BAKER
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CMC Healthcare System, Inc.

Audited Consolidated Financial Statements and Other Financial Information

Year Ended September 30, 2018
With Independent Auditors' Report

Baker Newman & Noyes LLC
MAINE | MASSACHUSETTS | NEW HAMPSHIRE
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CMC HEALTHCARE SYSTEM, INC.

AUDITED CONSOLIDATED FINANCIAL STATEMENTS
AND OTHER FINANCIAL INFORMATION

Year Ended September 30, 2018

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
CMC Healthcare System, Inc.

We have audited the accompanying consolidated financial statements of CMC Healthcare System, Inc., which comprise the consolidated balance sheet as of September 30, 2018, and the related consolidated statements of operations, changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of CMC Healthcare System, Inc. as of September 30, 2018, and the results of its operations, changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Baker Newman & Noyes LLC

Manchester, New Hampshire
February 12, 2019

CMC HEALTHCARE SYSTEM, INC.

CONSOLIDATED BALANCE SHEET

September 30, 2018

ASSETS

Current assets:	
Cash and cash equivalents	$ 61,849,320
Short-term investments	29,009,260
Accounts receivable, less allowance for doubtful accounts of $21,892,905	55,326,986
Inventories	3,583,228
Other current assets	10,664,957
Total current assets	160,433,751
Property, plant and equipment, net	134,597,894
Other assets:	
Intangible assets and other	17,581,549
Assets whose use is limited:	
Pension and insurance obligations	17,859,458
Board designated and donor restricted investments and restricted grants	127,267,085
Held by trustee under revenue bond agreements	36,660,053
	181,786,596
Total assets	$494,399,790

LIABILITIES AND NET ASSETS

Current liabilities:	
Accounts payable and accrued expenses	$ 30,789,153
Accrued salaries, wages and related accounts	22,673,489
Amounts payable to third-party payors	14,643,104
Current portion of long-term debt	4,365,199
Total current liabilities	72,470,945
Accrued pension and other liabilities, less current portion	122,463,230
Long-term debt, less current portion	122,913,717
Total liabilities	317,847,892
Net assets:	
Unrestricted	166,125,080
Temporarily restricted	1,190,721
Permanently restricted	9,236,097
Total net assets	176,551,898
Total liabilities and net assets	$494,399,790

See accompanying notes.

CMC HEALTHCARE SYSTEM, INC.

CONSOLIDATED STATEMENT OF OPERATIONS

Year Ended September 30, 2018

Net patient service revenues, net of contractual allowances and discounts	$452,510,375
Provision for doubtful accounts	(20,334,249)
Net patient service revenues less provision for doubtful accounts	432,176,126
Other revenue	19,454,686
Disproportionate share funding	17,993,289
Total revenues	469,624,101
Expenses:	
Salaries, wages and fringe benefits	266,813,278
Supplies and other	160,290,214
New Hampshire Medicaid enhancement tax	19,968,497
Depreciation and amortization	16,136,984
Interest	4,368,765
Total expenses	467,577,738
Income from operations	2,046,363
Nonoperating gains (losses):	
Investment income	3,168,746
Net realized gains on sale of investments	2,918,048
Net periodic pension cost, other than service cost	(1,099,092)
Unrestricted contributions	629,198
Development costs	(635,408)
Other nonoperating loss	(489,294)
Total nonoperating gains, net	4,492,198
Excess of revenues and gains over expenses	6,538,561
Unrealized appreciation on investments	2,325,151
Change in fair value of interest rate swap agreement	302,826
Assets released from restriction used for capital	128,600
Pension-related changes other than net periodic pension cost	20,436,931
Increase in unrestricted net assets	29,732,069
Unrestricted net assets at beginning of year	136,393,011
Unrestricted net assets at end of year	$166,125,080

See accompanying notes.

CMC HEALTHCARE SYSTEM, INC.

