




Atlantic General Hospital Corporation

Independent Auditor's Report and Financial Statements

June 30, 2024 and 2023



Atlantic General Hospital Corporation
Contents
June 30, 2024 and 2023

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Independent Auditor's Report

Board of Trustees
Atlantic General Hospital Corporation
Berlin, Maryland

Opinion

We have audited the financial statements of Atlantic General Hospital Corporation (the "Corporation"), which comprise the balance sheets as of June 30, 2024 and 2023, and the related statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Corporation as of June 30, 2024 and 2023, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We 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 Corporation 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 from 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 Corporation's ability to continue as a going concern within 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 from 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 for 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 Corporation'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 Corporation'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.

Forvis Mazars, LLP

**Tysons, Virginia
October 28, 2024**

Atlantic General Hospital Corporation
Balance Sheets
June 30, 2024 and 2023

	2024	2023
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 13,712,398	\$ 16,799,219
Investments	17,115,539	14,870,749
Patient accounts receivable, net	17,581,394	12,238,696
Supply inventories	3,019,333	3,332,558
Current portion of pledges receivable	75,450	151,920
Prepaid expenses and other current assets	3,981,831	4,437,730
	<u>55,485,945</u>	<u>51,830,872</u>
Land, buildings, and equipment, net	<u>53,031,665</u>	<u>54,321,471</u>
Right-of-use assets, operating leases	<u>20,939,239</u>	<u>3,079,025</u>
Other Assets		
Assets whose use is limited		
Cash and cash equivalents restricted by donor	339,004	344,110
Cash and cash equivalents internally designated for an endowment	244,078	112,379
Investments internally designated for deferred compensation	2,996,420	3,949,691
Investments internally designated for an endowment	4,899,402	4,524,479
Noncurrent pledges receivable, net	64,105	700,804
Goodwill and intangible assets, net	1,106,427	1,332,674
Swap contracts	2,611,979	2,298,340
Other noncurrent assets	4,710,043	5,771,988
	<u>16,971,458</u>	<u>19,034,465</u>
Total other assets	<u>16,971,458</u>	<u>19,034,465</u>
Total assets	<u>\$ 146,428,307</u>	<u>\$ 128,265,833</u>

Atlantic General Hospital Corporation
Balance Sheets
June 30, 2024 and 2023

(Continued)

	2024	2023
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable and accrued expenses	\$ 11,569,505	\$ 9,791,052
Salaries, wages, and related items	7,148,980	7,362,751
Interest payable	140,970	118,349
Advances from third-party payors	2,974,351	2,623,732
Current portion of long-term obligations	2,035,002	1,751,624
Current portion of operating lease obligations	1,654,996	970,375
	<u>25,523,804</u>	<u>22,617,883</u>
Total current liabilities	25,523,804	22,617,883
Noncurrent Liabilities		
Long-term obligations, less current portion and net of unamortized debt issuance costs	37,133,952	34,548,759
Other liabilities	9,206,463	11,221,679
Long-term operating lease obligations	19,284,243	2,108,650
	<u>91,148,462</u>	<u>70,496,971</u>
Total liabilities	91,148,462	70,496,971
Net Assets		
Without donor restrictions		
General	49,890,314	51,943,066
Board-designated	4,910,972	4,628,962
With donor restrictions	478,559	1,196,834
	<u>55,279,845</u>	<u>57,768,862</u>
Total net assets	55,279,845	57,768,862
Total liabilities and net assets	<u>\$ 146,428,307</u>	<u>\$ 128,265,833</u>

Atlantic General Hospital Corporation
Statements of Operations
Years Ended June 30, 2024 and 2023

	<u>2024</u>	<u>2023</u>
Operating Revenue		
Net patient service revenue	\$ 148,046,685	\$ 146,247,385
Other operating revenue	15,026,620	10,489,234
Total Operating Revenue	<u>163,073,305</u>	<u>156,736,619</u>
Operating Expenses		
Salaries	73,733,679	74,262,733
Employee benefits and other related expenses	14,797,193	13,535,715
Professional fees and contracted services	12,943,909	13,636,210
Supplies and other expense	45,096,992	42,547,700
Utilities	2,113,624	1,905,582
Maintenance and repairs	9,615,014	8,711,372
Insurance	2,148,090	2,015,118
Interest	1,748,320	1,561,724
Depreciation	7,164,620	8,019,847
Amortization	226,248	226,836
Total Operating Expenses	<u>169,587,689</u>	<u>166,422,837</u>
Loss from Operations	<u>(6,514,384)</u>	<u>(9,686,218)</u>
Other Income (Loss)		
Investment income (loss)	3,760,134	(33,285)
Net unrealized (losses) gains	(427,665)	2,550,501
Change in fair value of swap contracts	313,639	1,621,631
Other	979,753	1,523,303
Total Other Income	<u>4,625,861</u>	<u>5,662,150</u>
Deficit of Revenue and Gains over Expenses	<u>\$ (1,888,523)</u>	<u>\$ (4,024,068)</u>

Atlantic General Hospital Corporation
Statements of Changes in Net Assets
Years Ended June 30, 2024 and 2023

	2024		Total
	Without Donor Restrictions	With Donor Restrictions	
Net Assets, Beginning of Year	\$ 56,572,028	\$ 1,196,834	\$ 57,768,862
Deficit of revenue and gains over expenses	(1,888,523)	-	(1,888,523)
Restricted contributions	-	226,260	226,260
Net assets released from restrictions used for operations	-	(826,754)	(826,754)
Net assets released from restrictions used for capital acquisitions	117,781	(117,781)	-
Changes in net assets	<u>(1,770,742)</u>	<u>(718,275)</u>	<u>(2,489,017)</u>
Net Assets, End of Year	<u>\$ 54,801,286</u>	<u>\$ 478,559</u>	<u>\$ 55,279,845</u>
	2023		Total
	Without Donor Restrictions	With Donor Restrictions	
Net Assets, Beginning of Year	\$ 58,675,028	\$ 3,100,181	\$ 61,775,209
Deficit of revenue and gains over expenses	(4,024,068)	-	(4,024,068)
Restricted contributions	-	17,721	17,721
Net assets released from restrictions used for capital acquisitions	1,921,068	(1,921,068)	-
Changes in net assets	<u>(2,103,000)</u>	<u>(1,903,347)</u>	<u>(4,006,347)</u>
Net Assets, End of Year	<u>\$ 56,572,028</u>	<u>\$ 1,196,834</u>	<u>\$ 57,768,862</u>

Atlantic General Hospital Corporation
Statements of Cash Flows
Years Ended June 30, 2024 and 2023

(Continued)

	<u>2024</u>	<u>2023</u>
Operating Activities		
Change in net assets	\$ (2,489,017)	\$ (4,006,347)
Items not requiring (providing) cash		
Depreciation and amortization expense	7,390,868	8,246,683
Non-cash operating lease expense	1,623,432	1,078,514
Amortization of debt issuance costs	52,140	52,141
Recognition of change in fair value of swap contracts	(313,639)	(1,621,631)
Realized (gains) losses on sale of investments	(2,727,873)	650,132
Unrealized losses (gains) on trading portfolio	427,665	(2,550,501)
Donations and grants for capital acquisition	(117,781)	(1,921,068)
Changes in		
Decrease (increase) in		
Patient accounts receivable, net	(5,342,698)	816,397
Supply inventories	313,225	(157,795)
Prepaid expenses and other current assets	455,899	(63,878)
Other assets	1,775,113	1,834,748
Increase (decrease) in		
Accounts payable and accrued expenses	1,734,786	397,875
Salaries, wages, and related items	(213,771)	(2,244,938)
Interest payable	22,621	4,735
Advances from third-party payors	350,619	(5,231,598)
Operating lease obligations	(1,623,432)	(1,078,514)
Other liabilities	(2,015,216)	685,370
Net cash used in operating activities	<u>(697,059)</u>	<u>(5,109,675)</u>
Investing Activities		
Net sale (purchase) of investments	633,766	(3,356,948)
Purchase of land, buildings, and equipment	(5,831,147)	(2,655,820)
Net cash used in investing activities	<u>(5,197,381)</u>	<u>(6,012,768)</u>
Financing Activities		
Payments on long-term obligations	(1,944,661)	(1,695,490)
Proceeds from issuance of long-term obligations	4,761,092	-
Donations received restricted for capital acquisitions	117,781	1,921,068
Net cash provided by financing activities	<u>2,934,212</u>	<u>225,578</u>

