from patients and third-party payors (in percentages) at June 30 was as follows:

	2023	**2022**
Medicare	**32%**	32%
Medicaid	**28**	23
Blue Cross	**14**	16
HMOs and PPOs	**13**	17
Commercial insurance and other third-party payors	**7**	7
Patients	**6**	5
	100%	100%

(Dollars in Thousands)

13. Functional Expenses

The System and its subsidiaries provide general health care services to residents within its geographic location. Expenses related to providing these services are as follows:

	Program	General and Administrative	Total
Year ended June 30, 2023			
Salaries and wages	**$ 221,277**	**$ 36,595**	**$ 257,872**
Employee benefits	**44,419**	**7,498**	**51,917**
Professional fees	**6,186**	**4,632**	**10,818**
Cost of goods sold	**88,363**	**1,232**	**89,595**
Supplies	**14,613**	**894**	**15,507**
Contract services	**48,133**	**8,437**	**56,570**
Other	**13,041**	**2,913**	**15,954**
Utilities	**4,095**	**907**	**5,002**
Insurance	**1,486**	**3,874**	**5,360**
Depreciation	**29,071**	**3,837**	**32,908**
Interest	**5,797**	**488**	**6,285**
	$ 476,481	**$ 71,307**	**$ 547,788**
Year ended June 30, 2022			
Salaries and wages	$ 202,624	$ 35,608	$ 238,232
Employee benefits	45,657	7,442	53,099
Professional fees	6,184	4,773	10,957
Cost of goods sold	81,386	275	81,661
Supplies	15,708	882	16,590
Contract services	49,764	8,423	58,187
Other	11,078	4,643	15,721
Utilities	4,371	1,923	6,294
Insurance	1,181	1,022	2,203
Depreciation	26,493	3,179	29,672
Interest	4,428	300	4,728
	$ 448,874	$ 68,470	$ 517,344

(Dollars in Thousands)

14. Net Assets

Net assets with temporary donor restrictions are available for the following purposes or periods at June 30:

	2023	2022
Health care services:		
Buildings and equipment	**$ 4,300**	$ 5,549
Restricted by time only	**1,320**	2,491
Specific health care services	**–**	1,400
Staff resiliency programs	**454**	1,028
Education programs	**447**	418
Indigent care and research	**488**	441
	$ 7,009	$ 11,327

Net assets with permanent donor restrictions consist of investments to be held in perpetuity, the income from which is expendable for the following:

	2023	2022
General health care services (reported as other operating revenue)	**$ 971**	$ 971
Specific health care services (reported as net assets released from restrictions)	**5**	5
	$ 976	$ 976

During 2023 and 2022, net assets were released from donor restrictions by incurring expenses or capital expenditures satisfying the restricted purposes in the amounts of $7,287 and $6,853, respectively.

15. Commitments and Contingencies

The System has been named as a defendant in various legal proceedings arising from the performance of its normal activities. In the opinion of management, after consultation with legal counsel and after consideration of applicable insurance, the amount of the System’s ultimate liability under all current legal proceedings will not have a material adverse effect on its consolidated financial position or results of operations.

15. Commitments and Contingencies (continued)

On July 1, 2011, MIL, a single-parent captive, was created to provide a flexible risk financing structure to meet the needs of the System's organization. As of June 30, 2012, MIL provided FMH with Primary Medical Professional Liability and Primary General Liability coverage with policy limits of liability of $1,000 each and every medical incident with a $3,000 annual aggregate for the 2011/2012 policy year and with a $5,000 annual aggregate for the 2012/2013 policy year through to the 2017/2018 policy year. Effective for the 2018/2019 policy year, MIL provides FMH with Primary Medical Professional Liability (MPL) and Primary General Liability (GL) coverage with policy limits of liability of $1,000 per claim/per occurrence for both MPL and GL separately, with a $4,000 aggregate for both MPL and GL combined. The System also issued a Buffer Medical Professional Liability and General Liability policy providing limits of liability of $1,000 each and every medical incident with a $2,000 aggregate, for Medical Professional Liability and General Liability combined. The MIL Primary Policy coverage form is mature claims-made with a retroactive date of July 1, 2005. The policy funding is retrospectively rated.

For policy years 2019/2020 through 2021/2022, the System's Primary MPL/GL policy provides limits of liability of $2,000,000 per claim/per occurrence for both MPL and GL separately, with a $6,000,000 aggregate for both MPL and GL combined.