CONSOLIDATED STATEMENT OF CHANGES IN NET ASSETS

Year Ended September 30, 2018

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total Net Assets
Balances at September 30, 2017	$136,393,011	$ 924,871	$8,801,136	$146,119,018
Excess of revenues and gains over expenses	6,538,561	–	–	6,538,561
Restricted investment income	–	5,421	21,952	27,373
Changes in interest in perpetual trust	–	–	341,439	341,439
Restricted contributions	–	616,466	30,458	646,924
Unrealized appreciation on investments	2,325,151	–	61,431	2,386,582
Change in fair value of interest rate swap agreement	302,826	–	–	302,826
Assets released from restriction used for operations	–	(227,437)	(20,319)	(247,756)
Assets released from restriction used for capital	128,600	(128,600)	–	–
Pension-related changes other than net periodic pension cost	20,436,931	–	–	20,436,931
	29,732,069	265,850	434,961	30,432,880
Balances at September 30, 2018	$166,125,080	$1,190,721	$9,236,097	$176,551,898

See accompanying notes.

CMC HEALTHCARE SYSTEM, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year Ended September 30, 2018

Operating activities:	
Increase in net assets	$ 30,432,880
Adjustments to reconcile increase in net assets to net cash provided by operating activities:	
Depreciation and amortization	16,136,984
Pension-related changes other than net periodic pension cost	(20,436,931)
Restricted gifts and investment income	(674,297)
Net realized gains on sales of investments	(2,918,048)
Increase in interest in perpetual trust	(341,439)
Unrealized appreciation on investments	(2,386,582)
Change in fair value of interest rate swap agreements	(487,593)
Bond discount/premium and issuance cost amortization	(313,993)
Change in operating assets and liabilities:	
Accounts receivable, net	(5,828,809)
Inventories	(176,498)
Other current assets	1,711,535
Other assets	(1,031,639)
Accounts payable and accrued expenses	(5,312,460)
Accrued salaries, wages and related accounts	2,561,918
Amounts payable to third-party payors	291,872
Accrued pension and other liabilities	6,039,303
Net cash provided by operating activities	17,266,203
Investing activities:	
Purchases of property, plant and equipment	(36,812,874)
Net change in assets held by trustee under revenue bond agreements	14,819,012
Proceeds from sales of investments	32,671,019
Purchases of investments	(40,605,899)
Net cash used by investing activities	(29,928,742)
Financing activities:	
Payments on long-term debt	(11,509,593)
Proceeds from issuance of long-term debt	8,130,000
Payments on capital leases	(707,299)
Bond issuance costs	(120,118)
Restricted gifts and investment income	674,297
Net cash used by financing activities	(3,532,713)
Decrease in cash and cash equivalents	(16,195,252)
Cash and cash equivalents at beginning of year	78,044,572
Cash and cash equivalents at end of year	$ 61,849,320

See accompanying notes.

1. Organization

CMC Healthcare System, Inc. (the System) is a not-for-profit organization formed effective July 1, 2001. The System functioned as the parent company and sole member of Catholic Medical Center (the Medical Center) (until December 31, 2016, as discussed below), Physician Practice Associates, Inc. (PPA), Alliance Enterprises, Inc. (Enterprises), Alliance Resources, Inc. (Resources), Alliance Ambulatory Services, Inc. (AAS), Alliance Health Services, Inc. (AHS), Doctors Medical Association, Inc. (DMA) and St. Peter's Home, Inc.

On December 30, 2016, the System became affiliated with Huggins Hospital (HH), a 25-bed critical access hospital in Wolfeboro, New Hampshire, and Monadnock Community Hospital (MCH), a 25-bed critical access hospital in Peterborough, New Hampshire, through the formation of a common parent, GraniteOne Health (GraniteOne). GraniteOne is a New Hampshire voluntary corporation that is recognized as being a Section 501(c)(3) tax-exempt and "supporting organization" within the meaning of Section 509(a)(3) of the Internal Revenue Code of 1986, as amended (the Code). GraniteOne serves as the sole member of HH and MCH and co-member of the Medical Center, along with the System. GraniteOne is governed by a thirteen member Board of Trustees appointed by each of the respective hospitals within the GraniteOne system. The GraniteOne Board of Trustees governs the GraniteOne system through the existence and execution of reserved powers to approve certain actions by the Boards of Trustees of each of the hospitals. Through GraniteOne, this more integrated healthcare system enhances the affiliated hospitals' ability to coordinate the delivery of patient care, implement best practices, eliminate inefficiencies and collaborate on regional planning. These efforts strengthen the hospitals' ability to meet the healthcare needs of their respective communities and provide for a more seamless patient experience across the continuum of care. The accompanying consolidated financial statements for the year ended September 30, 2018 do not include the accounts and activity of GraniteOne, HH and MCH.

