Mercy Health Services, Inc. and Subsidiaries

Independent Auditor's Report, Consolidated Financial Statements, and Supplementary Consolidating Information

June 30, 2023 and 2022

Table of Contents

FORVIS

Independent Auditor's Report

Board of Trustees
Mercy Health Services, Inc. and Subsidiaries
Baltimore, Maryland

Opinion

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

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Mercy Health Services, Inc. and Subsidiaries, as of June 30, 2023 and 2022 and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in United States of America.

We did not audit the financial statements of Greenleaf Insurance Company, Ltd., a wholly-owned subsidiary, which statements reflect total assets constituting 12% & 11% of Mercy Health Services, Inc. and Subsidiaries' consolidated total assets as of June 30, 2023 and 2022, respectively. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for Greenleaf Insurance Company, Ltd, is based solely on the report of the other auditors.

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 Consolidated Financial Statements section of our report. We are required to be independent of Mercy Health Services, Inc. and Subsidiaries 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 Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Mercy Health Services, Inc. and Subsidiaries' ability to continue as a going concern for one year after the date that the consolidated financial statements are issued.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 consolidated 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 consolidated 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 consolidated 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 Mercy Health Services, Inc. and Subsidiaries' 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 consolidated financial statements.

- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Mercy Health Services, Inc. and Subsidiaries' 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

Report on Supplementary Financial Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information on pages 50 to 57 is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position and results of operations of the individual companies and is not a required part of the consolidated 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 consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, which insofar as it relates to Greenleaf Insurance Company, Ltd. is based on the report of other auditors, the consolidating information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

FORVIS, LLP

Charleston, West Virginia
September 12, 2023

Mercy Health Services, Inc. and Subsidiaries
Consolidated Balance Sheets
June 30, 2023 and 2022
(in thousands)

	2023	2022
ASSETS		
Current assets:		
Cash and cash equivalents	**$ 261,559**	$ 283,318
Short-term investments	**1,778**	1,656
Current portion of funds held by trustee -- *Note 6*	**13,427**	15,662
Resident prepayment deposits	**797**	571
Patient accounts receivable, net -- *Note 3*	**80,464**	77,139
Other amounts receivable, net	**4,734**	7,744
Current pledges receivable, net -- *Note 4*	**2,595**	2,541
Supplies inventory	**14,867**	16,505
Other current assets	**3,535**	3,731
Total current assets	**383,756**	408,867
Property and equipment, net -- *Note 5*	**543,499**	542,185
Investments and other assets:		
Funds held by trustee, less current portion -- *Note 6*	**1,601**	1,504
Board designated and donor restricted cash and investments -- *Note 7*	**316,754**	275,348
Restricted cash and investments	**147,370**	124,688
Long-term pledges receivable, net -- *Note 4*	**21,815**	20,588
Investments in and advances to affiliates -- *Note 8*	**4,564**	4,590
Reinsurance receivable -- *Note 10*	**6,335**	6,815
Right of use assets -- *Note 24*	**40,302**	43,476
Other assets -- *Note 9*	**3,626**	3,705
Total assets	**$ 1,469,622**	$ 1,431,766

(in thousands)

	2023	2022
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term debt -- *Note 11*	**$ 12,508**	$ 12,059
Accounts payable and accrued expenses	**148,763**	160,188
Advances from third-party payers	**22,791**	31,861
Medicare advance contract liability, current	**-**	15,209
Resident prepayment deposits	**964**	571
Provision for outstanding losses, current -- *Note 10*	**6,889**	8,529
Operating lease liability, current -- *Note 24*	**4,012**	4,012
Construction retainage	**505**	506
Total current liabilities	**196,432**	232,935
Long-term debt, less current portion -- *Note 11*	**359,674**	371,825
Provision for outstanding losses, long-term -- *Note 10*	**132,589**	123,238
Post-retirement obligation -- *Note 14*	**5,779**	6,911
Interest rate swap liabilities -- *Note 11*	**6,529**	11,401
Operating lease liabilities -- *Note 24*	**38,039**	40,689
Other long-term liabilities -- *Note 23*	**4,283**	3,752
Total liabilities	**743,325**	790,751
Net assets:		
Without donor restrictions	**673,290**	593,263
With donor restrictions -- *Note 16*	**53,007**	47,752
Total net assets	**726,297**	641,015
Total liabilities and net assets	**$ 1,469,622**	$ 1,431,766

Mercy Health Services, Inc. and Subsidiaries
Consolidated Statements of Operations
Years Ended June 30, 2023 and 2022
(in thousands)

	2023	2022
Revenue:		
Net patient service revenue	**$ 886,731**	$ 855,091
CARES Act provider relief funds	**-**	1,647
Other operating revenue	**47,068**	33,779
Net assets released from restriction used for operations	**3,476**	5,172
Total revenue	**937,275**	895,689
Expenses -- *Note 19:*		
Salaries and benefits	**509,795**	481,768
Medical and surgical supplies	**76,865**	75,335
Pharmacy supplies	**80,469**	78,056
Other expendable supplies	**39,237**	38,599
Professional fees	**22,457**	22,115
Insurance	**22,094**	23,164
Other purchased services	**63,214**	61,891
Interest expense	**13,255**	13,196
Repairs	**19,890**	18,473
Depreciation and amortization	**43,235**	44,029
Total expenses	**890,511**	856,626
Operating income	**46,764**	39,063
Other income (losses):		
Investment income -- *Note 7*	**2,985**	13,143
Net unrealized gains (losses) on investments -- *Note 7*	**23,445**	(71,819)
Unrealized gains on interest rate swaps -- Note 11	**4,872**	11,664
Equity earnings in joint ventures -- *Note 8*	**1,000**	653
Gain on extinguishment of debt	**-**	380
Other	**(384)**	948
Net other income (losses)	**31,918**	(45,031)
Excess (deficiency) of revenues over expenses	**78,682**	(5,968)
Changes to pension and post retirement plan obligations -- *Notes 14 and 15*	**966**	1,825
Federal grant funding for the purchase of property and equipment -- *Note 5 and 25*	**251**	233
Net assets released from restrictions for the purchase of property and equipment	**128**	250
Increase (decrease) in net assets without donor restrictions	**$ 80,027**	$ (3,660)

Mercy Health Services, Inc. and Subsidiaries
Consolidated Statements of Changes in Net Assets
Years Ended June 30, 2023 and 2022
(in thousands)

	Without Donor Restrictions	With Donor Restrictions	Total
Net assets, June 30, 2021	$ 596,923	$ 24,144	$ 621,067
Deficit of revenue under expenses	(5,968)	-	(5,968)
Net assets released from restrictions for the purchase of property and equipment	250	(250)	-
Federal grant funding for the purchase of property and equipment	233	(233)	-
Investment loss on net assets with donor restrictions	-	(1,274)	(1,274)
Restricted gifts, bequests and contributions	-	30,537	30,537
Changes to pension and post retirement plan obligations	1,825	-	1,825
Net assets released from restrictions used for operations	-	(5,172)	(5,172)
Change in net assets	(3,660)	23,608	19,948
Net assets, June 30, 2022	593,263	47,752	641,015
Excess of revenue under expenses	**78,682**	**-**	**78,682**
Net assets released from restrictions for the purchase of property and equipment	**128**	**(128)**	**-**
Federal grant funding for the purchase of property and equipment	**251**	**(251)**	**-**
Investment loss on net assets with donor restrictions	**-**	**675**	**675**
Restricted gifts, bequests and contributions	**-**	**8,435**	**8,435**
Changes to pension and post retirement plan obligations	**966**	**-**	**966**
Net assets released from restrictions used for operations	**-**	**(3,476)**	**(3,476)**
	80,027	**5,255**	**85,282**
Net assets, June 30, 2023	**$ 673,290**	**$ 53,007**	**$ 726,297**

(in thousands)

	2023	2022
Operating activities:		
Change in net assets	**$ 85,282**	$ 19,948
Adjustments to reconcile change in net assets to net cash and cash equivalents (used in) provided by operating activities:		
Depreciation and amortization	**43,235**	44,029
Amortization of debt issuance cost, premiums and discounts	**(106)**	(283)
Gain on interest rate swaps	**(4,872)**	(11,664)
Gain on extinguishment of debt	**-**	(380)
Gain on asset disposal	**(38)**	(1,145)
Realized and unrealized (gain) loss on investments	**(22,231)**	62,334
Restricted gifts, bequests, and contributions and restricted investment income	**(8,435)**	(30,537)
Federal grant funding for the purchase of property and equipment	**(251)**	(233)
Increase in:		
Patient accounts receivable, net	**(3,325)**	(11,900)
Other amounts receivable, net	**3,490**	2,934
Inventory	**1,638**	969
Other assets	**442**	7,262
Trading portfolio	**6,418**	(27,395)
Increase (decrease) in:		
Accounts payable and accrued expenses	**(20,469)**	17,725
Medicare advance contract liability	**(15,209)**	(53,094)
Provision for outstanding losses	**7,711**	3,930
Operating leases	**(2,650)**	(1,822)
Post-retirement obligation	**(1,132)**	(1,511)
Other long-term liabilities	**531**	(7,092)
Net cash and cash equivalents provided by operating activities	**70,029**	12,075
Investing activities:		
Purchases of investments	**(68,144)**	(94,032)
Sales of investments	**39,955**	90,885
Purchases of property and equipment	**(41,338)**	(34,560)
Net cash and cash equivalents used in investing activities	**(69,527)**	(37,707)

Mercy Health Services, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
Years Ended June 30, 2023 and 2022
(in thousands)

(Continued)

	2023	2022
Financing activities:		
Proceeds from restricted gifts, bequests, contributions and restricted investment income	**$ 7,154**	$ 10,422
Proceeds from federal grants	**251**	233
Payment of financing costs	**-**	(417)
Proceeds from long term debt	**-**	80,535
Repayment of long term debt	**(11,596)**	(95,166)
Net cash and cash equivalents used in financing activities	**(4,191)**	(4,393)
Net decrease in cash, cash equivalents and restricted cash	**(3,689)**	(30,025)
Cash, cash equivalents and restricted cash at beginning of year	**318,646**	348,671
Cash, cash equivalents and restricted cash at end of year	**$ 314,957**	$ 318,646
Cash paid for interest	**$ 13,306**	$ 12,719

Notes to Consolidated Financial Statements

1. Organization and Summary of Significant Accounting Policies

Organization, basis of presentation and principles of consolidation

Mercy Health Services, Inc. (MHS) was formed for the purpose of supporting, benefiting, or carrying out some or all of the purposes of Mercy Medical Center, Inc. (Medical Center or MMC), Stella Maris, Inc. (SMI), the physician practice groups comprising the Physician Enterprise (as further described below) and Mercy Health Foundation (MHF). MHS is the sole member of the Medical Center, SMI, the Physician Enterprise and MHF. MHS prepares its consolidated financial statements on the accrual basis of accounting. The accompanying consolidated financial statements include MMC, SMI, the Physician Enterprise and MHF. All material intercompany balances and transactions have been eliminated.

Mercy Medical Center, Inc.

The Medical Center, a subsidiary of MHS, provides inpatient, outpatient and emergency care services primarily for the citizens of the Baltimore metropolitan area. In addition, the following entities are wholly owned subsidiaries of the Medical Center:

Name of Subsidiary	Tax Status
Mercy Transitional Care Services, Inc. (MTC) *Provider of subacute services*	Tax Exempt
Greenleaf Insurance Company, Ltd. (GIC) *Provider of self-insured general and malpractice coverage to MHS*	Foreign Subsidiary

Stella Maris, Inc.

SMI, a subsidiary of MHS, is the sole member of the Stella Maris Operating Corporation, as well as the Cardinal Shehan Center, Incorporated (CSC). SMI provides sub-acute, hospice, long-term care, skilled homecare, personal care and adult day care to patients in the central Maryland service area within its 412-bed and 18 emergency certificate of need bed facility. SMI was licensed for 18 additional emergency beds during the period ending June 30, 2019. CSC is engaged in maintaining and providing care and housing of aged and infirmed persons. CSC owns St. Elizabeth Hall, a 200-unit apartment complex for the elderly.

Physician Enterprise

The Physician Enterprise includes Maryland Family Care, Inc. (MFC), St. Paul Place Specialists, Inc. (SPPS) and Maryland Specialty Services, LLC (MSS). MSS is the sole member of Lutherville Hematology and Oncology, LLC and North Calvert Anesthesiology Services, LLC, and is the sole stockholder of Vascular Specialty Services, Inc. These entities provide primary care and specialty services within the Baltimore area. MFC, SPPS and MSS are wholly owned/controlled subsidiaries of MHS.

Mercy Health Foundation, Inc.

MHF, a subsidiary of MHS, was formed to coordinate and strengthen the fundraising function on behalf of MHS.

Income taxes

MHS, MMC, SMI, MFC, SPPS, MHF, MTC, CSC and MSS are not-for-profit organizations exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, and are, therefore, not subject to federal income tax under current income tax regulations. MHS subsidiaries otherwise exempt from federal and state taxation are nonetheless subject to taxation at corporate tax rates at both the federal and state level on their unrelated business income.