MIL has also issued an Excess Umbrella Liability mature claims-made policy with a retroactive date of July 1, 2005. This policy is structured on a "dualtower" design. The Excess Medical Professional Liability Tower follows the form of the underlying Primary Medical Professional Liability coverage providing $20,000 limits of liability ($10,000 prior to July 1, 2016). The Umbrella Liability Tower provides $20,000 limits of liability ($10,000 prior to July 1, 2016) excess of scheduled underlying coverages. The "dualtowers" are 100% reinsured with a commercial carrier with an AM Best rating of A- or better.

Effective June 30, 2012, MIL assumed Professional Liability and Comprehensive General Liability coverage previously included under FMH's self-insured plan, for incidents occurring between July 1, 2005 and June 30, 2011, that were reported to FMH prior to June 30, 2011. The policy provides limits of liability of $1,000 each and every medical incident for the hospital professional liability and $1,000 each and every medical incident for comprehensive general liability. The policy is subject to a $3,000 annual aggregate for the hospital professional liability and comprehensive general liability combined, which applies to each covered year separately on a claims-made basis.

15. Commitments and Contingencies (continued)

Effective June 30, 2012, MIL further assumed Professional Liability and Comprehensive General Liability coverage previously included under another FMH self-insurance plan, for incidents occurring between July 1, 1999 and June 30, 2001, with a limit of liability of $100 per claim. The Primary Medical Professional and Primary General Liability policy is 100% MIL retained risk. The Excess Umbrella Liability coverage is fully reinsured with a commercial carrier with an AM Best rating of A- or better.

Effective September 1, 2017, MIL issued a Cyber Deductible Liability Policy to the System at a per claim limit of liability of $100 and an annual aggregate limit of $200. The per claim limit of liability changed to $150,000/annual aggregate of $300,000 effective September 1, 2021. The policy funding is retrospectively rated.

There are known claims and incidents that could result in the assertion of additional claims, as well as claims from unknown incidents that could be asserted arising from services provided to patients.

Through MIL, a wholly owned subsidiary, the System maintains reserves, including excess coverage, in the amount of $17,226 and $19,001 at June 30, 2023 and 2022, respectively, and a related reinsurance receivable of $7,980 and $7,639 at June 30, 2023 and 2022, respectively. In addition, the System has also estimated a tail liability for claims incurred but not reported under the claims-made policy totaling $4,062 and $4,046 as of June 30, 2023 and 2022, respectively. The System employs an independent actuary to estimate the ultimate settlement of such claims.

These reserves are recorded on an undiscounted basis at June 30, 2023 and 2022. In management's opinion, the amounts recorded provide an adequate reserve for loss contingencies. However, changes in circumstances affecting professional liability claims could cause these estimates to change upon final resolution of such matters.

(Dollars in Thousands)

16. Leases

The System leases equipment, office space, and certain facilities. Included on the accompanying consolidated statements of operations and changes in net assets are lease expenses of $6,999 and $5,774 in 2023 and 2022, respectively. The following table summarizes the components of lease expense for the year ended June 30:

	2023	2022
Finance lease cost:		
Amortization	**$ 2,123**	$ 1,647
Interest	**179**	163
Total finance lease cost	**2,302**	1,810
Operating lease cost	**4,339**	3,616
Short-term lease cost	**358**	348
Total lease cost	**$ 6,999**	$ 5,774

As of June 30, 2023, the System recognized $27,945 and $8,297 of operating and financing right-of-use assets, respectively. As of June 30, 2022, the System recognized $28,261 and $10,440 of operating and financing right-of-use assets, respectively.

A summary of the components of operating and finance lease liabilities classified as current and noncurrent on the accompanying consolidated balance sheets are as follows:

	Operating Leases	Finance Leases	Total
June 30, 2023			
Leases, current	**$ 3,619**	**$ –**	**$ 3,619**
Leases, long term	**28,321**	**–**	**28,321**
Other current liabilities	**–**	**1,930**	**1,930**
Other long-term liabilities	**–**	**6,507**	**6,507**
Total lease liabilities	**$ 31,940**	**$ 8,437**	**$ 40,377**
June 30, 2022			
Leases, current	$ 3,258	$ –	$ 3,258
Leases, long term	29,780	–	29,780
Other current liabilities	–	2,029	2,029
Other long-term liabilities	–	8,411	8,411
Total lease liabilities	$ 33,038	$ 10,440	$ 43,478

(Dollars in Thousands)

16. Leases (continued)

The following table summarizes cash flows from operating and finance leases for the years ended June 30:

	2023	2022
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows paid for operating leases	**$ 4,563**	$ 3,615
Operating cash flows paid for interest portion of finance leases	**179**	163
Financing cash flows paid for principal portion of finance leases	**2,058**	1,624
Right-of-use assets obtained in exchange for lease obligations:		
Operating leases	**2,692**	5,392
Finance leases	**–**	6,239

The weighted average discount rates and the System's weighted remaining lease terms as of June 30 are as follows:

	2023	2022
Weighted average discount rate:		
Operating leases	**2.20%**	2.18%
Financing leases	**1.84**	1.89
Weighted average lease term (in years):		
Operating leases	**11.43**	11.16
Financing leases	**5.00**	5.78

(Dollars in Thousands)

16. Leases (continued)

The following table reconciles undiscounted future operating and finance lease obligations for each of the next five years and thereafter, as of June 30, 2023, to the lease obligation recorded on the consolidated balance sheet at June 30, 2023:

	Operating Leases	Finance Leases	Total
Year ended June 30:			
2024	$ 4,391	$ 2,066	$ 6,457
2025	3,819	1,695	5,514
2026	3,564	1,517	5,081
2027	3,437	1,517	4,954
2028	3,353	1,517	4,870
Thereafter	17,766	506	18,272
Total future undiscounted lease obligations	36,330	8,818	45,148
Less lease payment representing interest	(4,390)	(381)	(4,771)
Present value of future lease payments	31,940	8,437	40,377
Less current portion of future lease payments	(3,619)	(1,930)	(5,549)
Long-term lease obligations	$ 28,321	$ 6,507	$ 34,828

Workers' Compensation

The System is self-insured against workers' compensation claims, currently up to $600 per occurrence. Excess insurance attaches at $600 and has unlimited liability above this amount. Expenses include claims paid, reserves on known claims, and reserves on unreported claims (incurred but not reported).

Letter of Credit

The System has a letter of credit issued by a lending institution in the amount of $1,463. This letter of credit is renewed on an annual basis and is required by the state of Maryland as collateral for unemployment benefits.

(Dollars in Thousands)

17. Liquidity and Availability

Financial assets available for general expenditure within one year of the balance sheet date comprise the following at June 30:

	2023	2022
Cash and cash equivalents	**$ 20,414**	$ 32,267
Patient accounts receivable, net	**76,459**	70,954
Promises to give, net	**675**	730
Other receivables	**5,154**	2,629
Investments with daily and weekly liquidity	**142,200**	142,658
Total	**$ 244,902**	$ 249,238

The System's most restrictive bond covenant requires the Obligated Group to maintain unrestricted cash and marketable securities on hand to meet 75 days of normal operating expenses, which would be approximately $105,797 and $100,265 as of June 30, 2023 and 2022, respectively.

18. Regulatory Environment

Medicare and Medicaid

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

18. Regulatory Environment (continued)

Also, future changes in federal and state reimbursement funding mechanisms and related government budgeting constraints could have an adverse effect on the System.

In 1983, Congress approved a Medicare prospective payment plan for most inpatient services as part of the Social Security Amendments Act of 1983. Hospitals in Maryland are currently exempt from these federal reimbursement regulations under a special waiver. The waiver currently in effect is subject to renewal based upon criteria defined in the federal law. Under these payment arrangements with Medicare, a retroactive adjustment could occur if certain performance standards are not attained by all hospitals on a statewide basis. The impact, if any, of any retroactive adjustment of the Medicare prospective payment system, should hospitals in Maryland become subject to such system, on future operations of the System has not been determined.

State of Maryland Health Services Cost Review Commission

Certain hospital charges are subject to review and approval by the HSCRC. Hospital management has filed the required forms with the Commission and believes the Hospital to be in compliance with the Commission's requirements.

Through June 2023, 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, CMS approved a modernized waiver that will be in place as long as Maryland hospitals commit to achieving significant quality improvements, limits on all-payor per 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.

Starting in January 2019, Maryland's hospitals began operating under a new ten-year contract with the federal government entitled Maryland Total Cost of Care Model (TCOC). TCOC is designed to test whether the improvements hospitals have made under the previous modernized waiver can be expanded to all health care providers. The Global Budget Revenue (GBR) methodology will remain in place for hospital rate setting under TCOC. In addition, programs aimed to measure and reduce total health care spending for attributed Medicare patients, including pre- and post-acute care by all providers, are being introduced and will be further defined in the next fiscal year.

18. Regulatory Environment (continued)

Beginning in fiscal year 2014, the System entered into an agreement with HSCRC to participate in the 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.