On January 24, 2019, GraniteOne and Dartmouth-Hitchcock Health signed a non-binding letter of intent (LOI) to combine the two integrated healthcare delivery systems. This non-binding LOI is the first step in a potential lengthy process that may include due diligence, negotiation of a definitive agreement, review and approval of each member's Board of Trustees, including that of the System and the Roman Catholic Bishop of the Diocese of Manchester in terms of the Medical Center's participation, and federal and state regulatory approval processes. The combined organization will have a total operating revenue and assets of almost $3 billion. Expected benefits of the combination include expanding both organizations' primary and specialty services in southern New Hampshire, expanding access to health care in rural communities, and increasing competition by delivering higher-quality, lower cost care in New Hampshire.

2. Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared using the accrual basis of accounting.

2. Significant Accounting Policies (Continued)

Principles of Consolidation

The consolidated financial statements include the accounts of the Medical Center, PPA, Enterprises, Resources, AAS, AHS, DMA and St. Peter's Home, Inc. Significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The primary estimates relate to collectibility of receivables from patients and third-party payors, amounts payable to third-party payors, accrued compensation and benefits, conditional asset retirement obligations, and self-insurance reserves.

Income Taxes

The System and all related entities, with the exception of Enterprises and DMA, are not-for-profit corporations as described in Section 501(c)(3) of the Code and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. Management evaluated the System's tax positions and concluded the System has maintained its tax-exempt status, does not have any significant unrelated business income and had taken no uncertain tax positions that require adjustment to the consolidated financial statements.

Enterprises and DMA are for-profit organizations and, in accordance with federal and state tax laws, file income tax returns, as applicable. There was no provision for income taxes for the year ended September 30, 2018. There are no significant deferred tax assets or liabilities. These entities have concluded there are no significant uncertain tax positions requiring disclosure and there is no material liability for unrecognized tax benefits. It is the policy of these entities to recognize interest related to unrecognized tax benefits in interest expense and penalties in income tax expense.

Performance Indicator

Excess of revenues and gains over expenses is comprised of operating revenues and expenses and nonoperating gains and losses. For purposes of display, transactions deemed by management to be ongoing, major or central to the provision of health care services are reported as operating revenue and expenses. Peripheral or incidental transactions are reported as nonoperating gains or losses, which include contributions, development costs, realized gains and losses on the sales of securities, unrestricted investment income, other nonoperating losses, and contributions to community agencies.

Charity Care

The System has a formal charity care policy under which patient care is provided to patients who meet certain criteria without charge or at amounts less than its established rates. The System does not pursue collection of amounts determined to qualify as charity care; therefore, they are not reported as revenues.

2. Significant Accounting Policies (Continued)

Of the System's $467,577,738 total expenses reported for the year ended September 30, 2018, an estimated $7,500,000 arose from providing services to charity patients. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the System's total expenses divided by gross patient service revenue.

Concentration of Credit Risk

Financial instruments which subject the System to credit risk consist primarily of cash equivalents, accounts receivable and investments. The risk with respect to cash equivalents is minimized by the System's policy of investing in financial instruments with short-term maturities issued by highly rated financial institutions. The System's accounts receivable are primarily due from third-party payors and amounts are presented net of expected contractual allowances and uncollectible amounts. The System's investment portfolio consists of diversified investments, which are subject to market risk. Investments that exceeded 10% of investments include the SSGA S&P 500 Tobacco Free Fund and the Dreyfus Treasury Securities Cash Management Fund as of September 30, 2018.

Cash and Cash Equivalents

Cash and cash equivalents include certificates of deposit with maturities of three months or less when purchased and investments in overnight deposits at various banks. Cash and cash equivalents exclude amounts whose use is limited by board designation and amounts held by trustees under revenue bond and other agreements. The System maintains approximately $60,000,000 at September 30, 2018 of its cash and cash equivalent accounts with a single institution. The System has not experienced any losses associated with deposits at this institution.

Net Patient Service Revenues and Accounts Receivable

The System has agreements with third-party payors that provide for payments at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, per diem payments and fee schedules. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the year the related services are rendered and adjusted in future years as final settlements are determined. Changes in these estimates are reflected in the consolidated financial statements in the year in which they occur.

The System recognizes patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients, the System provides a discount approximately equal to that of its largest private insurance payors.