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

Basis of presentation

The consolidated 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 (losses) gains on investments are reported as follows:

- change in net assets with donor restrictions if the terms of the gift or the MHS’ interpretation of relevant state law require that they be added to the principal of a permanent net asset with donor restriction;
- change in net assets with donor restrictions if the terms of the gift impose restrictions on the use of the income;
- change in net assets without donor in all other cases.

Supplies inventory

Supplies inventory are stated at the lower of cost, determined by the first-in, first-out method, or net realizable value.

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 not restricted by donors and donor restricted contributions whose restrictions are met in the same period in which they are received, or in the same period in which conditions are met, are accounted for in net assets without donor restrictions.

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 that resources be maintained in perpetuity. All revenues restricted by donors 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.

Restricted and long-term investments

Restricted investments represent funds that have been set aside to cover a portion of GIC's estimated outstanding claims, and donor restricted funds from net assets with donor restrictions. At June 30, 2023 and 2022, respectively, restricted investments of $147,370 and $124,688 were set aside to cover estimated outstanding claims and donor restricted funds. Long-term investments represent board designated funds associated with the GIC's investment portfolio.

Investments and investment risk

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value. Investments in hedge funds, private equity funds and other limited partnerships are also measured at fair value. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in excess (deficit) of revenues over (under) expenses unless the income or loss is restricted by donor or law. MHS' investments are comprised of a variety of financial instruments and are managed by investment advisors. The fair values reported in the accompanying consolidated balance sheets are subject to various risks including changes in the equity markets, the interest rate environment, and general economic conditions. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the fair value of investment securities, particularly for alternative investments and investments measured at net asset value (NAV), it is reasonably possible that the amounts reported in the accompanying consolidated financial statements could change materially in the near term.

Advances from third-party payers

The Medical Center receives advances from third-party payers 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.

Net patient service revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered. MMC charges are based on rates established by the State of Maryland Health Services Cost Review Commission (the Commission); accordingly, revenue reflects actual charges to patients based on rates in effect during the period in which the services are rendered (see Note 18). SMI and Physician Enterprise are paid for services based on either negotiated contracts with commercial payers, fee schedules with Medicare and Medicaid or standardized pricing for self-pay patients.

Explicit price concessions represent the difference between amounts billed as patient service revenue and amounts allowed by third-party payers and are accrued in the period in which the related services are rendered.

Based on historical experience, a significant portion of MHS' uninsured patients will be unable or unwilling to pay for services provided. Thus, MHS estimates an implicit price concession related to uninsured patients in the period the services are provided based upon management's assessment of historical and expected net collections. This estimate considers business and general economic conditions, trends in healthcare coverage and other collection indicators. Throughout the year, management assesses the adequacy of these implicit price concessions based upon its review of patient accounts receivable and collections to date. Other factors, such as account aging and payment cycles, are considered when estimating implicit price concessions. MHS follows established guidelines for placing its self-pay patient accounts with an outside collection agency. After collection efforts are exhausted, the uncollected balances are returned to the appropriate MHS entities for final write-off.

Effective October 1, 2019, MTC and SMI are reimbursed under a new prospective payment system called the patient driven payment model (PDPM), which bases payment on resident characteristics, rather than services provided. PDPM payment depends on the summation of case-mix adjusted components (physical therapy, occupational therapy, speech language pathology, nursing, and nontherapy ancillaries) each with its own case-mix groups and application of a variable per day adjustment schedule. Part-B rehabilitative services are billed and paid based on billable minutes using timed based (or constant attendance) codes.

Charity care

The Medical Center provides medically necessary services without charge or at amounts less than its established rates to patients who qualify for charity care under its financial assistance policy. Because the Medical Center does not pursue collection of those amounts determined to qualify as charity care, they are not reported as net patient service revenue and are not included in patient accounts receivable.

The criteria for qualifying for charity care applied by the Medical Center includes family income, net assets and the size of the patient's bill relative to the patient's ability to pay. Discounts are provided to patients who are unable to pay based on a sliding scale that is applied for family incomes up to approximately 400% above the U.S. Department of Health and Human Services (HHS) Poverty Guidelines. Free care is provided to patients with family incomes up to approximately 200% above the HHS Poverty Guidelines.

Charity care is provided to patients who qualify under the Medical Center's financial assistance policy at any time. Once the Medical Center determines that the patient qualifies for charity care, the Medical Center makes no further attempt to collect on the amount qualifying for charity care.

Certain other controlled subsidiaries of MHS also provide services without charge or at amounts less than their established rates to patients who qualify for charity care under their respective financial assistance policies.

Impairment of long-lived assets

MHS accounts for impairment or disposal of long-lived assets in accordance with applicable guidance. Such guidance requires that long-lived 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 assets to be held and used is measured by comparison of the carrying amount of an asset to future net cash 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 by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Management believes that no asset impairment existed at June 30, 2023 and 2022.

Property and equipment

Property and equipment acquisitions costing more than $3,000 or more and having a useful life longer than one years are capitalized and recorded at cost. Donated property and equipment are recorded at fair value at the date of the donation. Depreciation is provided on the straight-line method over the estimated useful lives of the assets, buildings and the parking center at 40 years, building improvements are depreciated over 25 years, machinery and equipment ranges from three to ten years.

The cost of new implemented software is capitalized and included within machinery and equipment and is being depreciated over 10 years. Costs include payment to vendors for the purchase and assistance in its installation, payroll costs of employees directly involved in the software installation and interest costs of the software project if financed by debt. Preliminary costs to document system requirements, vendor selection and any costs before software purchases are expensed. Capitalization of costs will generally end when the project is completed, and the software is ready to be used. Where implementation of the project is in phases, only those costs incurred that further the development of the project will be capitalized. Costs incurred to maintain the applications are expensed. Depreciation expense was $42,620 and $43,796 for the period ending June 30, 2023 and 2022, respectively.

(dollars in thousands)

Resident prepayment deposits

SMI's private pay residents are required to make a non-interest-bearing prepayment of two months' room and board at the time of admission. St. Elizabeth Hall obtains an interest-bearing security deposit, which is the lesser of one month rent or the resident responsibility. At the time of discharge or acceptance by Medical Assistance or similar government assistance programs, any prepayment remaining after application to the resident's outstanding bill will be refunded. At June 30 2023 and 2022, resident prepayment deposits approximated $797 and $571, respectively, and have been recorded as a current asset and a current liability within the consolidated balance sheets.

Accounting estimates

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

Cash and cash equivalents

Cash and cash equivalents include certain investments in highly-liquid instruments purchased with a maturity of three months or less, excluding assets whose use is limited. The carrying amount of cash and cash equivalents approximates fair value.

MHS maintains cash and cash equivalent accounts that may, at times, exceed federally insured limits. MHS has not experienced any losses from maintaining these accounts in excess of federally insured limits. Management believes it is not subject to significant risks associated with these accounts.

Restricted cash held in board designated investments have been set aside by the Board of Trustees (Board) for future capital improvements or strategic initiatives over which the Board retains control and may, at its discretion, subsequently use for other purposes. Cash held in donor restricted funds will be used to satisfy donor restricted purposes. Funds held by trustee or authority will be primarily used to satisfy future debt service requirements (Note 6).

Following is a reconciliation of cash, cash equivalents and restricted cash as presented in the accompanying consolidated statements of cash flows as of June 30:

	2023	2022
Cash and cash equivalents	$ **261,559**	$ 283,318
Board designated and donor restricted cash	**38,368**	20,313
Restricted cash	**-**	5,507
Funds held by trustee	**15,030**	9,508
Total cash, cash equivalents and restricted cash shown in the accompanying consolidated statements of cash flows	$ **314,957**	$ 318,646

Derivative instruments

Current accounting standards require that an entity recognize all derivative instruments as either assets or liabilities in the statement of financial position and measure those instruments at fair value. MHS has entered into interest rate swap agreements to manage its interest rate risk (see Note 11). The interest rate swaps do not qualify for hedge accounting under current accounting standards; therefore, management accounts for the derivative instruments as speculative derivative instruments with the change in the fair value reflected in the accompanying consolidated statements of operations as a component of other non-operating income. Net settlement payments are reported as a component of interest cost, with the exception of the payments associated with construction activities that are capitalized. Entering into interest rate swap agreements involves varying degrees and elements of credit, default, prepayment, market and documentation risk in excess of the amounts recognized on the consolidated balance sheets. Such risks involve the possibility that there will be no liquid market for these agreements, the counterparty to these agreements may default on its obligation to perform and there may be unfavorable changes in interest rates.

Debt issuance costs

Costs incurred in connection with the issuance of long-term debt have been deferred and are being amortized over the term of the related debt using the straight-line method, which approximates the effective interest method. Such costs are reflected as a reduction of long-term debt in the accompanying consolidated balance sheets. Amortization of debt issuance costs was $106 and $283 for the years ending June 30, 2023 and 2022, respectively.

Leases

At lease inception, MHS determines whether an arrangement is or contains a lease. Operating leases are included in operating lease right-of-use (ROU) assets, current operating lease liabilities and noncurrent lease liabilities in the accompanying consolidated financial statements. ROU assets represent MHS' right to use leased assets over the term of the lease. Lease liabilities represent MHS' 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 as the present value of the lease payments over the lease term. MHS uses the rate implicit in the lease if it is determinable. When the rate implicit in the lease is not determinable, MHS uses its incremental borrowing rate at the commencement date of the lease to determine the present value of the lease payments. 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 MHS if the option were not exercised. Lease expense is recognized on a straight-line basis over the lease term. MHS 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 other purchased services in the accompanying consolidated statements of operations.

Excess (deficit) of revenue over (under) expenses

The consolidated statements of operations include excess (deficit) excess of revenue over (under) expenses. Changes in net assets without donor restrictions, which are excluded from excess (deficit) of revenue over (under) expenses, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets) and includes changes in pension and post retirement cost. Activities that result in gains or losses unrelated to the primary operations of MHS are considered to be nonoperating.

Measure of operations

The accompanying consolidated statements of operations reflect operating income, which includes all operating revenues and expenses that are an integral part of the MHS' healthcare services and supporting activities and net assets released from donor restrictions to support operating expenditures. Activities included in excess (deficit) excess of revenue over (under) expenses that are excluded from operating income, consistent with industry practice include, changes in net unrealized gains and losses on derivative financial instruments and losses on refinancing of long-term debt, investment income (including realized and unrealized gains and losses on investments, interest, dividends and investment expenses), except for interest income earned on operating cash and cash equivalents and realized gains and losses and interest income associated with the malpractice insurance program, which are included in other operating revenue, as such proceeds are utilized in operations.

CARES Act Provider Relief Funding

MHS has received provider relief funding under the federal Coronavirus Aid, Relief and Economic Security (CARES) Act. These relief funds are considered non-exchange transactions subject to terms and conditions specified by the resource provider distributed by the Health Resources Service Administration (HRSA) section of the U.S. Department of Health and Human Services (HHS). These conditions create a restriction that such funds must be used to prevent, prepare or respond to the coronavirus (COVID 19). This conditional grant revenue is recognized as other operating revenue to the extent terms and conditions/restrictions are met for coronavirus related expenses or lost revenues. MHS reports conditional contributions for which restrictions are met in the same reporting period as receipt of such funding as net assets without donor restrictions. Such funds are subject to recoupment.

Medicare Accelerated and Advance Payment Program

The CARES Act also expanded the Medicare Accelerated and Advance Payment Program, which allows for eligible health care facilities to request up to six months of advance Medicare payments. Such accelerated payments are interest free for 29 months for most acute care hospitals. The Centers for Medicare & Medicaid Services (CMS) has applied claims for services provided to Medicare beneficiaries against the advanced payments received by MHS. Amounts received represent contract liabilities under Accounting Standards Codification (ASC) Topic 606, *Revenue Recognition (Topic 606)* and are recorded within Medicare advance contracts liability on the accompanying consolidated balance sheet as of June 30, 2022 based on the established repayment scheduled.

Contributions

Unconditional promises to give cash and other assets to MHS are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received.

2. Net Patient Service Revenue

Estimated uncollectible amounts from patients are considered implicit price concessions (as defined in Topic 606) and, therefore, included in net patient service revenue. Allowances for price concessions continue to be presented as a direct reduction of patient accounts receivable.

Management has determined that MHS 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 MHS' facilities at the balance sheet date. Accordingly, MHS accrues revenues 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 MHS does not have any amounts that should be reflected separately as contract assets.

As permitted from Topic 606, MHS elected certain available practical expedients under the standard. First, MHS elected the practical expedient that allows nonrecognition of the promised amount of consideration from patients and third-party payers for the effects of a significant financing component due to MHS' expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payer pays for that service will be one year or less. However, MHS 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, MHS 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 MHS otherwise would have recognized is one year or less in duration.

Patient service revenue is reported at the amount that reflects the consideration to which MHS expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payers (including health insurers and government programs) and others. Generally, MHS bills patients and third-party payers several days after services are performed or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services provided by MHS. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected charges. MHS 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 obligations. Generally, performance obligations satisfied over time relate to patients in the Medical Center or SMI. MHS measures the performance obligation from admission to the facility to the point when the facility is no longer required to provide services to that patient, or resident which is generally the time of discharge. Revenue for performance obligations satisfied at a point in time generally relate to patients receiving outpatient services or patients and customers in a retail setting and MHS does not believe it is required to provide additional goods or services.