Atlantic General Hospital Corporation
Statements of Cash Flows
Years Ended June 30, 2024 and 2023

(Continued)

	<u>2024</u>	<u>2023</u>
Net Change in Cash, Cash Equivalents, and Restricted Cash	(2,960,228)	(10,896,865)
Cash, Cash Equivalents, and Restricted Cash, Beginning of Year	<u>17,255,708</u>	<u>28,152,573</u>
Cash, Cash Equivalents, and Restricted Cash, End of Year	<u>\$ 14,295,480</u>	<u>\$ 17,255,708</u>
Supplemental Cash Flow Disclosure		
Interest paid	\$ 1,718,801	\$ 1,514,318
Noncash Supplemental Cash Flow Disclosure		
Land, building, and equipment in accounts payable	\$ 43,667	\$ 2,746,475
Right-of-use assets obtained in exchange for new operating lease liabilities	\$ 19,483,646	\$ -
Capital lease obligation for the acquisition of equipment	\$ -	\$ 1,005,050

Note 1. Organization and Nature of Activities

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

Note 2. Summary of Significant Accounting Policies

Use of Estimates

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

Basis of Presentation

The financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Revenues are reported as increases in net assets without donor restrictions unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in net assets without donor restrictions. Gains and losses are reported as increases or decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulation or by law. Contributions, including unconditional promises to give, with no donor-imposed restrictions are recognized in the period received as increases in net assets without donor restrictions. Contributions with donor-imposed restrictions are reported as increases in net assets with donor restrictions. Expirations of restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Income and realized net gains (losses) on investments are reported as follows:

- Increases (decreases) in net assets with donor restrictions if the terms of the gift or the Corporation's interpretation of relevant state law require that they be added to the principal of a permanent net asset with donor restriction;
- Increases (decreases) in net assets with donor restrictions if the terms of the gift impose restrictions on the use of the income;
- Increases (decreases) in net assets without donor restrictions in all other cases.

Cash and Cash Equivalents

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

Atlantic General Hospital Corporation
Notes to Financial Statements
June 30, 2024 and 2023

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

	<u>2024</u>	<u>2023</u>
Cash and cash equivalents, classified as a current asset	\$ 13,712,398	\$ 16,799,219
Amounts restricted by donor	339,004	344,110
Amounts internally designated for an endowment	<u>244,078</u>	<u>112,379</u>
Total cash and cash equivalents (as reported in the accompanying statements of cash flows)	<u>\$ 14,295,480</u>	<u>\$ 17,255,708</u>

Investments

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

Investments are exposed to certain risks such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, changes in the value of investment securities could occur in the near term, and these changes could materially differ from the amounts reported in the accompanying financial statements.

Patient Accounts Receivable

Patient accounts receivable are reported at estimated net realizable amounts from patients, third-party payors, and others for services rendered. Patient accounts receivable include Hospital and physician charges for accounts due from Medicare, Maryland Medical Assistance ("Medicaid"), CareFirst, commercial and managed care insurers, and self-paying patients. Deducted from patient accounts receivable are estimates of implicit price concessions for the excess of charges over the payments on patient accounts to be received from third party payors and uncollectible amounts related to self-paying patients. These estimates are calculated by management based on historical collection experience and the aging of accounts receivable balances.

The Hospital performs periodic assessments to determine if an allowance for expected credit losses is necessary. The Hospital considers its incurred loss experience and adjusts for known and expected events and other circumstances. In estimating its expected credit losses, the Hospital may consider changes in the length of time its receivables have been outstanding, changes in credit ratings for payors, requests from payors to alter payment terms due to financial difficulty, and notices of payor bankruptcies or payors entering receivership. Because the Hospital's accounts receivables are typically paid for by highly-solvent, creditworthy payors, such as Medicare, other governmental programs, and highly-regulated commercial insurers on behalf of the patient, the Hospital's credit losses are immaterial to the financial statements.

Supply Inventories

Supply inventories consists primarily of drugs and medical supplies and are stated at the lower of cost or net realizable value, as determined principally by the first-in, first-out method.

Pledges Receivable

Unconditional promises to give cash and others assets are recorded at fair value in the year that they are made net of allowance for uncollectible accounts and discounted to their present value. As of June 30, 2024, promises to give that are expected to be received in less than one year total \$75,450 and one to five years total \$64,105. The allowance for doubtful accounts for pledges receivable was \$62,562 and \$120,055 at June 30, 2024 and 2023, respectively. The promises to give in future years are discounted in the amount of \$178,958 at a rate of 5.758% at June 30, 2023. The discount for pledges receivable as of June 30, 2024 is not significant.

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consist primarily of prepaid expenditures for insurance and other contract services and other miscellaneous receivables. Prepaid expenditures paid in the current or prior fiscal years and benefiting more than one accounting period are allocated among accounting periods.

Land, Buildings, and Equipment, Net

Land, buildings, and equipment are recorded at cost, including net interest on related borrowings capitalized during periods of construction. Donated items are recorded at fair value at the date of the donation. Expenditures that materially increase values, change capacities, or extend useful lives are capitalized. The carrying amounts of significant assets sold, retired, or otherwise disposed of and the related allowances for depreciation are eliminated from the accounts.

Depreciation, which includes amortization of equipment under financing leases, is recorded on the straight-line basis using the half-year convention over the estimated useful lives (or lease term if shorter) of 10 to 40 years for buildings and improvements and 3 to 10 years for equipment. Any acquisitions from July 1, 1999 and forward that are in excess of \$100,000 are depreciated on the straight-line basis without using the half-year convention.

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support, and are excluded from revenue and gains in excess of expenses and losses. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Leases

At lease inception, the Corporation determines whether an arrangement is or contains a lease. Operating leases are included in right-of-use ("ROU") assets – operating leases, current portion of operating lease obligations, and long-term operating lease obligations in the accompanying balance sheets. Finance leases are included in land, buildings and equipment, current portion of long-term obligations, and long-term obligations in the accompanying balance sheets. ROU assets represent the Corporation's right to use leased assets over the term of the lease. Lease liabilities represent the Corporation's contractual obligation to make lease payments over the lease term.

For operating leases, ROU assets and lease liabilities are recognized at the commencement date. The lease liability is measured at the present value of the lease payments over the lease term. The Corporation elected the practical expedient to use the risk-free discount rate. Operating ROU assets are calculated as the present value of the lease payments plus initial direct costs and any prepayments less any lease incentives received. Lease terms may include renewal or extension options to the extent they are reasonably certain to be exercised. The assessment of whether renewal or extension options are reasonably certain to be exercised is made at lease commencement. Factors considered in determining whether an option is reasonably certain of exercise include, but are not limited to, the value of any leasehold improvements, the value of renewal rates compared to market rates and the presence of factors that would cause a significant economic penalty to the Corporation if the option were not exercised. The Corporation has elected not to recognize a ROU asset and obligation for leases with an initial term of twelve months or less. The expense associated with short-term leases is included in supplies and other expense in the accompanying statements of operations. Variable lease costs include common area maintenance costs and represent non-lease components. As such, these costs are not included in the lease obligation calculation and are expensed as incurred.