2. Significant Accounting Policies (Continued)

The provision for doubtful accounts is based upon management's assessment of historical and expected net collections considering historical business and economic conditions, trends in health care coverage, and other collection indicators. The System records a provision for doubtful accounts in the year services are provided related to self-pay patients, including both uninsured patients and patients with deductible and copayment balances due for which third-party coverage exists for a portion of their balance.

Periodically, management assesses the adequacy of the allowance for doubtful accounts based upon historical write-off experience. The results of this review are then used to make any modifications to the provision for doubtful accounts to establish an appropriate allowance for doubtful accounts. Accounts receivable are written off after collection efforts have been followed in accordance with internal policies.

Inventories

Inventories of supplies are stated at the lower of cost (determined by the first-in, first-out method) or net realizable value.

Related Party Activity

The Medical Center has engaged in various transactions with GraniteOne, HH and MCH. The Medical Center recognized approximately $3.4 million in revenue from these related parties for the year ended September 30, 2018, which is reflected within other revenues in the accompanying consolidated statement of operations. The Medical Center also incurred approximately $399,000 in expenses from transactions with these related parties for the year ended September 30, 2018, which is reflected within operating expenses in the accompanying consolidated statement of operations. As of September 30, 2018, the System has a net amount due from these related parties of approximately $507,000, which is reflected within other current assets in the accompanying consolidated balance sheet.

Property, Plant and Equipment

Property, plant and equipment is stated at cost at time of purchase or fair value at the time of donation, less accumulated depreciation. The System's policy is to capitalize expenditures for major improvements and charge maintenance and repairs currently for expenditures which do not extend the lives of the related assets. The provisions for depreciation and amortization have been determined using the straight-line method at rates intended to amortize the cost of assets over their estimated useful lives, which range from 2 to 40 years. Assets which have been purchased but not yet placed in service are included in construction in progress and no depreciation expense is recorded.

2. Significant Accounting Policies (Continued)

Conditional Asset Retirement Obligations

The System recognizes the fair value of a liability for legal obligations associated with asset retirements in the year in which the obligation is incurred, in accordance with the Accounting Standards for *Accounting for Asset Retirement Obligations* (ASC 410-20). When the liability is initially recorded, the cost of the asset retirement obligation is capitalized by increasing the carrying amount of the related long lived asset. The liability is accreted to its present value each year, and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the related asset. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the consolidated statement of operations.

As of September 30, 2018, $1,078,784 of conditional asset retirement obligations are included within accrued pension and other liabilities in the accompanying consolidated balance sheet.

Goodwill

The System reviews its goodwill and other long-lived assets annually to determine whether the carrying amount of such assets is impaired. Upon determination that an impairment has occurred, these assets are reduced to fair value. There were no impairments recorded for the year ended September 30, 2018. The net carrying value of goodwill is $4,490,154 at September 30, 2018 and is reflected within intangible assets and other in the accompanying consolidated balance sheet.

Retirement Benefits

The Catholic Medical Center Pension Plan (the Plan) provides retirement benefits for certain employees of the Medical Center and PPA who have attained age twenty-one and work at least 1,000 hours per year. The Plan consists of a benefit accrued to July 1, 1985, plus 2% of plan year earnings (to legislative maximums) per year. The System's funding policy is to contribute amounts to the Plan sufficient to meet minimum funding requirements set forth in the Employee Retirement Income Security Act of 1974, plus such additional amounts as may be determined to be appropriate from time to time. The Plan is intended to constitute a plan described in Section 414(k) of the Code, under which benefits derived from employer contributions are based on the separate account balances of participants in addition to the defined benefits under the Plan.

Effective January 1, 2008 the Medical Center decided to close participation in the Plan to new participants. As of January 1, 2008, current participants continued to participate in the Plan while new employees receive a higher matching contribution to the tax-sheltered annuity benefit program discussed below.

During 2011, the Board of Trustees voted to freeze the accrual of benefits under the Plan effective December 31, 2011.

The Plan was amended effective as of May 1, 2016 to provide a limited opportunity for certain terminated vested participants to elect an immediate lump sum or annuity distribution option.

2. Significant Accounting Policies (Continued)

The System also maintains tax-sheltered annuity benefit programs in which it matches one half of employee contributions up to 3% of their annual salary, depending on date of hire, plus an additional 3% - 5% based on tenure. The System made matching contributions under the program of $7,733,193 for the year ended September 30, 2018.