Because all of its performance obligations relate to contracts with a duration of less than one year, MHS has elected to apply the optional exemption provided in current applicable accounting standards and, therefore, 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. Any unsatisfied or partially unsatisfied performance obligations 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 patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

As discussed in Note 18, MMC charges are based on rates established by the Commission, which is subsequently reduced by contractual discounts provided to third-party payers and discounts provided to uninsured patients in accordance with MHS policy. SMI and Physician Enterprise determine the transaction price based on standard charges for goods and services provided, reduced by explicit price concession in the form of contractual adjustments provided to third-party payers, discounts provided to uninsured patients in accordance with internal policy, and implicit price concessions provided to uninsured patients. MHS determines its estimate of implicit price concessions based on historical collection experience with this class of patients using a portfolio approach as a practical expedient to account for patient contracts as collective groups rather than individually. Management believes that the financial effects of using this practical expedient are not materially different from an individual contract approach.

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. As a result of investigations by governmental agencies, various healthcare organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which in some instances have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge compliance of MHS with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon MHS. The results of such governmental review could include fines, penalties and exclusion from participation in the Medicare and Medicaid programs. In addition, the contracts MHS has with commercial payers also provide for retroactive audit and review of claims.

(dollars in thousands)

Generally, patients who are covered by third-party payers are responsible for related deductibles and coinsurance, which vary in amount. MHS also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. MHS 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 charge by any discounts and price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to 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 mission of MHS, care is provided to patients regardless of their ability to pay. Therefore, MHS has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts MHS expects to collect based on its collection history with those patients.

Net patient service revenue from third-party payers and others (including uninsured patients) for the years ended June 30, 2023 and 2022, are summarized in the following tables:

	2023				
	Medicare	**Medicaid**	**Commercial**	**Other**	**Total**
Hospital | Inpatient	**$ 75,843**	**$ 53,502**	**$ 60,740**	**$ 1,331**	**$ 191,416**
Hospital | Outpatient	**127,252**	**46,007**	**172,045**	**6,702**	**352,006**
Hospital | Emergency Room	**4,267**	**8,478**	**3,774**	**1,371**	**17,890**
Stella | Skilled Nursing	**15,063**	**26,132**	**2,738**	**7,651**	**51,584**
Stella | Home Health	**8,479**	**157**	**1,990**	**1,591**	**12,217**
Physician Enterprise | FFS	**52,036**	**27,370**	**92,931**	**11,924**	**184,261**
Physician Enterprise | Ancillary	**35,825**	**3,665**	**37,577**	**290**	**77,357**
	$ 318,765	**$ 165,311**	**$ 371,795**	**$ 30,860**	**$ 886,732**

	2022				
	Medicare	**Medicaid**	**Commercial**	**Other**	**Total**
Hospital | Inpatient	$ 74,781	$ 46,972	$ 65,697	$ 3,288	$ 190,738
Hospital | Outpatient	126,761	41,611	163,204	9,003	340,579
Hospital | Emergency Room	4,369	8,843	3,325	2,106	18,643
Stella | Skilled Nursing	12,497	22,349	1,174	12,266	48,286
Stella | Home Health	10,920	229	792	1	11,942
Physician Enterprise | FFS	46,761	25,119	86,226	13,162	171,268
Physician Enterprise | Ancillary	34,529	4,907	33,936	263	73,635
	$ 310,618	$ 150,030	$ 354,354	$ 40,089	$ 855,091

Revenue from deductibles and coinsurance are included in the categories presented above based on the primary payer.

(dollars in thousands)

3. Patient Accounts Receivable and Charity Care

Approximately 47% and 48% of gross patient accounts receivable were due from Medicare and Medicaid at June 30, 2023 and 2022, respectively.

The net cost of charity care provided by MHS totaled $19,829 and $18,488 for the years ended June 30, 2023 and 2022, respectively. The cost of charity care was calculated by applying the cost-to-charge ratio to the total amount of charges foregone for each of the controlled subsidiaries of MHS that provide charity care. The cost of charity care was determined net of any patient-related revenue due to sliding scale payments or other patient-specific sources and includes both direct and indirect cost of rendering care. The net cost of charity care is excluded from the uncompensated care fund net receipts (see Note 18). Additionally, MHS and certain of its controlled subsidiaries provide structured repayment plans to patients without collateral.

4. Pledges Receivable, Net

Pledges receivable resulting from unconditional promises to give are reported in the period when the pledge is made. As of June 30, 2023, pledges receivable consisted of contributions to fund capital and operating campaigns for the MHS. Pledges receivable are classified as net assets with donor restrictions.

MHS had unconditional promises to give representing the following at June 30, 2023:

	2023	2022
Amounts to be received within one year	**$ 3,634**	$ 2,668
Amounts to be received within two to five years	**9,448**	7,568
Amounts to be received after five years	**21,070**	22,011
Total Pledges	**34,152**	32,247
Less unamortized discount	**(9,742)**	(9,118)
Less current portion	**(2,595)**	(2,541)
Long-term portion	**$ 21,815**	$ 20,588

MHS discounts long term pledge receivables at a rate range of 2.25% to 4.63% which includes a risk adjustment factor. Approximately $23,000 and $24,000 of the total gross pledge receivable attributable to one major donor, as of the year ended June 30, 2023 and 2022, respectively.

(dollars in thousands)

5. Property and Equipment

Property and equipment, at cost, consists of the following at June 30:

	2023	2022
Buildings and improvements	**$ 701,816**	$ 686,745
Machinery and equipment	**293,076**	278,544
Parking center	**41,971**	41,234
Construction-in-progress	**36,011**	23,104
Land	**18,976**	18,976
	1,091,850	1,048,603
Accumulated depreciation	**(548,351)**	(506,418)
	$ 543,499	$ 542,185

Construction in progress consists primarily of major renovation and expansion projects. Interest costs incurred on borrowed funds, net of income earned, during the period of construction of facilities are capitalized as a component of the cost of those assets.

MMC completed construction and IT projects to expand services and capacity that cost approximately $15,446 and $10,353 as of June 30, 2023 and 2022, respectively. The spend associated with these projects have been capitalized and are included in buildings and improvements. MMC has applied for and received financial assistance from FEMA in response to the COVID-19 outbreak and subsequent projects in the amounts of $298 and $233, for the years ended June 30, 2023 and 2022, respectively. See further discussion of the FEMA funds received for capital projects at Note 25. In addition, MMC has multiple ongoing projects with the construction company. The president and CEO of MMC's primary general contractor was a member of MHS board of trustees as of June 30, 2022. MHS spent approximately $10,789 with this general contractor during the years ended June 30, 2022,

6. Funds Held by Trustee

Funds held by trustee, which consist primarily of cash and government obligations (at fair value), are limited as to use as follows at June 30:

	2023	2022
Debt service fund	**$ 13,427**	$ 15,662
Reserve for replacements and residual receipts	**1,601**	1,504
	15,028	17,166
Less current portion	**(13,427)**	(15,662)
Long-term portion	**$ 1,601**	$ 1,504

(dollars in thousands)

7. Board Designated and Donor Restricted Investments

Board designated investments are set aside by the board of trustees for costs relating to replacement or improvement of existing assets, or to cover the cost of services rendered as charity care and other programs. All board-designated investments are without donor restrictions, as the board at its discretion may undesignated the use of such funds. Investments with donor restrictions have been limited by donors to a specific purpose.

Board designated and investments with donor restrictions consist of the following at June 30:

	2023	2022
Equity	**$ 193,661**	$ 155,790
Fixed maturity	**34,903**	34,521
Cash	**38,368**	20,313
Alternatives	**35,555**	41,076
Pooled investments	**14,267**	23,648
	$ 316,754	$ 275,348

The investments above have been allocated, by source, as follows at June 30:

	2023	2022
Board designated	**$ 290,336**	$ 252,904
With donor restrictions subject to passage of time or use	**26,418**	22,444
	$ 316,754	$ 275,348

Investments with perpetual donor restrictions at June 30, 2023 and 2022 of $2,178 are reported as restricted cash and investments.

Earnings on investments without donor restrictions are as follows for the years ended June 30:

	2023	2022
Interest and dividends	**$ 4,199**	$ 3,658
Net realized (losses) gains	**(1,214)**	9,485
	2,985	13,143
Unrealized gains (losses) on investments	**23,445**	(71,819)
	$ 26,430	$ (58,676)

MHS has certain charitable gift annuities with certain individuals and other third party entities. As of June 30, 2023 and 2022, MHS maintained reserve assets in the amount of $93 and $96, in a segregated account, respectively**.** As of June 30, 2023 and 2022, MHS maintained reserves on its outstanding annuity agreements in the amount of $47 and $48, respectively. Management believes the reserve assets are sufficient to meet the reserve requirements.

(dollars in thousands)

8. Investments In and Advances to Affiliates

Investments in and advances to affiliates include joint venture relationships in which MHS or its subsidiaries have an ownership interest of 50% or less. Investments over which MHS has significant influence are generally carried on the equity method, while the others where MHS does not have significant influence are carried at cost.

MHS has investments totaling $4,564 and $4,590 at June 30, 2023 and 2022, respectively, in the following joint ventures:

		Percentage of Ownership		Investment	
Joint Venture	**Business Purpose**	**2023**	**2022**	**2023**	**2022**
Premier Purchasing Partners, Inc.	Capital balance in group purchasing organization	**n/a**	n/a	**$ 276**	$ 276
Johns Hopkins Medicare Advantage	Medicare Advantage plan	**1.11%**	1.11%	**4,288**	4,314
				$ 4,564	$ 4,590

MHS recorded non-operating income of $873 and $653 related to the operations of these investments for the years ended June 30, 2023 and 2022, respectively. MHS receives rebates from Premier Purchasing Partners, Inc., which are netted with associated supplies expense in the accompanying consolidated financial statements.

In June 1997, MMC executed a joint venture agreement with the Archbishop of Baltimore to form Mercy Ridge, Inc. (MR) for the purpose of developing a continuing care retirement community located in Timonium, MD. MMC has a 50% ownership in the joint venture. Since the original contribution into the joint venture, MMC has received distributions greater than the original investment. As of June 30, 2023 and 2022, MR has operated at a net deficit. MMC has recorded the equity method in the investment at zero for the period ending June 30, 2023 and 2022, since MMC is not obligated to make additional contributions into MR.

In September 2016, MHS invested in the Maryland Health Advantage Medicare Advantage Plan (the MA Plan) as a minority owner acquiring a six percent ownership stake. The MA Plan is comprised of various Maryland healthcare providers to deliver comprehensive provider, physician, prescription medicine, wellness and other coverage to participating Medicare beneficiaries in Maryland through a health care network. MHS and the Physician Enterprise are also contracted as participating providers in the MA Plan.

MHS recognizes its ownership in the MA Plan using the cost basis of accounting. MHS' current committed capital is $5,141 and the mandatory capital was limited to $3,000. Any additional capital requirements are optional but electing not to contribute will dilute MHS' ownership percentage accordingly. MHS contributed $183 during the year ended June 30, 2023 and $296 during the period ending June 30, 2022. All net revenue from providing services to MA Plan beneficiaries is recognized at expected reimbursable amounts in the accompanying consolidated statements of operations. Members are allocated a portion of profits or losses in accordance with their participation in the MA Plan based on the terms of the membership agreement. The amount of such allocated profits or losses cannot be estimated at the present time. Accordingly, they will be recognized in the period the amount of such allocations become known.

(dollars in thousands)

9. Other Assets

Other long-term assets consist of the following at June 30:

	2023	2022
Amortizable assets, net	**$ 1,280**	$ 1,764
Health insurance prepayment	**1,449**	1,449
Other investments	**897**	492
	$ 3,626	$ 3,705

Gross amortizable assets of $11,699 and $11,588 for the years ended June 30, 2023 and 2022, respectively, are amortized over the expected useful life of the asset on a straight-line basis. MHS has recorded accumulated amortization of $10,419 and $9,824 for the years ended June 30, 2023 and 2022, respectively. Amortization expense is included with depreciation and amortization on the consolidated statements of operations.

10. Reinsurance Receivable and Provision for Outstanding Losses

GIC management based the provision for losses relating to medical malpractice and general liability at June 30, 2023 on a report dated July 2022 prepared by GIC's independent actuaries, As of June 30, 2023 and 2022, GIC's outstanding losses undiscounted was $139,478 and $131,767, respectively, and the reinsurance receivable for such losses was $6,335 and $6,815, respectively, after factoring in actual losses paid to June 30. The estimates provided by the actuaries are based on the historical data of the program blended together with relevant insurance industry loss development statistics. See Note 17 for further information regarding policies and coverage.