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 consists of establishing an acceptable unit rate for defined inpatient and outpatient service centers within the System. The actual average unit charge for each service center is compared with 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; however, uncertainties exist as to the final outcome of HSCRC rate setting decision-making. The System was overcharged by $1,567 for the year ended June 30, 2023, and undercharged $1,781 for the year ended June 30, 2022.

The timing of HSCRC's rate adjustments for the System could result in an increase or a 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 System's policy is to record revenue based on actual charges for services to patients in the year in which the services are performed.

HSCRC established an uncompensated care fund whereby certain hospitals are required to contribute to the fund to help cover the costs associated with uncompensated care for all Maryland hospitals equitably. The System received from the fund $195 and $1,428 for the years ended June 30, 2023 and 2022, respectively.

19. Subsequent Events

The System has evaluated subsequent events through October 16, 2023, the date of issuance of these accompanying consolidated financial statements. The System is unaware of any subsequent events that would require recognition or disclosure at this time.

Supplementary Information

Frederick Health, Inc. and Subsidiaries

Supplementary Consolidating Balance Sheet
(In Thousands)

June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Inc. Consolidated	Monocacy Insurance, Ltd.	Frederick Health Medical Group, LLC	Frederick Health Services Corporation	Frederick Integrated Healthcare Network, LLC	Frederick Health Village, LLC	Elimination	Frederick Health Incorporated Consolidated
Assets									
Current assets:									
Cash and cash equivalents	$ 71	$ 16,536	$ 113	$ 1,182	$ 1,669	$ 822	$ 21	$ –	$ 20,414
Patient receivables	–	61,023	–	13,269	2,167	–	–	–	76,459
Other receivables	–	4,844	–	310	–	–	–	–	5,154
Inventory	–	8,414	–	2,213	604	–	–	–	11,231
Prepaid expenses	–	6,179	6	162	163	–	82	–	6,592
Assets limited as to use	–	6,140	56	–	–	–	–	–	6,196
Promises to give, net	–	675	–	–	–	–	–	–	675
Total current assets	71	103,811	175	17,136	4,603	822	103	–	126,721
Net property and equipment	–	270,280	–	1,820	4,762	–	26,800	–	303,662
Right-of-use assets, net	–	16,333	–	7,783	3,829	–	–	–	27,945
Other assets:									
Assets limited as to use	–	2,853	–	–	–	–	–	–	2,853
Investments – donor restricted	–	3,416	–	–	–	–	–	–	3,416
Promises to give, net	–	3,894	–	–	–	–	–	–	3,894
Long-term investments	–	180,672	7,348	–	–	–	–	–	188,020
Other investments	742	15,122	–	–	3,772	–	–	–	19,636
Investments in subsidiaries	310,507	16,210	–	–	–	–	–	(326,717)	–
Other assets	–	150	7,980	–	4,483	–	–	–	12,613
Intercompany receivables	–	47,114	7,928	–	–	–	–	(55,042)	–
Total other assets	311,249	269,431	23,256	–	8,255	–	–	(381,759)	230,432
Total assets	$ 311,320	$ 659,855	$ 23,431	$ 26,739	$ 21,449	$ 822	$ 26,903	$ (381,759)	$ 688,760

Frederick Health, Inc. and Subsidiaries

Supplementary Consolidating Balance Sheet (continued)

(In Thousands)

June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Inc. Consolidated	Monocacy Insurance, Ltd.	Frederick Health Medical Group, LLC	Frederick Health Services Corporation	Frederick Integrated Healthcare Network, LLC	Frederick Health Village, LLC	Elimination	Frederick Health Incorporated Consolidated
Liabilities and net assets									
Current liabilities:									
Current maturities of long-term debt	$ –	$ 2,385	$ –	$ –	$ 109	$ –	$ –	$ –	$ 2,494
Accounts payable	–	42,627	–	988	346	7	591	–	44,559
Accrued expenses	–	21,056	70	5,847	928	–	–	–	27,901
Advances from third-party payors	–	11,333	–	–	–	–	–	–	11,333
Leases, current	–	2,258	–	506	855	–	–	–	3,619
Other current liabilities	–	6,322	17	1,041	96	1	–	–	7,477
Total current liabilities	–	85,981	87	8,382	2,334	8	591	–	97,383
Long-term liabilities, net of current portion:									
Long-term debt	–	236,981	–	–	–	–	–	–	236,981
Interest rate swap contract	–	–	–	–	–	–	–	–	–
Other long-term liabilities	–	13,550	17,226	–	541	–	1	–	31,318
Leases, long term	–	17,178	–	7,851	3,292	–	–	–	28,321
Intercompany liabilities	233	8,029	5,998	10,470	3,677	324	26,311	(55,042)	–
Total long-term liabilities, net of current portion	233	275,738	23,224	18,321	7,510	324	26,312	(55,042)	296,620
Total liabilities	233	361,719	23,311	26,703	9,844	332	26,903	(55,042)	394,003
Net assets:									
Without donor restrictions	302,541	290,151	120	36	11,044	490	–	(318,171)	286,211
With donor restrictions	7,985	7,985	–	–	–	–	–	(7,985)	7,985
Noncontrolling interests	561	–	–	–	561	–	–	(561)	561
Total net assets	311,087	298,136	120	36	11,605	490	–	(326,717)	294,757
Total liabilities and net assets	$ 311,320	$ 659,855	$ 23,431	$ 26,739	$ 21,449	$ 822	$ 26,903	$ (381,759)	$ 688,760