During 2007, the Medical Center created a nonqualified deferred compensation plan covering certain employees under Section 457(b) of the Code. Under the plan, a participant may elect to defer a portion of their compensation to be held until payment in the future to the participant or his or her beneficiary. Consistent with the requirements of the Code, all amounts of deferred compensation, including but not limited to any investments held and all income attributable to such amounts, property, and rights will remain subject to the claims of the Medical Center's creditors, without being restricted to the payment of deferred compensation, until payment is made to the participant or their beneficiary. No contributions were made by the System for the year ended September 30, 2018.

The System also provides a noncontributory supplemental executive retirement plan covering certain former executives of the Medical Center, as defined. The System's policy is to accrue costs under this plan using the "Projected Unit Credit Actuarial Cost Method" and to amortize past service costs over a fifteen year period. Benefits under this plan are based on the participant's final average salary, social security benefit, retirement income plan benefit, and total years of service. Certain investments have been designated for payment of benefits under this plan and are included in assets whose use is limited–pension and insurance obligations.

During 2007, the System created a supplemental executive retirement plan covering certain executives of the Medical Center under Section 457(f) of the Code. The System recorded compensation expense of $682,820 for the year ended September 30, 2018 related to this plan.

Employee Fringe Benefits

The System has an "earned time" plan. Under this plan, each qualifying employee "earns" hours of paid leave for each pay period worked. These hours of paid leave may be used for vacations, holidays, or illness. Hours earned but not used are vested with the employee and are paid to the employee upon termination. The System expenses the cost of these benefits as they are earned by the employees.

Debt Issuance Costs/Original Issue Discount or Premium

The debt issuance costs incurred to obtain financing for the System's construction and renovation programs and refinancing of prior bonds and the original issue discount or premium are amortized to interest expense using the effective interest method over the repayment period of the bonds. The original issue discount or premium and debt issuance costs are presented as a component of long-term debt.

Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted include assets held by trustees under indenture agreements, pension and insurance obligations, designated assets set aside by the Board of Trustees, over which the Board retains control and may, at its discretion, subsequently use for other purposes, and donor-restricted investments.

2. Significant Accounting Policies (Continued)

Classification of Net Assets

Gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of donated assets. Temporarily restricted net assets are those whose use by the System has been limited by donors to a specific time period or purpose. When a donor restriction expires (i.e., when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statement of operations as either net assets released from restrictions used for operations (for noncapital-related items and included in other revenue) or as net assets released from restrictions used for capital (for capital-related items).

Permanently restricted net assets have been restricted by donors to be maintained by the System in perpetuity. Income earned on permanently restricted net assets, to the extent not restricted by the donor, including net unrealized appreciation or depreciation on investments, is included in the consolidated statement of operations as unrestricted resources or as a change in temporarily restricted net assets in accordance with donor-intended purposes or applicable law.

Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

Investments and Investment Income

Investments are carried at fair value in the accompanying consolidated financial statements. See Note 7 for further discussion regarding fair value measurements. Realized gains or losses on the sale of investment securities are determined by the specific identification method and are recorded on the settlement date. Unrealized gains and losses on investments are excluded from the excess of revenues and gains over expenses unless the investments are classified as trading securities or losses are considered other-than-temporary. Interest and dividend income on unrestricted investments, unrestricted investment income on permanently restricted investments and unrestricted net realized gains/losses are reported as nonoperating gains/losses.

Derivative Instruments

Derivatives are recognized as either assets or liabilities in the consolidated balance sheet at fair value regardless of the purpose or intent for holding the instrument. Changes in the fair value of derivatives are recognized either in the excess of revenues and gains over expenses or net assets, depending on whether the derivative is speculative or being used to hedge changes in fair value or cash flows. See also Note 5.

Beneficial Interest in Perpetual Trust

The System is the beneficiary of trust funds administered by trustees or other third parties. Trusts wherein the System has the irrevocable right to receive the income earned on the trust assets in perpetuity are recorded as permanently restricted net assets at the fair value of the trust at the date of receipt. Income distributions from the trusts are reported as investment income that increase unrestricted net assets, unless restricted by the donor. Annual changes in the fair value of the trusts are recorded as increases or decreases to permanently restricted net assets.