Movement in the provision for outstanding losses is summarized as follows:

	2023	2022
Beginning balance	**$ 131,767**	$ 127,837
Less: outstanding losses recoverable	**(6,815)**	(8,853)
	$ 124,952	$ 118,984
Incurred, net of reinsurance:		
Current year	**$ 30,448**	$ 28,392
Prior years	**(16,712)**	(12,565)
	$ 13,736	$ 15,827
Paid, net of reinsurance, related to:		
Current year	**$ (590)**	$ (44)
Prior years	**(4,955)**	(9,815)
	$ (5,545)	$ (9,859)

(dollars in thousands)

	2023	2022
Net balance at year end	**$ 133,143**	$ 124,952
Add: outstanding losses recoverable	**6,335**	6,815
Balance at end of year	**$ 139,478**	$ 131,767
Less: current portion	**(6,889)**	(8,529)
Provision for outstanding losses, long term	**$ 132,589**	$ 123,238

In the opinion of GIC management, the provision for outstanding losses relating to losses reported and losses incurred but not reported at the consolidated balance sheet dates is adequate to cover the expected ultimate liability of GIC. However, due to the nature of the insurance risks assumed, these provisions are necessary estimates, and could vary from the amounts ultimately paid.

Consistent with most companies with similar insurance operations, GIC's provision for outstanding losses is ultimately based on management's reasonable expectations of future events. It is reasonably possible that the expectations associated with these amounts could change in the near term (i.e., within one year) and that the effect of such changes could be material to the consolidated financial statements.

GIC's long-term estimated provision for outstanding losses exceeds GIC's retention limits by $6,335 and $6,815 for the years ended June 30, 2023 and 2022, respectively, and are recorded as reinsurance receivable in the accompanying consolidated balance sheets. GIC's current reinsurance receivable is $1,030 and $1,025 as of the years ending June 30, 2023 and 2022, respectively, and are recorded as other amounts receivable, net in the accompanying consolidated balance sheets.

In the event that GIC's reinsurers are unable to meet their obligations under the reinsurance agreements, GIC would still be liable to pay all losses under the insurance policies it issues but would only receive reimbursement to the extent the reinsurers could meet their above-mentioned obligations. GIC believes that all amounts included in reinsurance balances receivable and recoverable in the accompanying consolidated balance sheets will be collected in full from the reinsurers.

(dollars in thousands)

11. Long-Term Debt

Long-term debt consists of the following at June 30:

	2023	2022
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2006; interest rate 5.69%; due July 1, 2036	**$ 24,020**	$ 25,120
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2007 B and C (converted); interest rate 1.48%; due July 1, 2024	**7,470**	11,220
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2016A; interest rate ranging from 3.50% to 5.00%; due July 1, 2042	**135,250**	135,250
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2016C; variable interest rate (1.17% at June 30, 2022); due July 1, 2042, subject to mandatory redemption on May 19, 2023	**55,795**	57,815
MHHEFA Revenue Bonds, Stella Maris Issue, Series 2018; variable interest rate (4.24% at June 30, 2022); due 2050	**16,745**	17,065
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2021; fixed interest rate 1.65%; due July 1, 2031	**44,780**	46,425
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2022A; fixed interest rate 2.84%; due July 1, 2031	**45,200**	45,200
MHHEFA Revenue Bonds, Mercy Medical Center Issue, Series 2022B; variable interest rate (2.06% at June 30, 2022); due July 1, 2031	**35,335**	35,335
Taxable Term Loan, Mercy Medical Center; interest rate 1.37%; due 2022	**-**	3,070
HUD mortgage loan; interest rate 2.64%; due 2046	**4,017**	4,145
Other	**38**	50
Total long-term debt	**368,650**	380,695
Add: Net unamortized premium	**5,845**	6,171
Less: Net unamortized debt issuance costs	**(2,313)**	(2,982)
Current portion	**(12,508)**	(12,059)
Long -term portion	**$ 359,674**	$ 371,825

(dollars in thousands)

Principal payments on long-term debt are as follows for the years ending June 30:

2024	$ 12,508
2025	12,925
2026	13,419
2027	13,823
2028	14,231
Thereafter	301,744
	$ 368,650

Pursuant to an amended and restated Master Loan Agreement, as supplemented (the Loan Agreement), the Obligated Group members have issued debt through Maryland Health and Higher Educational Facilities Authority (MHHEFA). Currently the Medical Center, MHS and MHF comprise the Obligated Group for Mercy Medical Center issues. Each Obligated Group member is jointly and severally liable for the repayments under the obligations of the Loan Agreement. As security for the performance of the obligations of the Obligated Group members under the Loan Agreement, the Obligated Group members have granted to MHHEFA a security interest in their receipts, subject to certain permitted encumbrances. In addition, the Medical Center has mortgaged to MHHEFA certain real and personal property of the Medical Center. The Loan Agreement contains certain restrictive, financial and nonfinancial covenants. Under the terms of the Loan Agreement and other loan agreements, certain funds are required to be maintained on deposit with the trustee or MHHEFA to provide for repayment of the obligations of the Obligated Group (see Note 6).

Under the provisions of the Series 2018 Bonds agreement, SMI is the obligated party and has granted to MHHEFA a security interest in all of its real property and the assignment of its leases. In addition, payments on the Series 2018 Bonds are secured by an irrevocable letter of credit provided by a commercial bank.

SMI is required to maintain certain deposits with a trustee and satisfy certain measures of financial performance as long as the Series 2018 Bonds are outstanding. As of June 30, 2023, management believes SMI was in compliance with the financial covenant requirements of the bond indenture.

Mercy Medical Center issue, series 2006 bonds

In August 2006, MHHEFA authorized the issuance, sale and delivery of the $35,000 Mercy Medical Center Series 2006 Revenue Bonds. The proceeds were loaned by MHHEFA to MMC to finance the construction of a new parking garage as well as the financing of certain routine capital expenditures.

Principal repayment of these bonds began on July 1, 2009 and is paid annually through July 1, 2036. Interest is paid semiannually on January 1 and July 1. Interest accrues at a fixed rate of 5.69%. The bonds are currently callable at par (100%).

Mercy Medical Center issue, series 2007B and C (converted)

In October 2007, MHHEFA authorized the issuance, sale and delivery of its $100,000 Revenue Bonds, Mercy Medical Center Issue, Series 2007B and C, the proceeds of which were loaned by MHHEFA to MMC to finance the construction of a replacement hospital facility. On April 1, 2010, $18,080 of the $50,000 Series 2007B and $11,920 of the $50,000 Series 2007C Bonds were converted to Bank Qualified Revenue Bonds with a fixed interest rate, terminating July 1, 2024. Principal repayment of the converted bonds began July 1, 2012 and is scheduled to be paid annually through July 1, 2024. Interest accrues at a fixed rate of 1.48%. The monthly interest payments on the Series 2007B and C Bonds are made directly to the bank.

The portion of the Series 2007B and C bonds that were not converted to Bank Qualified Bonds were refinanced with other MHHEFA Revenue bonds.

Mercy Medical Center issue, series 2016A

In March 2016, MHHEFA authorized the issuance, sale and delivery of its $135,250 Revenue Bonds, Mercy Medical Center Issue, Series 2016A. The proceeds were loaned by MHHEFA to MMC to advance refund $145,880 aggregate principal amount and $11,452 aggregate interest due until July 1, 2017 of the MMC Issue, Series 2007A Bonds. As of June 30, 2016, the 2007A bonds were defeased and on July 1, 2017 the Series 2007A Bonds were fully refunded.

Principal repayment of the Series 2016A begins on July 1, 2032 and is scheduled to be paid annually through July 1, 2042. Interest accrues at a fixed rate ranging from 3.5% to 5.0%. The Series 2016A bonds were issued net of an original issue premium of $9,327, which is being amortized over the life of the bonds using the straight-line method, which approximates the effective interest method.

Mercy Medical Center issue series 2016C

In May 2016, MHHEFA authorized the issuance, sale and delivery of its $65,450 Revenue Bonds, Mercy Medical Center, Series 2016C. The proceeds were loaned by MHHEFA to MMC to refund the $65,290 Series 2013 and Series 2013B bonds then outstanding. The Series 2016C bonds were issued as a non-bank qualified revenue bonds and directly purchased by a commercial bank. The direct bank purchase terminates on May 19, 2023, at which time the Series 2016C bonds will be subject to a mandatory purchase at their par value by MMC unless the bank and MMC agree to an extension. Originally, the Series 2016C bonds bore interest at a variable rate equal to 70% of one-month LIBOR plus 0.83%. Effective January 1, 2018, as a result of the Tax Cuts and Jobs Act, and by function of the debt agreements for tax law changes, the effective interest rate changed to a variable rate equal to 85% of one-month LIBOR plus 1.01%. In December 2018, the bank agreed to modify the interest rate to 70% of one-month LIBOR plus 1.15%. Interest is paid monthly. Annual principal repayment of Series 2016C bonds began on July 1, 2016 with maturity on July 1, 2042.

Stella Maris issue, series 2018 bonds

In December 2018, MHHEFA authorized the issuance, sale and delivery of its $21,000 Revenue Bonds, Stella Maris issue. The proceeds were loaned to SMI to refund Series 1997 Bonds and to partially finance the construction of a Transitional Care Center in Stella Maris. Principal repayment of these bonds began on July 1, 2019 and is scheduled to be paid annually through July 1, 2050. All Series 2018 Bonds are subject to redemption prior to maturity. Interest accrues at a variable rate based on SIFMA. Interest on the bonds is payable monthly. An annual letter of credit fee, equal to 0.73% of the letter of credit amount, is payable quarterly by SMI. The letter of credit expires December 19, 2028.

Mercy Medical Center issue, series 2021 bonds

In April 2021, MHHEFA authorized the issuance, sale and delivery of its $46,680 Revenue Bonds, Mercy Medical Issue, Series 2021 Bonds. The proceeds were loaned by MHHEFA to MMC to refund Series 2011 Bonds and to finance new equipment purchases for Mercy Medical Center. Principal repayment of these bonds began on July 1, 2021 and is scheduled to be paid annually through July 1, 2031. Interest accrues at a fixed rate based of 1.65%, payable monthly.

Mercy Medical Center issue, series 2022A

In June 2022, MHHEFA authorized the issuance, sale and delivery of its $45,200 Revenue Bonds, Mercy Medical Issue, Series 2022A Bonds. The proceeds were loaned by MHHEFA to MMC to refund Series 2012 Bonds for Mercy Medical Center. Principal repayment of these bonds begins on July 1, 2023 and is scheduled to be paid annually through July 1, 2031. Interest accrues at a fixed rate based of 2.84%, payable monthly.

Mercy Medical Center issue, series 2022B

In June 2022, MHHEFA authorized the issuance, sale and delivery of its $35,335 Revenue Bonds, Mercy Medical Issue, Series 2022B Bonds. The proceeds were loaned by MHHEFA to MMC to refund Series 2016B Bonds for Mercy Medical Center. Principal repayment of these bonds begins on July 1, 2032 and is scheduled to be paid annually through July 1, 2037. The Series 2022B bonds interest accrues at a variable rate equal to 0.79% of the one month secured overnight financing rate plus the applicable spread of 0.92%, payable monthly.

Mercy Medical Center Taxable Loan

On March 26, 2020 Mercy Medical Center issued a taxable loan though a commercial bank to fully refund the outstanding principal of the Series 2008 Bonds (converted). Interest accrues at a fixed rate of 1.37% and is paid monthly to the bank. Principal repayment of these bonds began on July 1, 2020, which was paid annually through July 1, 2022 when the loans were paid off.

HUD mortgage loan

The mortgage loan from the U.S. Department of Housing and Urban Development (HUD) was used by CSC to construct St. Elizabeth Hall. This original note was refinanced during the year ended June 30, 2013. The current note reflects an interest rate of 2.64% per annum with monthly installments of $20, including interest, with the final payment due January 1, 2046 and requires mortgage insurance of 0.45% of the average annual outstanding principal balance. The note also requires a debt service savings and property replacement reserve fund. The liability of CSC under the mortgage note is limited to the underlying value of the real estate collateral plus other amounts deposited with the lender.

Lines of credit

The Medical Center has a $50,000 operating line of credit with a commercial bank. At June 30, 2023 and 2022, the operating line of credit had $0 outstanding. As of June 30, 2023 and 2022, the interest rate on the outstanding line of credit draw was 6.97% and 3.55%, respectively, and is based on one-month LIBOR plus 1.75%. This line of credit agreement is scheduled to remain in effect until all obligations, including other debt held by the bank, are paid in full or terminated by the bank.

Interest rate swaps

MHS' primary objective for holding derivative financial instruments is to manage interest rate risk. MHS does not utilize interest rate swap agreements or other financial instruments for trading or other speculative purposes. The derivative financial instruments are recorded at fair value based upon information supplied by the counterparty as described in Note 12.

On December 1, 2004, the Medical Center entered into a fixed spread basis swap. The fixed spread basis swap matures on December 1, 2024 and the exchanges of cash flows with the counter party began March 1, 2005. The notional amount of the swap is $50,000. Pursuant to the swap agreement, the Medical Center pays the counter party a variable rate equal to the USD-SIFMA Municipal Swap Index and receives interest at a variable rate equal to the sum of 67% of USD-LIBOR-BBA plus 0.60%.

Simultaneously, with the issuance of the Series 2006 bonds, MMC entered into an interest rate swap agreement, which was amended in November 2014, with a counter party with a notional amount of $35,000 to convert the fixed rate structure to a variable rate. Under this amended agreement, MMC will receive a fixed interest rate of 5.69% and pay to the counter party the USD-SIFMA Municipal Swap Index plus 0.80%. The interest rate swap agreement matures on April 1, 2023. Additionally, under this amended agreement, MMC will continue to receive a fixed interest rate of 5.69% and now pay to the counter party the USD-SIFMA Municipal Swap Index plus 0.836%. The interest rate swap does not qualify for hedge accounting under generally accepted accounting principles.