Frederick Health, Inc. and Subsidiaries

Supplementary Consolidating Statement of Operations and Changes in Net Assets
(In Thousands)

Year Ended June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Inc. Consolidated	Monocacy Insurance, Ltd.	Frederick Health Medical Group, LLC	Frederick Health Services Corporation	Frederick Integrated Healthcare Network, LLC	Frederick Health Village, LLC	Elimination	Frederick Health Incorporated Consolidated
Operating revenues:									
Net patient service revenue	$ –	$ 387,663	$ –	$ 89,233	$ 15,403	$ –	$ –	$ (920)	$ 491,379
Other revenue	–	17,612	2,052	14,366	2,993	2,449	–	(16,971)	22,501
Total operating revenues	–	405,275	2,052	103,599	18,396	2,449	–	(17,891)	513,880
Operating expenses:									
Salaries and wages	–	189,397	–	60,215	6,734	1,526	–	–	257,872
Employee benefits	–	40,615	–	9,625	1,314	363	–	–	51,917
Professional fees	–	22,457	127	95	78	242	–	(12,181)	10,818
Cost of goods sold	–	40,861	–	44,262	4,472	–	–	–	89,595
Supplies	–	14,706	–	773	–	8	20	–	15,507
Contract services	–	50,383	–	4,291	1,752	–	863	(719)	56,570
Other	–	11,906	111	4,595	1,850	5	426	(2,939)	15,954
Utilities	–	3,627	–	271	358	11	735	–	5,002
Insurance	–	3,872	2,017	1,282	177	–	64	(2,052)	5,360
Depreciation and amortization	–	29,445	–	539	842	–	2,082	–	32,908
Interest	–	6,190	–	–	303	–	–	(208)	6,285
Total operating expenses	–	413,459	2,255	125,948	17,880	2,155	4,190	(18,099)	547,788
(Loss) income from operations	–	(8,184)	(203)	(22,349)	516	294	(4,190)	208	(33,908)
Other income (loss), net:									
Gain on sale of assets	–	2	–	–	1	–	–	–	3
Loss on extinguishment of debt	–	(268)	–	–	–	–	–	–	(268)
Investment (loss) gain, net	(5,643)	10,436	641	–	311	–	–	5,435	11,180
Change in unrealized gains (losses) on trading securities, net	–	5,526	(438)	–	–	–	–	–	5,088
Realized losses and unrealized gains on interest rate swap contract, net	–	939	–	–	–	–	–	–	939
Other nonoperating gains, net	–	3,788	–	–	13	–	–	–	3,801
Total other (loss) income, net	(5,643)	20,423	203	–	325	–	–	5,435	20,743
(Deficit) excess of revenue over expenses	(5,643)	12,239	–	(22,349)	841	294	(4,190)	5,643	(13,165)
Less non-controlling interests	–	–	–	–	47	–	–	–	47
(Deficit) excess of revenue over expenses	(5,643)	12,239	–	(22,349)	888	294	(4,190)	5,643	(13,118)

Frederick Health, Inc. and Subsidiaries

Supplementary Consolidating Statement of Operations and Changes in Net Assets (continued)

(In Thousands)