Atlantic General Hospital Corporation
Notes to Financial Statements
June 30, 2024 and 2023

For finance leases, after lease commencement, the lease liability is measured on an amortized cost basis and increased to reflect interest on the liability and decreased to reflect the lease payment made during the period. Interest on the lease liability is determined each period during the lease term as the amount that results in a constant period discount rate on the remaining balance of the liability. The ROU asset is subsequently measured at cost, less any accumulated amortization and any accumulated impairment losses. Amortization on the ROU asset is recognized over the period from the commencement date to the earlier of (1) the end of the useful life of the ROU asset, or (2) the end of the lease term. The discount rate used by the Corporation for finance leases is generally the incremental borrowing rate, as most such leases do not provide a readily determinable implicit interest rate. To the extent a lease arrangement includes both lease and non-lease components, the components are not accounted for separately.

Goodwill

Goodwill represents the excess of the cost over the fair value of the identified net assets of acquired businesses. The Corporation evaluates goodwill for impairment at the entity level. Goodwill is tested for impairment only when a triggering event occurs, or circumstances change that indicate the fair value of the entity may be less than its carrying value. Goodwill is amortized over a period of 10 years (or less).

Net Assets

Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Net Assets without Donor Restrictions

Net assets available for use in general operations and not subject to donor restrictions. All revenue without donor restrictions and donor restricted contributions whose restrictions are met in the same period in which they are received are accounted for in net assets without donor restrictions.

Board-Designated Net Assets without Donor Restrictions

Net assets without donor restrictions include amounts designated by the Board of Trustees for a particular purpose. The Board of Trustees may remove or modify the designations at any time. The board-designated assets were a result of the Hospital being named beneficiary in a portion of an estate pursuant to a will in 2001. The Board of Trustees has determined that any investment income on the endowment will be internally designated by using a three-year rolling average market value method, of which 3% annually can be used to fund physician practice development.

Net Assets with Donor Restrictions

Net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates those resources be maintained in perpetuity. All revenues with donor restrictions as to either timing or purpose of the related expenditures or required to be maintained in perpetuity as a source of investment income are accounted for in net assets with donor restrictions. When a donor restriction expires, that is when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions.

Third-Party Advances

The Hospital receives advances from third-party payors to provide working capital for services rendered to the beneficiaries of such services. These advances are subject to periodic adjustment and are principally determined based on the timing difference between the provision of care and the anticipated payment date of the claim for service.

Atlantic General Hospital Corporation
Notes to Financial Statements
June 30, 2024 and 2023

Charity Care and Other Community Services

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

The cost of charity care provided by the Hospital totaled \$647,073 and \$720,246 for the years ended June 30, 2024 and 2023, respectively. Rates charged by the Hospital for regulated services are determined based on an assessment of direct and indirect cost calculated pursuant to the methodology established by the Maryland Health Services Cost Revision Commission ("HSCRC"). For any charity services rendered by the Hospital, the cost of charity care is calculated by applying the estimated total cost-to-charge ratio for the Hospital services to the total amount of charges for services provided to patients benefitting from the charity care policies of the Hospital.

A Maryland hospital either receives payments from or makes payments to the HSCRC with respect to an Uncompensated Care Fund ("UCC") established for rate-regulated hospitals in Maryland. The UCC is intended to provide Maryland hospitals with funds to support the provision of uncompensated care at those hospitals. The Hospital received net payments from the UCC of \$796,724 for the year ended June 30, 2024 and made net payments to the UCC of \$93,842 for the year ended June 30, 2023.

The HSCRC requires all Maryland hospitals to complete and submit a Community Benefit Report annually on December 15th for the preceding fiscal year. The Hospital's Community Benefit Report for the years ended June 30, 2023 and 2022 reported \$8,044,005 and \$6,329,065, respectively (unaudited), in community benefit services.

Statements of Operations

For purposes of display, transactions deemed by management to be ongoing, major or central to the provision of health care services are reported as revenue or expenses, as applicable. Peripheral or incidental transactions are reported as other income or losses, as applicable.

Other Operating Revenue

The majority of other operating revenue is derived from retail pharmacy sales and revenue from the Maryland Primary Care Program ("MDPCP"). During 2024 and 2023, the Corporation generated pharmacy revenue totaling \$11,251,749 and \$6,457,742, respectively and MDPCP revenue totaling \$2,117,195 and \$2,353,816, respectively. Other operating revenue also includes grant income, rental income, cafeteria income, rebates, physician billing fees, medical home revenue, and other miscellaneous income.

Advertising and Marketing Costs

The Corporation expenses advertising and marketing costs as they are incurred. Advertising and marketing expenses were approximately \$1,653,000 and \$1,610,000 for the fiscal years ended June 30, 2024 and 2023, respectively, and are reported as supplies and other expense in the accompanying statements of operations. No advertising or marketing costs have been capitalized in the accompanying balance sheets.

Deficit of Revenue and Gains Over Expenses

The statements of operations include deficit of revenue and gains over expenses. Changes in net assets without donor restrictions, which are excluded from deficit of revenue and gains over expenses, consistent with industry practice, include contributions of (and assets released from donor restrictions related to) long-lived assets and other items that are required by accounting principles generally accepted in the United States of America to be reported separately.

Atlantic General Hospital Corporation
Notes to Financial Statements
June 30, 2024 and 2023

Tax-Exempt Status

The Corporation is exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code as a public charity. Federal tax law requires that the Corporation be operated in a manner consistent with its initial exemption application in order to maintain its exempt status. Management has analyzed the operations of the Corporation and concluded that it remains in compliance with the requirements for exemption. The state in which the Corporation operates also provides general exemption from state income taxation for organizations that are exempt from federal income taxation. However, the Corporation is subject to both federal and state income taxation at corporate tax rates on its unrelated business income. Exemption from other state taxes, such as real and personal property taxes, is separately determined.

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

Maryland Health Services Cost Review Commission .

Patient service revenue is recorded at rates established by the HSCRC. The Hospital entered into the Global Budget Revenue (“GBR”) agreement with the HSCRC. The GBR agreement renews each year for a one-year period unless it is cancelled by the HSCRC or by the Hospital. The GBR agreement provides the Hospital with a fixed revenue amount (“CAP”) under which it must operate each year. The CAP is adjusted annually for inflation, change in the Hospital’s payor mix and uncompensated care, change in population and quality incentives. The Corporation’s policy is to accrue revenue based on actual charges for services to patients in the year in which the services are performed and billed. Overcharges and undercharges are recouped in succeeding years through the HSCRC’s rate setting methodology.

New Accounting Standard

Effective July 1, 2023, the Corporation adopted Accounting Standards Update (“ASU”) 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, as amended, which replaces the incurred loss with an expected loss methodology that is referred to as the current expected credit loss (“CECL”) methodology. The measurement of expected credit losses under CECL is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to certain qualifying insurance receivables and reinsurance recoveries and receivables. This accounting standard did not have a material impact on the financial statements.

Subsequent Events

In preparing these financial statements, the Corporation has evaluated events and transactions for potential recognition or disclosure through October 28, 2024, the date the financial statements were available to be issued.

Note 3. Net Patient Service Revenue

Management has determined that the Corporation has an unconditional right to payment only subject to the passage of time for services provided to date based on just the need to either finalize billing for such services (i.e., charge lag) or to discharge the patient and bill for such services for patients who are still receiving inpatient care in the Corporation’s facilities at the statement of financial position date. Accordingly, the Corporation accrues revenue and the related accounts receivable for services performed but not yet billed at the balance sheet date for in-house patients. Thus, management has determined that Corporation does not have any amounts that should be reflected separately as contract assets.