The fair value of this contract is based on two components: (i) the accrued but unpaid periodic cash flows and (ii) the termination value as defined in the agreement. By definition, the termination value is equal to the bond amount multiplied by the difference between highest price in the marketplace and the bonds base price (100%) and the call price would be the highest price in the marketplace on the valuation date. This is due to the fact that MHS would be economically inclined to call the bonds at par versus paying any termination payment on the swap and the bonds are carried on MHS' books at par. With MHS prepared to call the bonds at par, the market price should immediately converge on the call price. Additionally, MHS has the right to optionally terminate the contract. The counter party does not have the right to optionally terminate the agreement. The counter party can only terminate the agreement prior to its stated maturity if an event of default or an additional termination event exists.

During October 2007, MMC entered into a fixed payer swap with a notional amount of $65,000, which was amended in July 2014. Pursuant to the amended swap agreement, MMC pays the counter party a fixed rate of 3.459% and receives a variable rate equal to 70% of USD-LIBOR-BBA. The interest rate swap agreement terminates on July 1, 2042. At June 30, 2023 and 2022, the fair value of the interest rate swap liability was $(7,003) and $(11,801), respectively, and is included in interest rate swap liabilities in the accompanying consolidated balance sheets.

MHS recognizes gains and losses from changes in fair values of interest rate swap agreements as non-operating revenue or expense within net other income in the accompanying consolidated statement of operations. The net cash paid or received under the swap agreements is recognized as an adjustment to interest expense. No termination payments would be required if the swap agreements are held to maturity.

Entering into interest rate swap agreements involves, to varying degrees, elements of credit, default, prepayment, market and documentation risk. Such risks involve the possibility that there will be no liquid market for these agreements, the counterparty to these agreements may default on its obligation to perform and there may be unfavorable changes in interest rates. The notional amounts of the swap agreements are used to measure the interest to be paid or received and do not represent the amount of exposure to credit loss. Exposure to credit loss is limited to the receivable amount, if any, which may be generated as a result of the swap agreements. Management believes that losses related to credit risk are remote.

An unrealized gain on interest rate swaps totaling $4,872 and $11,664 is reflected in the accompanying consolidated statements of operations for the fiscal years ended June 30, 2023 and 2022, respectively.

12. Fair Value of Financial Instruments

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

Cash and cash equivalents, patient accounts receivable, other amounts receivable, accounts payable and accrued expenses due to third-party payers and construction retainage: The carrying amounts reported in the consolidated balance sheets approximate fair value.

Short-term investments, funds held by trustee and board designated and donor restricted investments: Fair values, which are the amounts reported in the consolidated balance sheets, are based on quoted market prices, if available, or estimated using quoted market prices for similar securities.

Pooled separate accounts: NAV units, as determined by the custodian, are used to estimate fair value since 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.

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. The three levels of inputs that may be used to measure fair value are:

Level 1: Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities that are traded in an active exchange market, as well as U.S. Treasury securities.

Level 2: Observable input 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 2 assets and liabilities include debt securities with quoted market prices that are traded less frequently than exchange-traded instruments. This category generally includes certain U.S. government and agency mortgage-backed debt securities, corporate-debt securities, and alternative investments.

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. This category generally includes certain private debt and equity instruments and alternative investments.

The following discussion describes the valuation methodologies used for financial assets and liabilities 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 business, value, or financial position of MHS based on the fair value information of financial assets and liabilities presented below.

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial asset or liability, 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 or liability. Furthermore, the disclosed fair values do not reflect any premium or discount that could result from offering for sale at one time an entire holding of a particular financial asset or liability. Potential taxes and other expenses that would be incurred in an actual sale or settlement are not reflected in the amounts disclosed.

MHS uses techniques consistent with the market approach for measuring fair value of its Level 2 and Level 3 assets and liabilities. The market approach is a valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. Fair values of equity securities and fixed maturity securities have been determined by MHS 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. Cash equivalents comprise short-term fixed maturity securities and carrying amounts approximate fair values, which have been determined from public quotations, when available. Money markets and certificates of deposit comprise short-term fixed maturity securities. The carrying amounts approximate fair values, which have been determined from public quotations, when available.

MHS holds alternative investments that are not traded on national exchanges or over-the-counter markets. MHS is provided information on net asset value per share as a practical expedient for these investments calculated by the funds of funds' managers (who are investment advisors registered with the Securities and Exchange Commission) based on information provided by the managers of underlying funds.

(dollars in thousands)

Fair value of the interest rate swaps represents, or are derived from, mid-market values. Mid-market prices and inputs may not be observable, and instead valuations may be derived from proprietary or other pricing models based on certain assumptions regarding past, present and future market conditions. Some inputs may be theoretical, not empirical, and require subjective assumptions and judgments. Valuations may be based on assumptions as to the volatility of the underlying security, basket or index, interest rates, exchange rates, dividend yields, correlations between these or other factors, the impact of these factors upon the value of the security (including any embedded options), as well as issuer funding rates and credit spreads (actual or approximated) or additional relevant factors.

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

The following table presents the fair value hierarchy for financial instruments reported by MHS measured at fair value on a recurring basis as of June 30, 2023.

Assets	Level 1	Level 2	Level 3	Total Fair Value
Board designated and donor restricted investments:				
Cash and cash equivalents	$ 38,367	$ -	$ -	$ 38,367
Equity securities:				
Mutual funds:				
International emerging markets	55,607	-	-	55,607
Domestic mutual fund-equity income	31,077	-	-	31,077
Common stocks:				
Consumer discretionary	10,500	-	-	10,500
Consumer staples	9,351	-	-	9,351
Energy	4,719	-	-	4,719
Financials	14,531	-	-	14,531
Real estate	3,737	-	-	3,737
Health care	12,984	-	-	12,984
Industrials	13,926	-	-	13,926
Information technology	25,839	-	-	25,839
Materials	4,046	-	-	4,046
Miscellaneous	959	-	-	959
Foreign stocks/American deposit receipt	-	6,385	-	6,385
Fixed maturity:				
U.S. government and agencies:				
U.S. treasury bonds	10,886	-	-	10,886
Government agency bonds	-	8,728	-	8,728
Corporate bonds:				
Asset backed securities	-	982	-	982
Financial	-	2,647	-	2,647
Industrial	-	4,189	-	4,189
Other	-	6,656	-	6,656
Mutual bond funds	14,267	-	-	14,267
Municipal bonds	-	815	-	815
Total assets in the fair value hierarchy	$ 250,796	$ 30,402	$ -	281,198
Investments measured at NAV [(a)]				35,556
Total board designated and donor restricted investments				$ 316,754

(dollars in thousands)

(continued)

Assets	Level 1	Level 2	Level 3	Total Fair Value
Restricted investments:				
Cash and cash equivalents	$ -	$ -	$ -	$ -
Exchange traded funds	33,093	-	-	33,093
Equity mutual fund	-	6,238	-	6,238
U.S. treasury securities	46,817	-	-	46,817
Corporate bonds	-	16,990	-	16,990
Mortgage-backed securities	-	1,338	-	1,338
Asset backed securities	-	42,894	-	42,894
Total restricted cash and investments	$ 79,910	$ 67,460	$ -	$ 147,370
Short-term investments:				
Cash and cash equivalents	$ -	$ 1,778	$ -	$ 1,778
Total short-term investments	$ -	$ 1,778	$ -	$ 1,778
Funds held by trustee (current):				
Money market	$ 13,427	$ -	$ -	$ 13,427
Funds held by trustee (non-current):				
Cash and cash equivalents	1,601	-	-	1,601
Total assets in the fair value hierarchy	$ 15,028	$ -	$ -	453,752
Investments measured at NAV [(a)]				35,556
Total investments at fair value				$ 480,930

Liabilities	Level 1	Level 2	Level 3	Total Fair Value
Interest rate swaps	$ -	$ 6,529	$ -	$ 6,529
Total liabilities at fair value	$ -	$ 6,529	$ -	$ 6,529

[(a)] *In accordance with current accounting standards, certain investments that were measured at NAV per share (or its equivalent) have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the line items presented in the consolidated balance sheets.*

(dollars in thousands)

The following table presents the fair value hierarchy for financial instruments reported by MHS measured at fair value on a recurring basis as of June 30, 2022.

Assets	Level 1	Level 2	Level 3	Total Fair Value
Board designated and donor restricted investments:				
Cash and cash equivalents	$ 20,313	$ -	$ -	$ 20,313
Equity securities:				
Mutual funds:				
International emerging markets	37,872	-	-	37,872
Domestic mutual fund-equity income	26,055	-	-	26,055
Common stocks:				
Consumer discretionary	8,475	-	-	8,475
Consumer staples	9,548	-	-	9,548
Energy	2,785	-	-	2,785
Financials	14,468	-	-	14,468
Real estate	4,154	-	-	4,154
Health care	11,161	-	-	11,161
Industrials	10,567	-	-	10,567
Information technology	19,909	-	-	19,909
Materials	2,292	-	-	2,292
Miscellaneous	1,871	-	-	1,871
Foreign stocks/American deposit receipt	-	6,633	-	6,633
Fixed maturity:				
U.S. government and agencies:				
U.S. treasury bonds	10,829	-	-	10,829
Government agency bonds	-	7,136	-	7,136
Corporate bonds:				
Asset backed securities	-	1,359	-	1,359
Financial	-	3,657	-	3,657
Industrial	-	8,082	-	8,082
Other	-	2,653	-	2,653
Mutual bond funds	23,648	-	-	23,648
Municipal bonds	-	805	-	805
Total assets in the fair value hierarchy	$ 203,947	$ 30,325	$ -	234,272
Investments measured at NAV [(a)]				41,076
Total board designated and donor restricted investments				$ 275,348
Restricted investments:				
Cash and cash equivalents	$ 5,507	$ -	$ -	$ 5,507
Exchange traded funds	23,831	-	-	23,831
Equity mutual fund	-	12,680	-	12,680
U.S. treasury securities	36,706	-	-	36,706
Corporate bonds	-	14,441	-	14,441
Mortgage-backed securities	-	4,045	-	4,045
Asset backed securities	-	27,478	-	27,478
Total restricted cash and investments	$ 66,044	$ 58,644	$ -	$ 124,688
Short-term investments:				
Cash and cash equivalents	$ 1,656	$ -	$ -	$ 1,656
Total short-term investments	$ 1,656	$ -	$ -	$ 1,656

(dollars in thousands)

(continued) Assets	Level 1	Level 2	Level 3	Total Fair Value
Funds held by trustee (current):				
Cash and cash equivalents	$ 8,004	$ -	$ -	$ 8,004
Fixed maturity:				
U.S. treasury bonds	7,658	-	-	7,658
Total funds held by trustee (current)	15,662	-	-	15,662
Funds held by trustee (non-current):				
Cash and cash equivalents	1,504	-	-	1,504
Funds held by trustee (non-current)	1,504	-	-	1,504
Total assets in the fair value hierarchy	$ 288,813	$ 88,969	$ -	387,246
Investments measured at NAV [(a)]				41,076
Total investments at fair value				$ 418,859

Liabilities	Level 1	Level 2	Level 3	Total Fair Value
Interest rate swaps	$ -	$ 11,401	$ -	$ 11,401
Total liabilities at fair value	$ -	$ 11,401	$ -	$ 11,401

[(a)] *In accordance with current accounting standards, certain investments that were measured at NAV per share (or its equivalent) have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the line items presented in the consolidated balance sheets.*

The following table summarizes investments for which fair value is measured using the NAV per share practical expedient as of June 30, 2023 and 2022.

	Fair Value at June 30, 2023	**Fair Value at June 30, 2022**	**Unfunded Commitments**	**Other Redemption Restrictions**	**Redemption Notice Period**
Multi-Strategy Fund [(1)]	**$ 8,395**	$ 8,217	None	None	65 days
Stepstone Opportunities [(2)]	**13,498**	13,911	510	None	None
Emerging Markets [(3)]	**-**	7,800	None	None	None
Other	**13,663**	11,148	-	-	-
	$ 35,556	$ 41,076			

[(1)] The multi-strategy fund is event-driven with a focus on opportunities to exploit situations in which announced or anticipated events create opportunities to invest in securities and other financial instruments at a discount to their exit values. The fund also invests in a long/short equities portfolio of securities that can be readily valued and trade at a discount or premium to the fair value of the underlying assets. The fund permits semiannual redemption subject to 65 days advance written notice.

[(2)] The fund's objective is to seek long-term capital appreciation by investing primarily by making, holding, and disposing of privately negotiated equity and equity-related investments principally in a diversified group of operating companies.

[(3)] The fund's objective is to provide long-term total return in excess of the MSCI Emerging Markets Index. The fund is primarily invested in international equities in emerging markets.