Year Ended June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Inc. Consolidated	Monocacy Insurance, Ltd.	Frederick Health Medical Group, LLC	Frederick Health Services Corporation	Frederick Integrated Healthcare Network, LLC	Frederick Health Village, LLC	Elimination	Frederick Health Incorporated Consolidated
(Deficit) excess of revenue over expenses (from previous page)	$ (5,643)	$ 12,239	$ –	$ (22,349)	$ 841	$ 294	$ (4,190)	$ 5,643	$ (13,165)
Other changes in net assets without donor restrictions:									
Other changes in unrestricted net assets*	82	(27,805)	–	22,385	1,499	(4)	4,190	(82)	265
Non-controlling equity interest related to business acquisition	–	4,621	–	–	–	–	–	–	4,621
Released from restriction used to purchase capital	–	2,636	–	–	–	–	–	–	2,636
Total other changes in net assets without donor restrictions	82	(20,548)	–	22,385	1,499	(4)	4,190	(82)	7,522
Changes in in net assets without donor restrictions	(5,561)	(8,309)	–	36	2,340	290	–	5,561	(5,643)
Net assets with donor restrictions:									
Released from restriction used for operations and nonoperating activities	(4,651)	(4,651)	–	–	–	–	–	4,651	(4,651)
Released from restriction used to purchase capital	(2,636)	(2,636)	–	–	–	–	–	2,636	(2,636)
Restricted gifts, bequests, and contributions	2,969	2,969	–	–	–	–	–	(2,969)	2,969
Changes in net assets with donor restrictions	(4,318)	(4,318)	–	–	–	–	–	4,318	(4,318)
Non-controlling interest:									
Excess of revenue over expenses	47	–	–	–	47	–	–	(47)	47
Other changes	514	–	–	–	514	–	–	(514)	514
Changes in non-controlling interest	561	–	–	–	561	–	–	(561)	561
Changes in net assets	(9,318)	(12,627)	–	36	2,901	290	–	9,318	(9,400)
Net assets, beginning of year	320,405	310,763	120	–	8,704	200	–	(336,035)	304,157
Net assets, end of year	$ 311,087	$ 298,136	$ 120	$ 36	$ 11,605	$ 490	$ –	$ (326,717)	$ 294,757

*Includes the board resolution to cancel intercompany liabilities exceeding subsidiaries' net assets.

Frederick Health, Inc. Obligated Group

Supplementary Combining Balance Sheet
(In Thousands)

June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Incorporated	Frederick Health Medical Group, LLC	Elimination	Frederick Health Obligated Group
Assets					
Current assets:					
Cash and cash equivalents	$ 71	$ 16,062	$ 1,182	$ –	$ 17,315
Patient receivables	–	61,023	13,269	–	74,292
Other receivables	–	4,844	310	–	5,154
Inventory	–	8,414	2,213	–	10,627
Prepaid expenses	–	6,179	162	–	6,341
Assets limited as to use	–	6,140	–	–	6,140
Promises to give, net	–	675	–	–	675
Total current assets	71	103,337	17,136	–	120,544
Net property and equipment	–	269,814	1,820	–	271,634
Right-of-use assets	–	16,333	7,783	–	24,116
Other assets:					
Assets limited as to use	–	2,853	–	–	2,853
Investments – donor restricted	–	3,172	–	–	3,172
Promises to give, net	–	3,894	–	–	3,894
Long-term investments	–	168,338	–	–	168,338
Other investments	742	15,122	–	–	15,864
Investments in subsidiaries	310,507	29,344	–	(314,502)	25,349
Other assets	–	150	–	–	150
Intercompany receivables	–	47,114	–	(10,703)	36,411
Total other assets	311,249	269,987	–	(325,205)	256,031
Total assets	$ 311,320	$ 659,471	$ 26,739	$ (325,205)	$ 672,325

The Obligated Group consists of Frederick Health Inc.; Frederick Health Hospital, Inc.; and Frederick Health Medical Group, LLC and the financial statements presented for the Obligated Group include only their accounts, which include their investment interest in controlled, affiliated entities, but do not include the revenues, expenses, assets, or liabilities of the Obligated Group or the revenues, expenses, assets, or liabilities of any of those controlled, affiliated entities.

Frederick Health, Inc. Obligated Group

Supplementary Combining Balance Sheet (continued)

(In Thousands)