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The Corporation elected certain available practical expedients under FASB ASU 2014-09, *Revenue from Contracts with Customers (ASC 606)*. First, the Corporation elected the practical expedient that allows nonrecognition of the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Corporation's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, the Corporation does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the respective contracts. Additionally, the Corporation has applied the practical expedient whereby all incremental customer contract acquisition costs are expensed as they are incurred, as the amortization period of the asset that the Corporation otherwise would have recognized is one year or less in duration.

Estimated uncollectible amounts from patients are considered implicit price concessions (as defined in Topic 606) and, therefore, included in net patient service revenue in the accompanying financial statements.

The Corporation routinely obtains assignments of (or is otherwise entitled to receive) patient benefits receivable under their health insurance programs, plans or policies (i.e., third-party payors). Third-party payors include both government payors, which include Medicare, Medicaid, and management care organizations, and commercial insurance carriers. Agreements with third-party payors typically provide for payments at amounts less than established charges. A summary of payment arrangements with third-party payors, by service type, is as follows:

- Global budget revenue – the Corporation has entered into agreements by which the third-party payors pay a percentage of approved Maryland HSCRC charges. A reduced percentage can be obtained if the payor advances a certain amount of working capital.
- Physician practice services – Corporation has entered into agreements by which the third-party payors pay negotiated rates per procedures as defined in the term sheet of the agreements.
- Regional cancer center revenue – Corporation has entered into agreements by which the third-party payors pay negotiated rates per procedures as defined in the term sheet of the agreements.
- Unregulated hospital patient revenue - the Corporation has entered into agreements by which the third-party payors pay negotiated rates per procedures as defined in the term sheet of the agreements.

Performance obligations are determined based on the nature of the services provided by the Corporation. Revenue for performance obligations satisfied over time are recognized based on actual charges incurred in relation to total expected (or actual) charges. The Corporation believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in our hospitals receiving services over multiple days. The Corporation measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. Revenue for performance obligations satisfied at a point in time are generally recognized when goods or services are provided and the Corporation does not believe it is required to provide additional services to the patient. Generally, performance obligations satisfied at a point in time relate to patients receiving outpatient services in a single day. The Corporation measures the performance obligation from the commencement of the outpatient service to the point when it is no longer required to provide services to that patient, which is generally the completion of the outpatient service.

All of the Corporation's performance obligations generally relate to contracts with a duration of less than one year, therefore the Corporation has elected to apply the optional exemptions provided under applicable standards and as a result is 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. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

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Generally, patients who are covered by third party payors are responsible for related deductibles and coinsurance, which vary in amount. The Corporation also provides services to uninsured patients, and offers those uninsured or underinsured patients financial assistance, by either policy or law, from standard charges. The Corporation estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions.

The initial estimate of the transaction price is determined by reducing the standard charges by any explicit price concession, financial assistance, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustment to net patient service revenue in the period of the change. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense.

Consistent with the Corporation's mission, care is provided to patients regardless of their ability to pay. Therefore, the Corporation has determined it has provided implicit price concessions to uninsured patients and other patient balances (for example, copays and deductibles). The Corporation aggregates revenue from contracts with customers by type of service and payor source.

Net patient service revenue disaggregated by service type are as follows for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Global budget revenue	\$ 111,955,306	\$ 106,510,605
Physician services revenue	23,653,466	26,733,299
Regional cancer center revenue	11,680,655	12,060,981
Unregulated hospital revenue	<u>757,258</u>	<u>942,500</u>
Total	<u>\$ 148,046,685</u>	<u>\$ 146,247,385</u>

Net patient service revenue disaggregated by payor are as follows for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Medicare	\$ 61,753,270	\$ 60,503,096
Medicaid	15,311,233	16,667,168
Commercial insurance and HMOs	13,073,500	10,932,708
CareFirst	18,668,567	16,947,230
Self-pay and others	<u>3,148,736</u>	<u>1,460,403</u>
	111,955,306	106,510,605
Physician services revenue	23,653,466	26,733,299
Regional cancer center revenue	11,680,655	12,060,981
Unregulated hospital revenue	<u>757,258</u>	<u>942,500</u>
Total	<u>\$ 148,046,685</u>	<u>\$ 146,247,385</u>

Atlantic General Hospital Corporation
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The following table presents the details of net patient service revenue for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Gross charges	\$ 213,577,493	\$ 212,159,776
Price concessions		
Explicit price concessions	(56,313,677)	(58,995,374)
Implicit price concessions	(8,092,362)	(5,605,301)
Charity care	<u>(1,124,769)</u>	<u>(1,311,716)</u>
Net patient service revenue	<u>\$ 148,046,685</u>	<u>\$ 146,247,385</u>

The following presents the beginning and ending balances of net patient accounts receivables as of June 30, 2024 and 2023:

Patient accounts receivables, net as of July 1, 2022	\$ 13,055,093
Patient accounts receivables, net as of June 30, 2023	12,238,696
Patient accounts receivables, net as of July 1, 2023	\$ 12,238,696
Patient accounts receivables, net as of June 30, 2024	17,581,394

Note 4. Investments

The composition of investments is as follows at June 30:

	<u>2024</u>	<u>2023</u>
Investments		
Common stock	\$ 2,557,510	\$ 2,475,250
Mutual funds - deferred compensation assets	2,996,420	3,949,691
Mutual funds – alternative investments	649,231	-
Mutual funds - equities	11,638,781	13,398,624
Mutual funds - fixed maturity	<u>7,169,419</u>	<u>3,521,354</u>
	25,011,361	23,344,919
Investments internally designated for an endowment	(4,899,402)	(4,524,479)
Investments internally designated for deferred compensation	<u>(2,996,420)</u>	<u>(3,949,691)</u>
Undesignated investments	<u>\$ 17,115,539</u>	<u>\$ 14,870,749</u>

Investment income (loss) consists of for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Interest and dividends	\$ 1,032,261	\$ 616,847
Realized gains (losses)	<u>2,727,873</u>	<u>(650,132)</u>
	<u>\$ 3,760,134</u>	<u>\$ (33,285)</u>

Fair Value Measurements

Current accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establish a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

- Level 1** Quoted prices in active markets for identical assets or liabilities such as debt and equity securities, mutual funds, and money market accounts that are traded in an active market, and other cash equivalents. Level one investments include common stocks, equity mutual funds and money market funds that are traded in an active market.
- Level 2** Observable inputs other than level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level two investments include corporate bonds, U.S. government obligations, and asset and mortgage-backed securities. A third-party pricing service may be used to determine the fair value of each of these investment securities. Because quoted prices in active markets for identical assets are not available, these prices are determined using observable market information such as quotes from less active markets and/or quoted prices of securities with similar characteristics.
- Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. Level three investments can include limited liability partnerships and limited liability companies. The fair value for these investments is determined by applying the ownership percentage to the net asset value of the investment fund. Underlying investments of the funds can include hedge funds, real estate funds, mortgage-backed securities, asset backed securities, and global equity fund of funds.

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

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial asset, including estimates of the timing, amount of expected future cash flows, and the credit standing of the issuer. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair value may not be realized in the immediate settlement of the financial asset. Fair values of common stock and mutual funds have been determined by the Corporation from observable market quotations, when available. Private placement securities and other equity securities where a public quotation is not available are valued by using broker quotes.