13. Defined Contribution and Profit-Sharing Plans

MHS had a qualified 401(k) plan covering substantially all employees of the Medical Center and SMI who have completed at least one year of service and are at least twenty-one years of age. MHS made an annual contribution on behalf of all eligible employees based on either the employee's contributions to the 401(k) plan or their annual compensation. MHS had matched, on a dollar-for-dollar basis (based on age and years of service thresholds) the amount contributed by the employee, not to exceed 6% of the employee's salary. MHS' contributions to the 401(k) plan for all participants employed prior to April 1, 1997 for Medical Center employees or July 1, 1997 for SMI employees, vested at a rate of 25% annually and completely vested on April 1, 2001 for Medical Center employees and July 1, 2001 for SMI employees. MHS' contributions for all participants employed on or after April 1, 1997 for Medical Center employees or July 1, 1997 for SMI employees vested after four years of service, with no vesting prior to four years of service. Effective January 1, 2018, Mercy made the following changes to the 401(k) plan: The age and service requirement used to calculate Mercy's match will be made at the beginning of each calendar quarter (as opposed to January 1). Additionally, the vesting schedule was changed to a 3-year cliff as described below. There is no age limit for participation in the plans which occurred retroactive to January 1, 2016.

Effective January 1, 2019, the plan was frozen and all contributions for MHS subsequent to this date are being directed to the 403(b) Plan. MHS has a qualified 403(b) plan covering substantially all employees of Mercy Medical Center and SMI. Eligibility for the employer match begins after the completion of one year of service. MHS makes a quarterly contribution on behalf of all eligible employees based on the employee's contributions into the 403(b). MHS matches up to 50% of an employee's contribution not to exceed 6% of the employee's salary. The MHS match increases based on age and years of services threshold up to 100% of the amount contributed by the employee not to exceed 6% of the employee's salary. Maryland Family Care (MFC) employees are matched up to 50% of their contribution not to exceed 6% of the employee's salary and their match does not increase with age and years of service. MHS' contributions into the 403(b) for all participants are vested after three years of service, with no vesting prior to three years of service. By December 31, 2021, generally all participants who had existing 401(k) Plan employer matching contribution accounts who were still employed by Mercy were fully vested.

Effective April 1, 2022, the 401(k) Plan was merged into the 403(b) Plan, with the 403(b) Plan being the surviving plan. Additionally, effective January 1, 2023, eligibility for the match will begin after the completion of six (6) months of service. Lastly, effective July 1, 2023, Mercy Health Services will transition from a revenue sharing administrative fee structure to a transparent administrative fee structure for all qualified and non-qualified retirement plans.

Contributions under these plans totaled approximately $6,848 and $6,412 for the years ended June 30, 2023 and 2022, respectively.

14. Post-Retirement Benefit Plan

MMC has an unfunded contributory health and medical post-retirement benefit plan available to all eligible employees who meet certain age and length of service requirements as defined by the plan. The plan provides for health and medical benefits including primary care physician and specialist visits, hospitalization and emergency care, prescription drugs, vision care and Medicare supplemental coverage.

(dollars in thousands)

The following table sets forth the components of the MHS obligation at June 30:

	2023	2022
Change in benefit obligation:		
Benefit obligation at beginning of year	**$ 7,239**	$ 8,740
Service cost	**35**	52
Interest cost	**312**	242
Actuarial gain and assumption changes	**(993)**	(1,455)
Employer portion of benefits paid	**(486)**	(340)
Benefit obligation at end of year	**6,107**	7,239
Change in plan assets:		
Employer contribution	**486**	340
Benefits paid	**(486)**	(340)
Fair value of plan assets at end of year	**-**	-
Unfunded status	**(6,107)**	(7,239)
Accrued post-retirement benefit cost	**(6,107)**	(7,239)
Less current portion included in accounts payable and accrued expenses	**328**	328
Total accrued post-retirement benefit cost, long-term portion	**$ (5,779)**	$ (6,911)

Net periodic post-retirement benefit cost included the following for the years ended June 30:

	2023	2022
Service cost - benefits attributed to service during the period	**$ 35**	$ 52
Interest cost on accumulated post-retirement benefit obligation	**312**	242
Net amortization	**-**	107
Net post-retirement benefit cost	**$ 347**	$ 401

Amounts not yet recognized as a component of net periodic pension cost include net actuarial gain of $1,445 and $449 as of June 30, 2023 and 2022, respectively. Estimated amortization of the net loss of $347 is expected to be recognized in benefit expenses in the next fiscal year.

The weighted average discount rate used in determining the accumulated post-retirement benefit obligation (APBO) for the plan was 4.90% and 4.41% for the years ended June 30, 2023 and 2022, respectively. For measurement purposes, the health care cost trend rates used in determining the APBO for the plan were 7.5% and 6.0% in 2023 and 2022.

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

	Benefit Payments
2024	$ 328
2025	$ 348
2026	$ 367
2027	$ 378
2028	$ 385
Next 5 years	$ 1,967

(dollars in thousands)

15. Retirement Annuity Plan

MMC had a pension plan that was terminated on April 1, 1997 and established a retirement annuity plan under which certain participants of the terminated plan were entitled to annuity payments. Participants in the plan include (a) the retirees and beneficiaries entitled to benefits from the terminated plan on April 1, 1997 and (b) other participants with benefits worth more than $4 that elected an annuity. All benefits are vested and based on the frozen accrued benefits at April 1, 1997.

The measurement dates for fiscal years 2023 and 2022 were June 30, 2023 and June 30, 2022, respectively. The following table sets forth the funded status of the retirement annuity plan and amounts recognized in accompanying consolidated financial statements as of and for the years ended June 30:

	2023	2022
Change in benefit obligation:		
Benefit obligation at beginning of year	**$ 3,097**	$ 3,741
Interest cost	**100**	97
Actuarial gain	**(225)**	(181)
Benefits paid	**(478)**	(560)
Benefit obligation at end of year	**2,494**	3,097
Change in plan assets:		
Fair value of plan assets at beginning of year	**1,046**	609
Actuarial return on plan assets	**13**	(3)
Employer contribution	**-**	1,000
Benefits paid	**(478)**	(560)
Fair value of plan assets at end of year	**581**	1,046
Unfunded status/accrued benefit cost (Note 23)	**$ (1,913)**	$ (2,051)
Net periodic pension cost:		
Interest cost	**$ 100**	$ 97
Expected return on plan assets	**(68)**	(40)
Amortization net (gain) loss	**111**	161
Net periodic pension cost	**$ 143**	$ 218

Amounts not yet recognized as a component of net periodic pension cost include net actuarial loss of $1,054 and $1,336 as of June 30, 2023 and 2022, respectively. There is no estimated amortization of the net loss expected to be recognized in net periodic pension costs in the next fiscal year. There is no minimum projected required contribution for the period ending June 30, 2024.

The discount rate to estimate the benefit obligation as of June 30, 2023 and 2022 was 4.25% and 2.75%, respectively. The expected rate of return on plan assets to estimate the benefit obligation was 6.5% for 2023 and 2022.

The weighted-average asset allocations in the plan as of June 30, 2023 and 2022, by asset category were as follows:

	2023	2022
Asset Category:		
Cash and cash equivalents	**100%**	100%
Total	**100%**	100%

(dollars in thousands)

The fair values of plan assets on a recurring basis as of June 30, 2023 by asset category are as follows:

Assets	Level 1	Level 2	Level 3	Total Fair Value
Cash and cash equivalents:				
Cash	**$ 581**	**$ -**	**$ -**	**$ 581**
Total assets fair value	**$ 581**	**$ -**	**$ -**	**$ 581**

The fair values of plan assets on a recurring basis as of June 30, 2022 by asset category are as follows:

Assets	Level 1	Level 2	Level 3	Total Fair Value
Cash and cash equivalents:				
Cash	$ 1,045	$ -	$ -	$ 1,045
Total assets fair value	$ 1,045	$ -	$ -	$ 1,045

There were no significant transfers between levels for the years ended June 30, 2023 and 2022.

The following benefit payments are expected to be paid for the following years ending June 30:

	Benefit Payments
2024	$ 432
2025	$ 389
2026	$ 346
2027	$ 306
2028	$ 267
Next 5 years	$ 864

16. Net Assets With Donor Restrictions

Net assets with donor restrictions are available for the following health care services and endowment funds at June 30:

	2023	2022
Mercy Forever campaign	**$ 25,866**	$ 20,660
Departmental expenses	**9,988**	8,691
Other	**4,064**	5,557
Pastoral care	**4,516**	4,516
Capital improvements	**2,657**	2,410
Research programs	**2,193**	1,997
Indigent care	**806**	1,065
SMI hospice endowment	**1,055**	1,055
Weinberg endowment	**1,000**	1,000
Education programs	**739**	678
Dr. Goodman endowment	**123**	123
	$ 53,007	$ 47,752

(dollars in thousands)

17. Commitments and Contingent Liabilities

Litigation

MHS has outstanding litigation involving claims brought against it in the normal course of business. 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, MHS receives inquiries, request for information regarding clinical procedures, licensing, billing or medical record documentation matters from various State and Federal agencies. MHS responds to such requests and provides any detailed information requested. Attorneys for MHS are representing MHS in all of the above matters. Management is currently unable to estimate, with reasonable certainty, the possible loss, or range of loss, if any, for such lawsuits and investigations. MHS is also subject to asserted and unasserted claims (in addition to litigation) encountered in the ordinary course of business. 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 a material adverse effect on the future financial position, results of operations and liquidity of MHS.

Self-insurance programs

As discussed in Notes 1 and 10, GIC provides general and professional liability coverage to MHS and its subsidiaries. GIC's policies provide primary and certain excess liability coverage. GIC retains the risk related to the primary policy and reinsures the whole of the excess policies. While insurance policy limits vary by year, management believes the amounts are appropriate.

GIC's primary coverage limits for the years ended June 30 are:

	2023	**2022**
Healthcare Professional Liability (HPL) and Managed Care Organization Liability (MCO)	**$9,000 per related loss event** **$42,000 aggregate**	$9,000 per related loss event $42,000 aggregate
Commercial General Liability (CGL)	**$9,000 per occurrence** **$42,000 aggregate**	$9,000 per occurrence $42,000 aggregate

GIC's primary coverage for HPL is $9,000 per loss event. GIC provides excess coverage for HPL and MCO in the aggregate amount of $75,000 in excess of $9,000 and $9,000 for related loss events and in excess of $42,000 and $42,000 for fiscal years 2023 and 2022, respectively. GIC provides excess coverage for CGL in the aggregate amount of $75,000 in excess of $9,000 and $9,000 per occurrence and in excess of $42,000 and $42,000 aggregate for fiscal years 2023 and 2022, respectively. All excess coverage is reinsured by commercial insurance companies.

In management's opinion, the assets of GIC are sufficient to meet its obligations as of June 30, 2023. If the financial condition of GIC were to materially deteriorate in the future, and GIC were unable to pay its claim obligations, the responsibility to pay those claims would return to MHS.

MHS and certain of its subsidiaries are self-insured against employee medical claims. Plan expenses include claims incurred and provisions for unreported claims. However, the program has an annual aggregate stop loss provision per employee.

MHS and certain of its subsidiaries are self-insured in the State of Maryland for the use and benefit of all employees of MHS for worker's compensation. The State of Maryland requires any self-insured employer to provide a workers' compensation surety bond issued by a corporate surety company that meets the State's financial rating under A.M. Best. MHS has had a surety bond in place since 1997 currently written by Fidelity and Deposit Company of Maryland in the amount of $2,800. All past, present, existing and potential liability under this bond shall remain in effect and to the benefit of the State of Maryland.

MHS and certain of its subsidiaries are self-insured against unemployment claims and have surety bonds of $1,633 for the Medical Center and $370 for SMI. The amounts change each October 1 as dictated by the Maryland Department of Licensing and Regulation.

18. Maryland Health Services Cost Review Commission

The Medical Center's charges are subject to review and approval by the State of Maryland Health Services Cost Review Commission (HSCRC). Management has made the required filings with the Commission and believes the Medical Center to be in compliance with the Commission's requirements. The Commission has jurisdiction over hospital reimbursement in Maryland by agreement with the Centers for Medicare and Medicaid Services. This agreement is based on a waiver from the Medicare Prospective Payment System reimbursement principles granted under Section 1814(b) of the Social Security Act. On January 1, 2014, Maryland's All-Payer Hospital System Modernization was approved by CMS. This was a new global budget arrangement which set a fixed revenue amount for the upcoming year, without fluctuation due to utilization or case mix. This was a five-year demonstration where Maryland successfully made significant progress toward reducing costs inside and outside of the hospital as well as improving patient care. Beginning January 2019, the new "Total Cost of Care Model" (the Model) was approved and builds upon the successes of the All-Payer 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.

The Commission established an uncompensated care fund whereby all hospitals are required to contribute 0.75% of revenues to this fund to help provide for the cost associated with uncompensated care for certain Maryland hospitals above the State average. In December 2008, the Commission modified this mechanism to finance uncompensated care statewide. The policy implemented 100% pooling and all Maryland hospitals have the same percentage of uncompensated care in rates. High uncompensated care hospitals receive funds and low uncompensated care hospitals pay into the fund. The Medical Center had net receipts of $1,835 and $1,263 for 2023 and 2022, respectively, related to its participation in the uncompensated care fund mechanism.

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

Under the global budget arrangement established by the HSCRC, the Medical Center is required to modify revenue rates based on regulated patient volume. The Medical Center volumes and set HSCRC rates created a minor Global Budget undercharge of $939 and $1,400, for fiscal years 2023 and 2022, respectively.