June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Incorporated	Frederick Health Medical Group, LLC	Elimination	Frederick Health Obligated Group
Liabilities and net assets					
Current liabilities:					
Current maturities of long-term debt	$ –	$ 2,385	$ –	$ –	$ 2,385
Accounts payable	–	42,359	988	–	43,347
Accrued expenses	–	21,041	5,847	–	26,888
Advances from third-party payors	–	11,333	–	–	11,333
Leases, current	–	2,258	506	–	2,764
Other current liabilities	–	6,221	1,041	–	7,262
Total current liabilities	–	85,597	8,382	–	93,979
Long-term liabilities, net of current portion:					
Long-term debt	–	236,981	–	–	236,981
Interest rate swap contract	–	–	–	–	–
Other long-term liabilities	–	13,550	–	–	13,550
Leases, long term	–	17,178	7,851	–	25,029
Intercompany liabilities	233	8,029	10,470	(10,703)	8,029
Total long-term liabilities, net of current portion	233	275,738	18,321	(10,703)	283,589
Total liabilities	233	361,335	26,703	(10,703)	377,568
Net assets:					
Without donor restrictions	302,541	290,151	36	(306,517)	286,211
With donor restrictions	7,985	7,985	–	(7,985)	7,985
Total net assets attributable to the System	310,526	298,136	36	(314,502)	294,196
Noncontrolling interest	561	–	–	–	561
Total net assets	311,087	298,136	36	(314,502)	294,757
Total liabilities and net assets	$ 311,320	$ 659,471	$ 26,739	$ (325,205)	$ 672,325

The Obligated Group consists of Frederick Health Inc.; Frederick Health Hospital Inc.; and Frederick Health Medical Group, LLC and the financial statements presented for the Obligated Group include only their accounts, which include their investment interest in controlled, affiliated entities, but do not include the revenues, expenses, assets, or liabilities of the Obligated Group or the revenues, expenses, assets, or liabilities of any of those controlled, affiliated entities.

Frederick Health, Inc. Obligated Group

Supplementary Combining Statement of Operations and Changes in Net Assets
(In Thousands)

Year Ended June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Incorporated	Frederick Health Medical Group, LLC	Elimination	Frederick Health Obligated Group
Operating revenues:					
Net patient service revenue	$ –	$ 387,663	$ 89,233	$ –	$ 476,896
Other revenue	–	16,200	14,366	(14,923)	15,643
Total operating revenues	–	403,863	103,599	(14,923)	492,539
Operating expenses:					
Salaries and wages	–	189,397	60,215	–	249,612
Employee benefits	–	40,615	9,625	–	50,240
Professional fees	–	22,457	95	(12,192)	10,360
Cost of goods sold	–	40,860	44,262	–	85,122
Supplies	–	14,627	773	–	15,400
Contract services	–	50,037	4,291	(908)	53,420
Other	–	10,829	4,595	(1,823)	13,601
Utilities	–	3,608	271	–	3,879
Insurance	–	3,872	1,282	–	5,154
Depreciation and amortization	–	29,385	539	–	29,924
Interest	–	6,190	–	–	6,190
Total operating expenses	–	411,877	125,948	(14,923)	522,902
Loss from operations	–	(8,014)	(22,349)	–	(30,363)
Other income (loss), net:					
Gain on sale of assets	–	2	–	–	2
Loss on extinguishment of debt	–	(268)	–	–	(268)
Investment (loss) gain, net	(5,690)	11,144	–	8,321	13,775
Change in unrealized gains (losses) on trading securities, net	–	4,648	–	–	4,648
Realized losses and unrealized gains on interest rate swap contract, net	–	939	–	–	939
Other nonoperating income	–	3,788	–	–	3,788
Total other (loss) income, net	(5,690)	20,253	–	8,321	22,884
(Deficit) excess of revenue over expenses	(5,690)	12,239	(22,349)	8,321	(7,479)

Continued on page 59.

Frederick Health, Inc. Obligated Group

Supplementary Combining Statement of Operations and Changes in Net Assets (continued)

(In Thousands)

Year Ended June 30, 2023

	Frederick Health Incorporated	Frederick Health Hospital, Incorporated	Frederick Health Medical Group, LLC	Elimination	Frederick Health Obligated Group
(Deficit) excess of revenue over expenses (from previous page)	$ (5,690)	$ 12,239	$ (22,349)	$ 8,321	$ (7,479)
Other changes in net assets without donor restrictions:					
Other changes in unrestricted net assets*	129	(27,805)	22,385	(130)	(5,421)
Non-controlling equity interest related to business acquisition	–	4,621	–	–	4,621
Released from restriction used to purchase capital	–	2,636	–	–	2,636
Total other changes in net assets without donor restrictions	129	(20,548)	22,385	(130)	1,836
Changes in net assets without donor restrictions	(5,561)	(8,309)	36	8,191	(5,643)
Net assets with donor restrictions:					
Released from restriction used for operations and nonoperating activities	(4,651)	(4,651)	–	4,651	(4,651)
Released from restriction used to purchase capital	(2,636)	(2,636)	–	2,636	(2,636)
Restricted gifts, bequests, and contributions	2,969	2,969	–	(2,969)	2,969
Changes in net assets with donor restrictions	(4,318)	(4,318)	–	4,318	(4,318)
Noncontrolling interest:					
Excess of revenue over expenses	47	–	–	–	47
Other changes	514	–	–	–	514
Change in noncontrolling interest	561	–	–	–	561
Changes in net assets	(9,318)	(12,627)	36	12,509	(9,400)
Net assets, beginning of year	320,405	310,763	–	(327,011)	304,157
Net assets, end of year	$ 311,087	$ 298,136	$ 36	$ (314,502)	$ 294,757

*Includes the board resolution to cancel intercompany liabilities exceeding subsidiaries' net assets.