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

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The following table presents the Corporation's fair value hierarchy for assets measured at fair value on a recurring basis:

	<u>Fair Value</u>	<u>Fair Value Measurements at June 30, 2024</u>		
		<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Mutual Funds				
Fixed maturity				
Taxable bond fund	\$ 6,842,208	\$ 6,842,208	\$ -	\$ -
Taxable high-yield funds	327,211	327,211	-	-
Equities				
International emerging markets	1,430,125	1,430,125	-	-
International developed	1,856,356	1,856,356	-	-
U.S. large/mid-cap	7,962,502	7,962,502	-	-
U.S. small-cap	389,798	389,798	-	-
Alternatives	649,231	649,231	-	-
Deferred compensation assets	2,996,420	2,996,420	-	-
Common Stocks				
Consumer discretionary	261,672	261,672	-	-
Energy	58,776	58,776	-	-
Consumer staples	61,933	61,933	-	-
Financials	270,369	270,369	-	-
Healthcare	276,661	276,661	-	-
Industrials	402,966	402,966	-	-
Communication services	42,254	42,254	-	-
Information technology	306,253	306,253	-	-
Real estate	29,448	29,448	-	-
Utilities	29,152	29,152	-	-
Materials	56,153	56,153	-	-
Total investments	24,249,488	24,249,488	-	-
Interest rate swaps assets	2,611,979	-	2,611,979	-
Investments at fair value	<u>\$ 26,861,467</u>	<u>\$ 24,249,488</u>	<u>\$ 2,611,979</u>	<u>\$ -</u>

Certain investments that were measured at cost have not been classified in the fair value hierarchy. As of June 30, 2024, the costs of these investments were \$761,873. There were no significant transfers between fair value hierarchy levels for the year ended June 30, 2024.

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The following table presents the Corporation's fair value hierarchy for assets measured at fair value on a recurring basis:

	<u>Fair Value</u>	<u>Fair Value Measurements at June 30, 2023</u>		
		<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Mutual Funds				
Fixed maturity				
Taxable bond fund	\$ 2,971,554	\$ 2,971,554	\$ -	\$ -
Taxable high-yield funds	549,800	549,800	-	-
Equities				
International emerging markets	835,601	835,601	-	-
International developed	4,389,042	4,389,042	-	-
U.S. large/mid-cap	6,250,441	6,250,441	-	-
U.S. REIT funds	272,631	272,631	-	-
U.S. small-cap	1,428,694	1,428,694	-	-
Commodities	222,215	222,215	-	-
Deferred compensation assets	3,949,691	3,949,691	-	-
Common Stocks				
Consumer discretionary	213,878	213,878	-	-
Energy	39,639	39,639	-	-
Consumer staples	94,331	94,331	-	-
Financials	220,932	220,932	-	-
Healthcare	237,143	237,143	-	-
Industrials	159,784	159,784	-	-
Communication services	134,429	134,429	-	-
Information technology	489,023	489,023	-	-
Real estate	30,561	30,561	-	-
Utilities	31,049	31,049	-	-
Materials	62,346	62,346	-	-
Total investments	22,582,784	22,582,784	-	-
Interest rate swaps assets	2,298,340	-	2,298,340	-
Investments at fair value	<u>\$ 24,881,124</u>	<u>\$ 22,582,784</u>	<u>\$ 2,298,340</u>	<u>\$ -</u>

Certain investments that were measured at cost have not been classified in the fair value hierarchy. As of June 30, 2023, the costs of these investments were \$762,135. There were no significant transfers between fair value hierarchy levels for the year ended June 30, 2023.

Note 5. Land, Buildings, and Equipment

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

	<u>2024</u>	<u>2023</u>
Land, buildings, and improvements	\$ 68,894,058	\$ 63,068,979
Fixed equipment	30,610,137	30,086,219
Movable equipment	61,175,311	58,087,554
Finance lease equipment	5,356,868	5,356,868
	<u>166,036,374</u>	<u>156,599,620</u>
Less: accumulated depreciation	<u>(113,792,840)</u>	<u>(106,628,220)</u>
	52,243,534	49,971,400
Construction in process	<u>788,131</u>	<u>4,350,071</u>
	<u>\$ 53,031,665</u>	<u>\$ 54,321,471</u>

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Accumulated amortization on leased equipment totaling \$4,187,763 and \$3,527,164 is included in the balance of accumulated depreciation as of June 30, 2024 and 2023, respectively. Amortization expense associated with finance lease equipment was \$660,599 and \$678,902 for the years ended June 30, 2024 and 2023, and is included in depreciation expense in the accompanying statements of operations.

Note 6. Non-Current Liabilities

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

	<u>2024</u>	<u>2023</u>
2023 construction loan	\$ 4,587,703	\$ -
2017 Series A Bond	3,125,000	4,079,000
2017 Series B Bond	20,013,000	20,013,000
2017 Series Mayor and Council of Berlin Hospital Revenue Bond (Atlantic General Hospital Facility)	10,000,000	10,000,000
2014 commercial mortgage loan	135,203	267,804
2015 commercial mortgage loan	442,039	470,585
2016 commercial loan	96,268	147,594
Finance leases payable, with interest ranging from 3.00% to 6.67%, secured by selected equipment.	<u>1,203,953</u>	<u>1,808,752</u>
Total long-term debt	39,603,166	36,786,735
Net unamortized debt issuance costs	(434,212)	(486,352)
Current portion	<u>(2,035,002)</u>	<u>(1,751,624)</u>
	<u>\$ 37,133,952</u>	<u>\$ 34,548,759</u>

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

	<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>	<u>2029</u>	<u>Thereafter</u>
Future minimum lease payments	\$ 528,358	\$ 412,791	\$ 341,069	\$ 19,548	\$ -	\$ -
Interest	<u>(54,036)</u>	<u>(32,390)</u>	<u>(11,278)</u>	<u>(109)</u>	<u>-</u>	<u>-</u>
	474,322	380,401	329,791	19,439	-	-
Notes/loans payable	488,983	358,508	333,516	351,775	371,043	3,357,388
Bonds payable	<u>984,000</u>	<u>1,009,000</u>	<u>1,041,000</u>	<u>1,071,000</u>	<u>1,108,000</u>	<u>27,925,000</u>
	<u>1,472,983</u>	<u>1,367,508</u>	<u>1,374,516</u>	<u>1,422,775</u>	<u>1,479,043</u>	<u>31,282,388</u>
	<u>\$ 1,947,305</u>	<u>\$ 1,747,909</u>	<u>\$ 1,704,307</u>	<u>\$ 1,442,214</u>	<u>\$ 1,479,043</u>	<u>\$ 31,282,388</u>

Swap Agreements

During 2018, the Corporation obtained a new swap agreement connected with the revenue bonds. The fair value of the swap agreements as of June 30, 2024 and 2023 (as determined after consultation with investment hedging consultants), based on the present value of cash flow differences over the lives of the swap agreements between the interest rate calculated on the swap agreements at inception and rates available on similar swap agreements is \$2,611,979 and \$2,298,340, respectively. Payments made to the counterparty to the swap agreements totaled \$1,420,685 and \$1,404,975 for the years ended June 30, 2024 and 2023, respectively. These amounts include interest due on both the bonds and swap agreements. The Corporation is exposed to credit loss in the event of nonperformance by the counterparty on the swap agreements but does not anticipate nonperformance by the counterparty.

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2014 Commercial Mortgage Loan

On May 23, 2014, the Corporation obtained a \$1,950,000 commercial mortgage from the Bank of Ocean City for the purposes of purchasing a medical office building. The loan is collateralized by a mortgage lien against the building. Principal and interest payments of \$11,810 are made monthly based on an interest rate of 3.99% and the loan matures on May 23, 2034.

2015 Commercial Mortgage Loan

On June 30, 2015, the Corporation obtained a \$680,000 commercial mortgage from the Bank of Ocean City for the purposes of purchasing a condominium unit in the medical office building. The loan is collateralized by a mortgage lien against the condominium. Principal and interest payments of \$4,118 are made monthly based on an interest rate of 3.99% and the loan matures on June 30, 2035.