(dollars in thousands)

The U.S. Federal Housing Administration (FHA) has contracted with CSC under Section 8 of Title II of the Housing and Community Development Act of 1974 to make housing assistance payments to CSC on behalf of certified tenants. For fiscal years 2023 and 2022, the maximum contract commitment was $1,440 and $1,380 per year, respectively. During the years ended June 30, 2023 and 2022, CSC received housing assistance payments of $1,130 and $1,008, respectively, which are included in patient service revenue in the accompanying consolidated statements of operations. The contract automatically renews each year on April 1 with an expiration date of March 31, 2033, subject to renewal at that time.

19. Functional Expenses

MHS and its subsidiaries provide general health care services to patients within what they consider their geographic service areas. Expenses related to providing these services, based on management's estimates of expense allocations, are as follows for the years ended June 30:

	2023			
	Healthcare Services	General and Administrative	Fundraising	Total
Salaries and benefits	**$ 441,868**	**$ 66,136**	**$ 1,791**	**$ 509,795**
Supplies	**190,303**	**6,191**	**77**	**196,571**
Other purchased services	**42,252**	**20,765**	**197**	**63,214**
Insurance	**19,587**	**2,507**	**-**	**22,094**
Professional fees	**21,003**	**1,446**	**8**	**22,457**
Depreciation and amortization	**31,564**	**11,671**	**-**	**43,235**
Interest	**8,551**	**4,704**	**-**	**13,255**
Repairs	**14,746**	**4,945**	**199**	**19,890**
Total	**$ 769,874**	**$ 118,365**	**$ 2,272**	**$ 890,511**

	2022			
	Healthcare Services	General and Administrative	Fundraising	Total
Salaries and benefits	$ 413,570	$ 66,404	$ 1,794	$ 481,768
Supplies	185,487	6,451	52	191,990
Other purchased services	41,064	20,654	173	61,891
Insurance	20,001	3,163	-	23,164
Professional fees	20,177	1,938	-	22,115
Depreciation and amortization	32,341	11,688	-	44,029
Interest	8,522	4,674	-	13,196
Repairs	14,068	4,182	223	18,473
Total	$ 735,230	$ 119,154	$ 2,242	$ 856,626

The accompanying consolidated financial statements report certain expense categories that are attributable to more than one health care service or support function. 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.

(dollars in thousands)

20. Liquidity and Availability

As of June 30, 2023 and 2022 , MHS had working capital of approximately $187,324 and $175,932, respectively, and average days (based on normal expenditures) cash on hand of 246 and 242, respectively.

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

	2023	2022
Cash and cash equivalents	**$ 261,559**	$ 283,318
Patient accounts receivable, net	**80,464**	77,139
Other accounts receivables, net	**4,734**	7,100
Short-term investments	**1,778**	1,656
Current portion of funds held by trustee	**13,427**	15,662
Total	**$ 361,962**	$ 384,875

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

21. Certain Risks and Uncertainties

Regulation and reimbursement

MHS provides health care services primarily through an acute care hospital in Baltimore City and a long-term care facility in Baltimore County, Maryland.

MHS and other healthcare providers in Maryland are subject to certain inherent risks, including the following:

- Dependence on revenues derived from reimbursement by the federal Medicare and State Medicaid programs;
- Regulation of hospital rates by the Commission;
- Government regulation, government budgetary constraints and proposed legislative and regulatory changes; and
- Lawsuits alleging malpractice and related claims.

Such inherent risks require the use of certain management estimates in the preparation of the consolidated financial statements of MHS, and it is reasonably possible that a change in such estimates may occur.

The Medicare and state Medicaid reimbursement programs represent a substantial portion of MHS' revenues and MHS' operations are subject to a variety of other federal, state and local regulatory requirements. Failure to maintain required regulatory approvals and licenses and/or changes in such regulatory requirements could have a significant adverse effect on MHS. Changes in federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on MHS.

The federal government and many states have aggressively increased enforcement under Medicare and Medicaid anti-fraud and abuse laws and physician self-referral laws. Recent federal initiatives have prompted a national review of federally funded health care programs. In addition, the federal government and many states have implemented programs to audit and recover potential overpayments to providers from the Medicare and Medicaid programs. MHS has implemented a compliance program to monitor conformance with applicable laws and regulations, but the possibility of future governmental review and enforcement action exists. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

As a result of federal health care reform legislation, substantial changes are underway in the U.S. health care delivery system. Such legislation includes numerous provisions affecting the delivery of health care services, the financing of health care costs, reimbursement of health care providers, and the legal obligations of health insurers, providers and employers. These provisions are currently slated to take effect at specified times over the next decade. The known impact of all currently applicable federal health care reform legislation has been accounted for in the consolidated financial statements for the year ended June 30, 2023.

Investments

MHS and certain of its subsidiaries have funds on deposit with financial institutions in excess of amounts insured by the Federal Deposit Insurance Corporation.

Certain alternative investments held in the MHS portfolio are exposed to potential risks in excess of the risks associated with the other investments in the MHS portfolio. These include, but are not limited to, the following potential risks:

- limited or no liquidity (including “side pocket” arrangements),
- derivative financial instruments that expose the investment funds to market risk (if the market value of the contract is higher or lower than the contract price at the maturity date) and credit risk (arising from the potential inability of counterparties to perform under the terms of the contracts),
- investment in non-marketable securities that are valued without the benefit of an active secondary market,
- substantially less regulation, and
- no current income production.

22. Endowment

Current accounting standards provide guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Act of 2006 (UPMIFA) and additional disclosures about an organization’s endowment funds. In 2008, the State of Maryland adopted UPMIFA.

The MHS endowments consist of three individual funds established for a variety of purposes. The endowments include both endowment funds with donor restrictions and funds designated by the board of trustees to function as endowments. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the board of trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The board of trustees of MHS has interpreted the Maryland State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, MHS classifies as net assets with donor restrictions (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts donated to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the endowment fund with donor restrictions is classified as net assets with donor restrictions until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, MHS considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

(dollars in thousands)

1. The duration and preservation of the fund
2. The purposes of the organization and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the organization
7. The investment policies of the organization

MHS has adopted an investment policy for endowment assets that attempts to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of funds with donor restrictions that must be held in perpetuity.

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

At June 30, 2023, the endowment net asset composition by type of fund consisted of the following:

	Without Donor Restriction	With Donor Restriction	Total
Donor-restricted funds	**$ -**	**$ 2,627**	**$ 2,627**

At June 30, 2022, the endowment net asset composition by type of fund consisted of the following:

	Without Donor Restriction	With Donor Restriction	Total
Donor-restricted funds	$ -	$ 2,446	$ 2,446

Changes in endowment net assets for the fiscal year ended June 30, 2023, consisted of the following:

	Without Donor Restriction	With Donor Restriction	Total
Endowment net assets, beginning of year	**$ -**	**$ 2,446**	**$ 2,446**
Investment return:			
Investment loss	**-**	**181**	**181**
Endowment net assets, end of year	**$ -**	**$ 2,627**	**$ 2,627**

(dollars in thousands)

Changes in endowment net assets for the fiscal year ended June 30, 2022, consisted of the following:

	Without Donor Restriction	With Donor Restriction	Total
Endowment net assets, beginning of year	$ -	$ 2,839	$ 2,839
Investment return:			
Investment loss	-	(335)	(335)
Appropriation of endowment asset for expenditure	-	(58)	(58)
Endowment net assets, end of year	$ -	$ 2,446	$ 2,446

23. Other Long-Term Liabilities

Other long-term liabilities consist of the following at June 30:

	2023	2022
Retirement annuity plan	**1,913**	2,051
Other	**2,370**	1,701
	$ 4,283	$ 3,752

24. Leases

MHS leases certain equipment and office buildings under the terms of non-cancellable operating leases. For leases with terms greater than 12 months, the related right-of-use assets and right-of-use obligations are recorded at the present value of lease payments over the term. Many of the leases include rental escalation clauses and renewal options that are factored into the determination of lease payments when appropriate.

Rental expense associated with finance leases was $7,638 and $6,399 for the years ended June 30, 2023 and 2022, respectively, which is recorded in the consolidated financial statements as other purchased services. These amounts approximated the cash paid associated with finance leases for the years then ended.

Current operating lease liabilities are included in operating lease liability, current in the accompanying consolidated balance sheets. Noncurrent operating lease liabilities are included in the operating lease liabilities in the accompanying consolidated balance sheets.

(dollars in thousands)

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

	2023	2022
Operating leases:		
Right-of-use operating lease assets	**$ 40,302**	$ 43,476
Current operating lease liabilities	**$ 4,012**	$ 4,012
Noncurrent operating lease liabilities	**38,039**	40,689
Total operating lease liabilities	**$ 42,051**	$ 44,701

	2023	2022
Other information:		
Weighted-average remaining lease term – equipment operating leases	**2.04 years**	2.94 years
Weighted-average remaining lease term – property Operating leases	**33.14 years**	32.66 years
Weighted-average discount rate – operating leases	**3.81%**	3.81%

The following is a schedule of lease liability maturities related to operating leases with third parties for the years ending June 30:

	Equipment	Property	Total
2024	$ 1,162	$ 2,993	$ 4,155
2025	706	3,040	3,746
2026	208	3,058	3,266
2027	-	3,066	3,066
2028	-	2,950	2,950
Thereafter	-	63,041	63,041
Total	2,076	78,148	80,224
Less: interest	(90)	(38,083)	(38,173)
Lease liability	$ 1,986	$ 40,065	$ 42,051

25. COVID-19 Pandemic

During 2020, the World Health Organization declared the outbreak of COVID-19, a novel strain of Coronavirus, a pandemic. The coronavirus outbreak has been disrupting supply chains and affecting operations across a range of industries. The ultimate extent of the impact of the outbreak on the MHS' operational and financial performance depends on certain developments, including the duration and spread of the outbreak, impact on patients, employees and vendors and governmental, regulatory and private sector responses. The consolidated financial statements do not reflect any adjustments as a result of the subsequent increase in economic uncertainty.

In response to the COVID-19 pandemic, the CARES Act was signed into law on March 27, 2020. One provision of the CARES Act was the establishment of the Provider Relief Funds, administered by HHS. The Provider Relief Funds have been distributed to healthcare providers throughout the country to support the battle against the COVID-19 pandemic. To date, the system has received $25,600 of distributions from this fund. These funds are intended to reimburse qualifying expenses and lost revenues attributable to COVID-19 and are subject to the terms, conditions and regulatory requirements set forth by HHS. If the total distributions received by MHS exceed the cumulative amount of qualifying expenses and lost revenues attributable to COVID-19, any excess funding may be subject to recoupment. The Provider Relief Funds are accounted for as conditional contributions and related revenues are recognized as conditions are substantially met. During the year ended June 30, 2022, the System recognized approximately $1,647, in the accompanying consolidated statements of operations and changes in net assets. The amounts recognized as income are subject to future audits and potential adjustments, which could be material and result in recoupments. Management is of the belief that the System is in compliance with the terms and conditions of the Provider Relief Funds and that there will not be recoupments.

During the year ended June 30, 2023 MHS received and recognized $2,197 from the Coronavirus State and Local Fiscal Recovery Funds (SLFRF), a part of the American Rescue Plan, passed through from the state of Maryland. The purpose of the funds received through the SLFRF is to provide premium pay to eligible workers performing essential work during the pandemic for workers up to $13 per hour.

In 2020, the Center for Medicare and Medicaid Services enhanced the Accelerated and Advance Payment (AAP) Program. The program enhancement was designed to increase cash flow to Medicare providers and suppliers impacted by COVID-19. In April 2020, MHS received approximately $77,159 from the CMS AAP program. The funds received from the AAP are an advance that providers must pay back. These funds have been used to offset actual Medicare claims subject to final determination by CMS. On September 30, 2020, the Continuing Appropriations Act was signed into law which includes provision to relax the recoupment of Medicare Advance Payments, including delaying recoupment for one year from when the advances were made. It also staggers the percentage of claims processed that will be recouped over a twenty-nine-month period. These funds are shown on the accompanying consolidated balance sheets as Medicare advance contract liability until recouped. As of June 30, 2023 and 2022 approximately $77,159 and $61,950 have been recouped by CMS, respectively.

With the national emergency declaration under the Stafford Act on March 13, 2020, private nonprofit organizations have up to 30 days after the end of the national emergency period to apply for federal funding through FEMA. In 2023 and 2022, MHS applied for and received monies from FEMA to assist in the reimbursement of capital projects during fiscal years ending June 30, 2023 and 2022. As of the years ended June 30, 2023 and 2022, MHS recognized approximately $298 and $233 in cost reimbursement related to capital projects, respectively. Management is of the belief that MHS is in compliance with the terms and conditions of these federal programs and that there will not be recoupments.

26. Subsequent Events

Management evaluated all events and transactions for potential recognition and disclosure that occurred after June 30, 2023 and through September 12, 2023, the date the consolidated financial statements were issued.