The Obligated Group consists of Frederick Health Inc.; Frederick Health Hospital Inc.; and Frederick Health Medical Group, LLC and the financial statements presented for the Obligated Group include only their accounts, which include their investment interest in controlled, affiliated entities, but do not include the revenues, expenses, assets, or liabilities of the Obligated Group or the revenues, expenses, assets, or liabilities of any of those controlled, affiliated entities.

Frederick Health, Inc. Obligated Group

Supplementary Combined Statements of Cash Flows
(In Thousands)

	Year Ended June 30	
	2023	**2022**
Operating activities		
Changes in net assets	**$ (9,400)**	$ (25,379)
Adjustments to reconcile changes in net assets to net cash (used in) provided by operating activities:		
Loss on advance refunding of debt	**268**	–
Depreciation of property and equipment	**29,924**	27,758
Noncash pension adjustment	**–**	(220)
Noncash changes in net assets	**–**	(2,007)
Amortization of original issue discount, premium, and bond issue costs	**(43)**	(368)
Equity in earnings and gain on joint ventures	**(3,478)**	(5,536)
Unrealized losses (gains) and realized losses (gains) on unrestricted investments	**(15,551)**	26,980
Proceeds from restricted contributions	**(5,595)**	(7,530)
Change in fair value of interest rate swap	**(939)**	(2,601)
Changes in operating assets and liabilities:		
Receivables, patient and other	**(7,125)**	(1,950)
Other assets	**1,027**	1,928
Inventories and prepaids	**(326)**	(2,139)
Pledges receivable	**1,357**	(841)
Accounts payable	**13,719**	5,356
Accrued expenses	**(6,500)**	(244)
Advances from third-party payors	**(10,856)**	(41,851)
Intercompany receivable, net	**(2,401)**	514
Other short-term liabilities	**(1,193)**	29
Other long-term liabilities	**(4,025)**	780
Net cash (used in) provided by operating activities	**(21,137)**	(27,321)
Investing activities		
Net purchases of long-term investments and assets limited as to use	**14,051**	(6,852)
Realized losses on interest rate swap contract	**(2,576)**	(1,550)
Other investments	**(745)**	(700)
Purchases of property and equipment	**(41,028)**	(47,244)
Net cash used in investing activities	**(30,298)**	(56,346)

Frederick Health, Inc. Obligated Group

Supplementary Combined Statements of Cash Flows (continued)
(In Thousands)

	Year Ended June 30	
	2023	**2022**
Fundraising and financing activities		
Proceeds from restricted contributions	**$ 5,595**	$ 7,530
Repayments of long-term debt	**(70,795)**	(4,875)
Proceeds from borrowings	**108,741**	10,000
Other	**–**	(5)
Payments for leases and equipment	**(2,058)**	(1,624)
Deferred financing costs paid	**(1,263)**	(84)
Net cash provided by (used in) fundraising and financing activities	**40,220**	10,942
Net decrease in cash, cash equivalents, and restricted cash	**(11,215)**	(72,725)
Cash, cash equivalents, and restricted cash at the beginning of the year	**34,670**	107,395
Cash, cash equivalents, and restricted cash at the end of the year	**$ 23,455**	$ 34,670
Cash and cash equivalents	**$ 17,315**	$ 28,297
Restricted cash, included in assets limited as to use	**6,140**	6,373
	$ 23,455	$ 34,670
Supplemental disclosures		
Cash paid for interest	**$ 4,436**	$ 4,728

The Obligated Group consists of Frederick Health Inc.; Frederick Health Hospital, Inc.; and Frederick Health Medical Group, LLC and the financial statements presented for the Obligated Group include only their accounts, which include their investment interest in controlled, affiliated entities, but do not include the revenues, expenses, assets, or liabilities of the Obligated Group or the revenues, expenses assets, or liabilities of any of those controlled, affiliated entities.

EY | Building a better working world

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

ey.com