2016 Commercial Loan

On March 1, 2016, the Corporation obtained a \$452,208 loan from an unrelated third party pertaining to leasehold improvements associated with a medical office building. Principal and interest payments of \$4,797 are made monthly based on an interest rate of 5.00% and the loan matures on March 1, 2026.

2017 Series Revenue Bonds

On September 1, 2017, pursuant to a loan and financing agreement (the 2017 Loan and Financing Agreement) between the Corporation, (the "Issuer"), and M&T Bank (the "Lender"), the Issuer issued the Hospital Revenue Bonds (Atlantic General Hospital Facility) 2017 Series A in the amount of \$7,501,000 and Series B in the amount of \$20,013,000. The Series A Bond proceeds were to refund a portion of the 2010 Series Revenue Bonds and to refinance a portion of the 2008 Commercial Mortgage Loan. The Series B Bond was issued in the maximum principal amount of \$20,013,000 in order to finance the 2017 Project, consisting of building renovations and equipment acquisitions, to refund a portion of the 2001 Series Refunding Revenue Bonds, 2002 Series Revenue Bonds, and 2010 Series Revenue Bonds, and to refinance a portion of the 2008 Commercial Mortgage Loan.

The financing requires monthly payments by the Corporation directly to the Lender sufficient to meet the principal and interest requirements of the 2017 Series A and Series B Bonds through their maturity on July 1, 2027, and March 3, 2042, respectively. Interest payments for Series A and Series B Bonds began on October 1, 2017. Principal and interest payments for Series A began September 3, 2019, with any outstanding interest and principal due July 1, 2027. Principal and interest payments for Series B are to begin August 2, 2027, with any outstanding interest and principal due March 3, 2042.

The Series 2017 Bonds bore interest at the respective index floating rates applicable to the bonds, excluding the immediately succeeding interest payments date, in which the interest rates were 2.21% and 2.45% for Series A and B, respectively. Thereafter, the index floating rate was determined by the London Interbank Offered Rate ("LIBOR") Interest Period. On April 11, 2023, the bonds were amended to base the index floating rate on the Term Secured Overnight Financing Rate ("SOFR"). The interest rates as of June 30, 2024 and 2023 for the 2017 Series A bonds were 6.11% and 5.87%, respectively. The interest rates as of June 30, 2024 and 2023 for the 2017 Series B bonds were 6.66% and 6.41%, respectively.

Each Series 2017 Bond is subject to redemption at the option of Maryland Health and Higher Educational Facilities Authority ("MHHEFA") upon the request of the Corporation, on any date upon not less than five days' notice to the lender, at a redemption price of 100% of the principal amount of the bond redeemed plus accrued interest to the redemption date. The Bonds may also be redeemed at the option of MHHEFA upon the request of the Corporation through purchase at a price equal to 100% of the principal amount of the bond plus accrued interest on the date set for redemption.

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On September 1, 2017, the Corporation also entered into a financing agreement with the Mayor and Council of Berlin and the Lender for a 2017 Taxable Bond in the amount of \$10,000,000 to finance the 2017 Project. The 2017 Taxable Bond bore interest at the index floating rate, excluding the immediately succeeding interest payment date, in which the interest rate was 2.36%. Thereafter, the index floating rate was determined by the LIBOR Interest Period. On May 3, 2023, the bond was amended to base the index floating rate on the Term SOFR. The interest rates as of June 30, 2024 and 2023 for the bond was 6.20% and 5.97%, respectively. Interest payments began November 1, 2017. Principal and interest payments are to begin April 1, 2042, with any outstanding interest and principal due July 1, 2047.

The 2017 Taxable Bond is subject to redemption at the option of the Corporation, in whole or in part, on any date upon not less than five days' notice to the lender, at a redemption price of 100% of the principal amount of the bond redeemed plus accrued interest to the redemption date.

The bonds are secured by a collateral interest in the Corporation's receipts, revenue, and other amounts received by or on behalf of the Corporation. The revenue bonds also place limits on the incurrence of additional borrowings and require the Corporation to maintain a certain debt service coverage, cash covenant, and capitalization ratio.

2023 Construction Loan

On March 30, 2023, the Corporation entered into a 14-year \$5,000,000 construction loan with Calvin B. Taylor Bank for the purposes of facilitating the tenant outfit project at the Ocean Pines facility. The Corporation draws down balances as the project progresses. As of June 30, 2024, approximately \$4,761,000 was drawn on the construction loan. The loan has a fixed rate of 5.5% with interest payments beginning in July 2023 following the first draw on the loan. Principal and interest payments began on October 30, 2023 on the unpaid principal sum. The loan matures on September 30, 2037. The loan is secured by a collateral interest in the Corporation's real property.

Line of Credit

In March 2020, the Corporation entered into an \$8,500,000 revolving line of credit agreement with M&T Bank of which \$7,000,000 matured in October 2020 with the remainder maturing February 28, 2025. Amounts drawn on the remaining \$1,500,000 are due on demand with an interest rate of SOFR plus 1.96448%. The line of credit is secured by a third security interest in all non-realty assets and the Corporation's property. There were no amounts drawn on the line as of June 30, 2024.

Note 7. Goodwill

In March 2018, the Corporation acquired 100% of the equity interest of Berlin Radiation Therapy Treatment Center, LLC (the "Center"). The Center is in the business of providing cancer care services to Berlin, Maryland and the surrounding area. The Corporation paid \$2,500,000 and acquired medical and office equipment of \$308,171. Goodwill of \$2,191,837 was recorded as part of the acquisition, which included the assembled workforce and noncompete agreements, as well as the Center's brand. Amortization expense was approximately \$219,000 for the years ended June 30, 2024 and 2023. Amortization expense will be approximately \$219,000 per year for the next five years.

Note 8. Professional Liability Insurance Coverage

The Corporation is presently exposed to asserted and unasserted potential legal claims encountered in the ordinary course of business. In the opinion of management, the resolution of such matters will not have a material adverse impact on the Corporation's June 30, 2024 financial position or the results of operations for the year then ended. Prior to 2005, the Corporation had claims-made professional liability insurance through a commercial insurance carrier covering claims arising from the performance of professional services and brought against the Corporation while the policy was in force. Insurable limits under this policy were \$1 million per claim and \$3 million annual aggregate shared limit basis. In addition, the Corporation maintained an umbrella policy of \$15,000,000 per occurrence and aggregate.

During 2005, the Hospital, became a shareholder of the newly formed Freestate Healthcare Insurance Company, Ltd. (the "Captive"), a Cayman Islands company, that provides claims-made professional and general liability coverage for the risks of its covered shareholders, their controlled affiliates, and their respective employees.

The Captive provides primary coverage to its covered shareholders and their affiliates with limits of liability of \$2,000,000 for each and every claim ("Retained Layer") and provides an excess policy with various limits of liability which is fully reinsured through commercial carriers. The Corporation has \$15,000,000 of additional reinsurance in the aggregate through such reinsurance arrangements. The estimated unpaid loss liability reserved by the Captive for the Hospital was \$4,710,043 and \$5,771,988 at June 30, 2024 and 2023, respectively and is included in noncurrent other liabilities in the balance sheets.

In accordance with current accounting standards, the June 30, 2024 and 2023 unpaid loss liability is recorded as a noncurrent liability, and the related insurance recovery was reported as a noncurrent asset in the accompanying balance sheets. An estimated liability for incurred but not reported professional liability claims has also been recorded in the amount of approximately \$1,500,000 as a noncurrent other liability in the accompanying balance sheets as of June 30, 2024 and 2023.