Supplementary Financial Information

Mercy Health Services, Inc. and Subsidiaries
Consolidating Balance Sheet Information
June 30, 2023
(in thousands)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
ASSETS							
Current assets:							
Cash and cash equivalents	$ 832	$ 10,443	$ 236,705	$ 12,808	$ 771	$ -	$ 261,559
Short-term investments	-	-	-	1,778	-	-	1,778
Current portion of funds held by trustee	-	-	12,883	544	-	-	13,427
Resident prepayment deposits	-	-	-	797	-	-	797
Patient accounts receivable, net	-	-	50,392	9,341	20,731	-	80,464
Other amounts receivable, net	547	-	6,320	784	3,837	(6,754)	4,734
Current pledges receivable, net	-	2,595	-	-	-	-	2,595
Supplies inventory	-	-	11,753	188	2,926	-	14,867
Other current assets	-	-	2,728	15	792	-	3,535
Total current assets	1,379	13,038	320,781	26,255	29,057	(6,754)	383,756
Property and equipment, net	-	-	472,521	49,779	21,199		543,499
Investments and other assets:							
Funds held by trustee, less current portion	-	-	-	1,601	-	-	1,601
Board designated and donor restricted investments	26,979	25,387	240,795	23,593	-	-	316,754
Restricted investments	-	2,055	145,315	-	-		147,370
Long-term Investments			-			-	-
Long-term pledges receivable, net	-	21,815	44,231	7,152	-	(51,383)	21,815
Investments in and advances to affiliates	17,627	(9,977)	9,597	(5,164)	(4,519)	(3,000)	4,564
Reinsurance receivable	-	-	6,335	6,235	-	(6,235)	6,335
Right of use assets	-	-	31,830	-	8,472	-	40,302
Other assets	138	-	2,197	178	1,113	-	3,626
Total assets	$ 46,123	$ 52,318	$ 1,273,602	$ 109,629	$ 55,322	$ (67,372)	$ 1,469,622

Mercy Health Services, Inc. and Subsidiaries
Consolidating Balance Sheet Information
June 30, 2023
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
LIABILITIES AND NET ASSETS							
Current liabilities:							
Current portion of long-term debt	$ 26	$ -	$ 12,000	$ 482	$ -	$ -	$ 12,508
Accounts payable and accrued expenses	632	50	110,778	10,103	34,067	(6,867)	148,763
Advances from third-party payers	-	-	22,791	-	-	-	22,791
Medicare advance contract liability, current	-	-	-	-	-	-	-
Resident prepayment deposits	-	-	167	797	-	-	964
Provision for outstanding losses, current	-	-	6,889	308	-	(308)	6,889
Right of use lease liability, current	-	-	3,160	-	852	-	4,012
Construction retainage	-	-	505	-	-	-	505
Total current liabilities	658	50	156,290	11,690	34,919	(7,175)	196,432
Long-term debt, less current portion	12	-	339,903	19,759	-	-	359,674
Provision for outstanding losses, long-term	-	-	132,588	5,928	-	(5,927)	132,589
Post-retirement obligation	-	-	5,779	-	-	-	5,779
Interest rate swap liabilities	-	-	6,529	-	-	-	6,529
Operating lease liabilities	-	-	30,001	-	8,038	-	38,039
Other long-term liabilities	-	-	1,913	-	2,370	-	4,283
Total liabilities	670	50	673,003	37,377	45,327	(13,102)	743,325
Net assets:							
Without donor restrictions	45,453	885	556,232	65,100	8,507	(2,887)	673,290
With donor restrictions	-	51,383	44,367	7,152	1,488	(51,383)	53,007
Total net assets	45,453	52,268	600,599	72,252	9,995	(54,270)	726,297
Total liabilities and net assets	$ 46,123	$ 52,318	$ 1,273,602	$ 109,629	$ 55,322	$ (67,372)	$ 1,469,622

Mercy Health Services, Inc. and Subsidiaries
Consolidating Balance Sheet Information
June 30, 2022
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
ASSETS							
Current assets:							
Cash and cash equivalents	$ 832	$ 6,531	$ 258,128	$ 16,677	$ 1,150	$ -	$ 283,318
Short-term investments	-	-	-	1,656	-	-	1,656
Current portion of funds held by trustee	-	-	15,086	576	-	-	15,662
Resident prepayment deposits	-	-	-	571	-	-	571
Patient accounts receivable, net	-	-	47,755	6,712	22,672	-	77,139
Other amounts receivable, net	573	-	5,371	1,113	1,582	(895)	7,744
Current pledges receivable, net	-	2,541	-	-	-	-	2,541
Supplies inventory	-	-	13,496	335	2,674	-	16,505
Other current assets	-	-	2,942	(17)	806	-	3,731
Total current assets	1,405	9,072	342,778	27,623	28,884	(895)	408,867
Property and equipment, net	-	-	470,581	49,037	22,567		542,185
Investments and other assets:							
Funds held by trustee, less current portion	-	-	(6)	1,510	-	-	1,504
Board designated and donor restricted investments	24,681	23,052	206,031	21,584	-	-	275,348
Restricted investments	-	2,055	122,633	-	-	-	124,688
Interest in net assets of MHF	-	-	39,140	7,087	-	(46,227)	-
Long-term investments	-	20,588	-	-	-	-	20,588
Investments in and advances to affiliates	17,164	(7,658)	9,532	(7,425)	(4,023)	(3,000)	4,590
Reinsurance receivable	-	-	6,815	6,262	-	(6,262)	6,815
Right of use assets	-	-	34,214	-	9,262	-	43,476
Other assets	138	-	1,837	178	1,552	-	3,705
Total assets	$ 43,388	$ 47,109	$ 1,233,555	$ 105,856	$ 58,242	$ (56,384)	$ 1,431,766

Mercy Health Services, Inc. and Subsidiaries
Consolidating Balance Sheet Information
June 30, 2022
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
LIABILITIES AND NET ASSETS							
Current liabilities:							
Current maturities of long-term debt	$ 26	$ -	$ 11,585	$ 448	$ -	$ -	$ 12,059
Accounts payable and accrued expenses	819	-	120,871	8,748	30,760	(1,010)	160,188
Advances from third-party payers	-	-	31,850	-	11	-	31,861
Medicare advance contract liability, current	-	-	15,209	-	-	-	15,209
Provider relief funds liability	-	-	-	571	-		571
Provision for outstanding losses, current	-	-	8,529	405	-	(405)	8,529
Resident prepayment deposits	-	-	3,160	-	852	-	4,012
Construction retainage	-	-	506	-	-	-	506
Total current liabilities	845	-	191,710	10,172	31,623	(1,415)	232,935
Long-term debt, less current portion	12	-	351,593	20,220	-	-	371,825
Provision for outstanding losses, long-term	-	-	123,237	5,858	-	(5,857)	123,238
Post-retirement obligation	-	-	6,911	-	-	-	6,911
Interest rate swap liabilities	-	-	11,401	-	-	-	11,401
Operating lease liabilities	-	-	31,981	-	8,708	-	40,689
Other long-term liabilities	-	-	2,240	-	1,512	-	3,752
Total liabilities	857	-	719,073	36,250	41,843	(7,272)	790,751
Net assets:							
Without donor restrictions	42,531	882	475,321	62,519	14,895	(2,885)	593,263
With donor restrictions	-	46,227	39,161	7,087	1,504	(46,227)	47,752
Total net assets	42,531	47,109	514,482	69,606	16,399	(49,112)	641,015
Total liabilities and net assets	$ 43,388	$ 47,109	$ 1,233,555	$ 105,856	$ 58,242	$ (56,384)	$ 1,431,766

Mercy Health Services, Inc. and Subsidiaries
Consolidating Statement of Operations Information
Year Ended June 30, 2023
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
Revenues:							
Net patient service revenue	$ -	$ -	$ 561,312	$ 63,801	$ 261,618	$ -	$ 886,731
Other operating revenue	4,443	408	39,744	9,656	12,696	(19,879)	47,068
Net assets released from restrictions used for operations	-	-	1,423	1,155	898	-	3,476
Total revenues	4,443	408	602,479	74,612	275,212	(19,879)	937,275
Expenses:							
Salaries and benefits	4,173	1,791	271,741	49,763	190,956	(8,629)	509,795
Medical and surgical supplies	-	-	73,818	936	2,111	-	76,865
Pharmacy supplies	-	-	22,736	1,340	56,393	-	80,469
Other expendable supplies	-	77	31,753	5,721	1,686	-	39,237
Professional fees	-	8	10,240	4,913	8,965	(1,669)	22,457
Insurance	-	-	14,138	953	7,035	(32)	22,094
Other purchased services	236	193	75,049	5,548	(6,402)	(11,410)	63,214
Interest expense	-	-	12,477	778	-	-	13,255
Repairs	-	199	16,122	1,765	1,804	-	19,890
Depreciation and amortization	-	-	37,266	2,937	3,032	-	43,235
Total expenses	4,409	2,268	565,340	74,654	265,580	(21,740)	890,511
Operating income (loss)	34	(1,860)	37,139	(42)	9,632	1,861	46,764

Mercy Health Services, Inc. and Subsidiaries
Consolidating Statement of Operations Information
Year Ended June 30, 2023
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
Other income (losses):							
Investment income	$ 203	$ 440	$ 2,512	$ 270	$ -	$ (440)	$ 2,985
Net unrealized gain on investments	1,999	1,423	19,271	2,175	-	(1,423)	23,445
Unrealized gain on interest rate swap	-	-	4,872	-	-	-	4,872
Equity earnings in joint ventures	686	-	314	-	-	-	1,000
Other	-	-	(384)	-	-	-	(384)
Net other income (losses) income	2,888	1,863	26,585	2,445	-	(1,863)	31,918
Excess of revenues over expenses	2,922	3	63,724	2,403	9,632	(2)	78,682
Changes to pension and post retirement plan obligations	-	-	966	-	-	-	966
Transfer of net assets	-	-	16,020	-	(16,020)	-	-
Federal grant funding for the purchase of property and equipment	-	-	251	-	-	-	251
Net assets released from restrictions for the purchase of property and equipment	-	-	(50)	178	-	-	128
Increase (decrease) in net assets without donor restriction	$ 2,922	$ 3	$ 80,911	$ 2,581	$ (6,388)	$ (2)	$ 80,027

Mercy Health Services, Inc. and Subsidiaries
Consolidating Statement of Operations Information
Year Ended June 30, 2022
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
Revenues:							
Net patient service revenue	$ -	$ -	$ 549,960	$ 60,228	$ 244,903	$ -	$ 855,091
CARES Act provider relief funds	-	-	-	1,297	350	-	1,647
Other operating revenue	3,568	4,950	28,386	6,439	13,428	(22,992)	33,779
Net assets released from restrictions used for operations	-	-	3,408	1,299	465	-	5,172
Total revenues	3,568	4,950	581,754	69,263	259,146	(22,992)	895,689
Expenses:							
Salaries and benefits	3,460	1,794	256,939	46,537	180,293	(7,255)	481,768
Medical and surgical supplies	-	-	72,107	1,202	2,026	-	75,335
Pharmacy supplies	-	-	24,203	1,224	52,629	-	78,056
Other expendable supplies	-	52	31,653	5,475	1,419	-	38,599
Professional fees	-	-	11,005	4,006	8,834	(1,730)	22,115
Insurance	-	-	15,497	958	6,730	(21)	23,164
Other purchased services	108	170	62,912	5,176	4,799	(11,274)	61,891
Interest expense	-	-	12,435	761	-	-	13,196
Repairs	-	223	15,014	1,464	1,772	-	18,473
Depreciation and amortization	-	-	37,270	3,839	2,920	-	44,029
Total expenses	3,568	2,239	539,035	70,642	261,422	(20,280)	856,626
Operating income (loss)	-	2,711	42,719	(1,379)	(2,276)	(2,712)	39,063

Mercy Health Services, Inc. and Subsidiaries
Consolidating Statement of Operations Information
Year Ended June 30, 2022
(in thousands)

(Continued)

	Mercy Health Services, Inc.	Mercy Health Foundation, Inc.	Mercy Medical Center, Inc.	Stella Maris, Inc.	Physician Enterprise	Eliminations	Consolidated
Other income (losses):							
Investment income	$ 1,346	$ 850	$ 10,387	$ 1,411	$ -	$ (851)	$ 13,143
Net unrealized gain on investments	(5,163)	(3,563)	(61,098)	(5,558)	-	3,563	(71,819)
Unrealized loss on interest rate swap	-	-	11,664	-	-	-	11,664
Equity earnings in joint ventures	653	-	-	-	-	-	653
Loss on extinguishment of debt	-	-	380	-	-	-	380
Other	-	-	1,145	(162)	(35)	-	948
Net other (losses) income	(3,164)	(2,713)	(37,522)	(4,309)	(35)	2,712	(45,031)
(Deficiency) excess of revenues (under) over expens	(3,164)	(2)	5,197	(5,688)	(2,311)	-	(5,968)
Changes to pension and post retirement plan obligations	-	-	1,825	-	-	-	1,825
Transfer of net assets	-	-	(15,245)	-	15,245	-	-
Federal grant funding for the purchase of property and equipment	-	-	233	-	-	-	233
Net assets released from restrictions for the purchase of property and equipment	-	-	245	-	5	-	250
(Decrease) increase in net assets without donor restriction	$ (3,164)	$ (2)	$ (7,745)	$ (5,688)	$ 12,939	$ -	$ (3,660)