Premiums are calculated by an actuary under a retrospectively rated policy and are based primarily on the experience of the Shareholders. The total premium is allocated to each of the Shareholders based on their experience. Premiums for the Corporation's professional and general liability insurance of approximately \$1,695,000 and \$1,764,000 were charged to operations during fiscal years 2024 and 2023. Retrospective premium assessments and credits are calculated based on the aggregate experience of all named insureds under the policy. Each named insured's assessment or credit is based on the percentage of their actual exposure to the actual exposure of all named insureds. Each named insured will not be charged or entitled to any retrospective premium assessments or credits until the policy period has been closed and no further claim obligations are expected. In management's opinion, the assets of the Captive are sufficient to meet its obligations as of June 30, 2024. If the financial condition of the Captive were to materially deteriorate in the future, and the Captive was unable to pay its claim obligations, the responsibility to pay those claims would return to the member hospitals.

Note 9. Commitments

Employment Agreements

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

Retirement Plans

The Corporation sponsors a 403(b) retirement covering substantially all employees of the Corporation. Participants may elect to contribute a percentage of their pretax annual compensation, as defined by the Plan, not to exceed the maximum allowable contributions under the IRC. The Corporation matches 50% of the first 5% of participants' elective deferrals and participants become fully vested in employer contributions after three years of continuous service. Plan expenses were \$1,028,716 and \$958,454 for the years ended June 30, 2024 and 2023, respectively.

Effective January 31, 2003, the Corporation entered into an agreement to sponsor a Section 457 deferred compensation plan. All contributions to the Section 457 plan are from participating employees; however, all assets of the Section 457 plan are the sole property of the Corporation and are fully subject to claims by the Corporation's general creditors. As of June 30, 2024 and 2023, \$2,996,420 and \$3,949,691, respectively, are recorded as investments internally designated for deferred compensation and a related liability in the same amounts as other liabilities on the balance sheets.

Self-Insured Plans

Effective May 1, 2002, the Corporation joined the Maryland Hospital Association ("MHA") Workers' Compensation Self-Insurance Group to self-insure for worker's compensation benefits. The annual premium for worker's compensation is calculated based on the Corporation's payroll estimate and MHA rates per payroll classification. The MHA rates are determined based on past experience. Amounts charged to operations for workers' compensation expense were \$379,763 and \$606,805 for the years ended June 30, 2024 and 2023, respectively.

In lieu of paying unemployment tax premiums to the State of Maryland, the Corporation secured a letter of credit with M&T Bank, effective May 21, 2004. As of June 30, 2024, the letter of credit was in the amount of \$490,071. Additionally, the Corporation paid actual Maryland unemployment claims in the amount of \$17,953 and \$78,216 for the years ended June 30, 2024 and 2023, respectively.

The Corporation maintains an agreement with a third-party to administer a self-insured health plan that benefits Hospital employees and their dependents. On behalf of participating employees, the Corporation pays the cost of health claims and an administration fee for each subscriber employee. The participating associates share in the cost by remitting a pre-established premium through payroll deductions.

Additionally, the Hospital obtains stop loss insurance to cover possible claims in excess of expected claims. The stop loss insurance agreements are annual agreements, subject to annual renewals. The Corporation submits a claim for reimbursement of stop loss insurance when claims exceed a pre-established ceiling. The Corporation's net health benefit expense for the fiscal years ended June 30, 2024 and 2023 was \$8,103,226 and \$6,649,195, respectively, net of premiums received from associates during the fiscal years of \$1,295,536 and \$1,275,577, respectively.

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

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Note 10. Leases Topic 842

The Corporation leases certain office space and medical equipment under the terms of non-cancellable operating leases and finance leases. Operating lease expense is recognized in operations on a straight-line basis over the lease term. In determining lease asset values, the Corporation considers fixed payment terms, incentives, and options to extend or terminate. Renewal, termination, or purchase options affect the lease term used for determining lease asset value only if the option is reasonably certain to be exercised. Variable payments, such as variable common area maintenance, are expensed in the period incurred and not included in the lease asset or liability values.

The components of lease expense (and related classification in the accompanying statements of operations) were as follows during the years ended June 30:

	<u>2024</u>	<u>2023</u>
Operating lease cost (supplies and other expense)	\$ 2,336,250	\$ 1,183,514
Short-term lease cost (supplies and other expense)	627,367	622,263
Finance lease costs:		
Amortization of right-of-use assets (depreciation expense)	660,599	678,902
Interest on lease liabilities (interest expense)	<u>77,913</u>	<u>69,958</u>
Total lease cost	<u>\$ 3,702,129</u>	<u>\$ 2,554,641</u>

Cash paid for amounts included in the measurement of lease liabilities is as follows for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Operating cash flows from operating leases	\$ 1,623,432	\$ 1,078,514
Operating cash flows from finance leases	77,913	69,958
Financing cash flows from finance leases	<u>660,599</u>	<u>678,902</u>
Total	<u>\$ 2,361,944</u>	<u>\$ 1,827,374</u>

Right-of-use assets obtained in exchange for new lease obligations are as follows for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Right-of-use assets obtained in exchange for new operating lease liabilities	<u>\$ 19,483,646</u>	<u>\$ -</u>
Right-of-use assets obtained in exchange for new finance lease liabilities	<u>\$ -</u>	<u>\$ 1,005,050</u>

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Operating lease right-of-use assets are classified as long-term assets with the related liabilities classified as current and long-term in the accompanying balance sheets.

The following table presents lease-related assets and liabilities at June 30:

	<u>2024</u>	<u>2023</u>
Right-of-use assets - operating leases	\$ 20,939,239	\$ 3,079,025
Current portion of operating lease obligations	1,654,996	970,375
Long-term operating lease obligations	<u>19,284,243</u>	<u>2,108,650</u>
Total operating lease liabilities	<u>\$ 20,939,239</u>	<u>\$ 3,079,025</u>

Current finance lease obligations are included in current portion of long-term obligations in the accompanying balance sheets. Noncurrent finance lease obligations are included in long-term obligations in the accompanying balance sheets.

The following table presents finance lease-related assets and liabilities at June 30:

	<u>2024</u>	<u>2023</u>
Property and equipment, net	\$ 1,169,005	\$ 1,829,704
Current portion of finance lease obligations	474,322	581,632
Long-term finance lease obligations	<u>729,631</u>	<u>1,227,120</u>
Total finance lease liabilities	<u>\$ 1,203,953</u>	<u>\$ 1,808,752</u>

Other information:

	<u>2024</u>	<u>2023</u>
Weighted-average remaining lease term – operating leases	12.27 years	4.02 years
Weighted-average remaining lease term – finance leases	2.04 years	3.04 years
Weighted-average discount rate – operating leases	4.79%	2.88%
Weighted-average discount rate – finance leases	5.35%	5.05%

Future operating lease liability maturities are as follows for the years ended June 30:

	<u>Operating</u>	<u>Finance</u>
2024	\$ 2,628,059	\$ 528,358
2025	2,332,500	412,791
2026	2,335,393	341,069
2027	2,262,317	19,548
2028	1,931,036	-
Thereafter	<u>16,939,570</u>	<u>-</u>
Total	28,428,875	1,301,766
Interest	<u>(7,489,636)</u>	<u>(97,813)</u>
Lease liability	<u>\$ 20,939,239</u>	<u>\$ 1,203,953</u>

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Note 11. Functional Expenses

The Corporation provides general health care services and related services to individual within its geographic location. Expenses related to providing these services, based on management's estimates of expense allocations, are as follows for the years ended June 30:

	2024		
	Healthcare Services	General and Administrative	Total
Salaries	\$ 54,767,081	\$ 18,966,598	\$ 73,733,679
Employee benefits and other related expenses	11,731,575	3,065,618	14,797,193
Professional fees and contracted services	8,577,656	4,366,253	12,943,909
Supplies and other expenses	40,974,126	4,122,866	45,096,992
Utilities	985,561	1,128,063	2,113,624
Maintenance and repairs	7,143,517	2,471,497	9,615,014
Insurance	392,449	1,755,641	2,148,090
Interest	440,735	1,307,585	1,748,320
Depreciation	5,248,540	1,916,080	7,164,620
Amortization	219,184	7,064	226,248
Total	<u>\$130,480,424</u>	<u>\$ 39,107,265</u>	<u>\$169,587,689</u>

	2023		
	Healthcare Services	General and Administrative	Total
Salaries	\$ 54,254,715	\$ 20,008,018	\$ 74,262,733
Employee benefits and other related expenses	10,997,295	2,538,420	13,535,715
Professional fees and contracted services	9,028,899	4,607,311	13,636,210
Supplies and other expenses	38,206,147	4,341,553	42,547,700
Utilities	383,139	1,522,443	1,905,582
Maintenance and repairs	6,550,511	2,160,861	8,711,372
Insurance	410,406	1,604,712	2,015,118
Interest	420,466	1,141,258	1,561,724
Depreciation	6,103,767	1,916,080	8,019,847
Amortization	219,182	7,654	226,836
Total	<u>\$126,574,527</u>	<u>\$ 39,848,310</u>	<u>\$166,422,837</u>

The financial statements report certain expense categories that are attributable to more than one health care service or support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including depreciation and amortization, interest, and other occupancy costs, are allocated to a function based on a square footage basis.

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Note 12. Business and Credit Concentrations

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

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

	<u>2024</u>	<u>2023</u>
Medicare	50%	48%
Medicaid	10%	14%
Blue Cross	17%	15%
Commercial	18%	18%
Self-pay and others	<u>5%</u>	<u>5%</u>
	<u>100%</u>	<u>100%</u>

Note 13. Perdue Kresge Challenge for the Community

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

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

Fund activity is presented below for the years ended June 30:

	<u>2024</u>	<u>2023</u>
Beginning fund balance	\$ 2,178,628	\$ 1,996,830
Interest and dividends	77,225	67,470
Net realized and unrealized gains	90,344	238,243
Administrative and management fees	(20,513)	(19,770)
Annual income distributions	<u>(104,786)</u>	<u>(104,145)</u>
Ending fund balance	<u>\$ 2,220,898</u>	<u>\$ 2,178,628</u>

Note 14. Certain Risks and Uncertainties

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

The Joint Commission, a non-governmental privately owned entity, provides accreditation status to hospitals and other health care organizations in the United States of America. Such accreditation is based upon a number of requirements including undergoing periodic surveys conducted by Joint Commission personnel. Certain managed care payors require hospitals to have appropriate Joint Commission accreditation in order to participate in those programs. In addition, the Center for Medicare and Medicaid Services of the U.S. Department of Health and Human Services ("CMS"), the agency with oversight of the Medicare and Medicaid programs, provides "deemed status" for facilities having Joint Commission accreditation. In other words, by being Joint Commission accredited, facilities are "deemed" to be in compliance with the Medicare and Medicaid conditions of participation. Termination as a Medicare provider or exclusion from any or all of these programs/payors would have a materially negative impact on the future financial position, operating results and cash flows of the Corporation. The Hospital has been accredited by the Joint Commission through February 12, 2025.

The HSCRC has jurisdiction over hospital reimbursement in Maryland by an agreement with CMS based on a waiver from the Medicare prospective payment system under Section 1814(b) of the Social Security Act. In January 2014, CMS approved a waiver to modernize Maryland's unique all-payor rate-setting system for hospital services. The waiver consisted of a five-year performance period. Maryland Hospitals are committed to achieving significant quality improvements including reductions in 30-day readmissions and hospital acquired conditions.

Maryland also limited annual Medicare per capita hospital cost growth to a rate lower than the national annual per capita growth rate per year for 2015 to 2018. Under this model, Medicare savings were estimated to be at least \$330 million. Under the waiver, Maryland shifted virtually all of its hospital revenue over the five-year performance period into global payment models.

In connection with the waiver, the HSCRC introduced new revenue arrangements, including the GBR model. This new model for Maryland hospitals moved payment to hospitals from each individual service to a total revenue for each hospital or a combination of hospitals to provide hospitals flexibility in the objectives of better care for individuals, higher levels of overall population health, and improved health care affordability. It removed the financial incentive from increasing volume and provided incentive to work with partners to provide care in the appropriate setting. Beginning January 2019, the new "Total Cost of Care Model" (the Model) was approved and builds upon the successes of the all-payor model. The Model encourages continued clinical redesign and provides tools to providers to treat complex and chronic conditions and is built on the same global budget arrangement mechanics for revenue setting as the predecessor model. This is approved for a 10-year term provided Maryland meets the Model performance requirements.

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

Changes in Federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on the Hospital. The healthcare industry is subject to numerous laws and regulation from federal, state and local governments, and the government has increased enforcement of Medicare and Medicaid anti-fraud and abuse laws, as well as physician self-referral laws (STARK law and regulation). The Hospital's compliance with these laws and regulations is subject to ongoing internal monitoring as well as periodic governmental review and inquiries, and the Hospital has responded appropriately to any such compliance matters. The Hospital is aware of certain asserted and unasserted compliance matters, and from time to time, the Hospital may agree to resolve certain compliance matters with the government through the self-disclosure process. The amount of such settlement for compliance matters currently being evaluated for submission under the self-disclosure process cannot be estimated at this time. The Hospital will continue to monitor its compliance and all related government inquiries and respond appropriately, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. As a result, there is at least a reasonable possibility that the recorded estimates will change by a material amount in the near term.

As a result of pending federal healthcare reform legislation, substantial changes may occur in the healthcare system. Such legislation potentially includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers and the legal obligations of health insurers, providers and employers.

Litigation in the normal course of business, as well as responses to claims and investigations described below, can be expensive, lengthy, and disruptive to normal business operations. Moreover, the results of complex legal proceedings and government investigations are difficult to predict and in certain cases the likelihood of outcome is unknown. Like most healthcare organizations, the Corporation receives inquiries, request for information regarding clinical procedures, licensing, taxes, billing or medical record documentation matters from various State and Federal agencies. The Corporation responds to such requests and provides any detailed information requested. Management is currently unable to estimate, with reasonable certainty, the possible loss, or range of loss, if any, for such lawsuits and investigations. As a result of the current level of governmental and public concerns with health care fraud and abuse, management recognizes that additional investigative activity could occur in the future. In the opinion of management and after consultation with legal counsel, management believes it has established adequate accrued reserves related to all known matters. The outcome of certain litigation, as well as any potential investigative, regulatory, or prosecutorial activity that may occur in the future is unknown. Accordingly, any associated potential future losses resulting from such matters could have an adverse effect on the future financial position, results of operations and liquidity of the Corporation.

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Note 15. Liquidity and Availability

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

	<u>2024</u>	<u>2023</u>
Cash and cash equivalents	\$ 13,712,398	\$ 16,799,219
Marketable securities	<u>22,251,323</u>	<u>19,499,911</u>
	35,963,721	36,299,130
Patient accounts receivable, net	17,581,394	12,238,696
Other receivables	<u>454,415</u>	<u>234,192</u>
Total	<u>\$ 53,999,530</u>	<u>\$ 48,772,018</u>

In addition to the assets in the table above, the Corporation has other investments and assets whose use is limited for specified purposes. Because these other investments assets whose use is limited for specified purposes are not available for general expenditure within one year, they are not reflected in the amounts above. The Corporation does, however, have investments and certain other long-term assets whose use is limited by board designation that could be made available for general expenditure within one year, if necessary.