2. Significant Accounting Policies (Continued)

Investment Policies

The System's investment policies provide guidance for the prudent and skillful management of invested assets with the objective of preserving capital and maximizing returns. The invested assets include endowment, specific purpose and board designated (unrestricted) funds.

Endowment funds are identified as permanent in nature, intended to provide support for current or future operations and other purposes identified by the donor. These funds are managed with disciplined longer-term investment objectives and strategies designed to accommodate relevant, reasonable, or probable events.

Temporarily restricted funds are temporary in nature, restricted as to time or purpose as identified by the donor or grantor. These funds have various intermediate/long-term time horizons associated with specific identified spending objectives.

Board designated funds have various intermediate/long-term time horizons associated with specific spending objectives as determined by the Board of Trustees.

Management of these assets is designed to maximize total return while preserving the capital values of the funds, protecting the funds from inflation and providing liquidity as needed. The objective is to provide a real rate of return that meets inflation, plus 4% to 5%, over a long-term time horizon.

The System targets a diversified asset allocation that places emphasis on achieving its long-term return objectives within prudent risk constraints.

Spending Policy for Appropriation of Assets for Expenditure

In accordance with the *Uniform Prudent Management of Institutional Funds Act* (UPMIFA), the System considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (a) the duration and preservation of the fund; (b) the purpose of the organization and the donor-restricted endowment fund; (c) general economic conditions; (d) the possible effect of inflation and deflation; (e) the expected total return from income and the appreciation of investments; (f) other resources of the organization; and (g) the investment policies of the organization.

Spending policies may be adopted by the System, from time to time, to provide a stream of funding for the support of key programs. The spending policies are structured in a manner to ensure that the purchasing power of the assets is maintained while providing the desired level of annual funding to the programs. The System currently has a policy allowing interest and dividend income earned on investments to be used for operations with the goal of keeping principal, including its appreciation, intact.

Federal Grant Revenue and Expenditures

Revenues and expenses under federal grant programs are recognized as the related expenditure is incurred.

2. Significant Accounting Policies (Continued)

Malpractice Loss Contingencies

The System has a claims-made basis policy for its malpractice insurance coverage. A claims-made basis policy provides specific coverage for claims reported during the policy term. The System has established a reserve to cover professional liability exposure, which may not be covered by insurance. The possibility exists, as a normal risk of doing business, that malpractice claims in excess of insurance coverage may be asserted against the System. In the event a loss contingency should occur, the System would give it appropriate recognition in its consolidated financial statements in conformity with accounting standards. The System expects to be able to obtain renewal or other coverage in future years.

In accordance with Accounting Standards Update (ASU) No. 2010-24, "*Health Care Entities*" (Topic 954): *Presentation of Insurance Claims and Related Insurance Recoveries*, at September 30, 2018, the System recorded a liability of $12,520,618 related to estimated professional liability losses covered under this policy. At September 30, 2018, the System also recorded a receivable of $8,829,118 related to estimated recoveries under insurance coverage for recoveries of the potential losses. These amounts are included in accrued pension and other liabilities, and intangible assets and other, respectively, on the consolidated balance sheet.

Workers' Compensation

The System maintains workers' compensation insurance under a self-insured plan. The plan offers, among other provisions, certain specific and aggregate stop-loss coverage to protect the System against excessive losses. The System has employed independent actuaries to estimate the ultimate costs, if any, of the settlement of such claims. Accrued workers' compensation losses of $3,061,261 at September 30, 2018 have been discounted at 1.25% and, in management's opinion, provide an adequate reserve for loss contingencies. At September 30, 2018, $1,359,646 and $1,701,615 is recorded within accounts payable and accrued expenses and accrued pension and other liabilities, respectively, in the accompanying consolidated balance sheet. The System has also recorded $248,403 and $408,513 within other current assets and intangible assets and other, respectively, in the accompanying consolidated balance sheet to limit the accrued losses to the retention amount at September 30, 2018.

Health Insurance

The System has a self-funded health insurance plan. The plan is administered by an insurance company which assists in determining the current funding requirements of participants under the terms of the plan and the liability for claims and assessments that would be payable at any given point in time. The System was insured above a stop-loss amount of $325,000 for the period October 1, 2017 through December 31, 2017 and $375,000 for the period January 1, 2018 through September 30, 2018 on individual claims. Estimated unpaid claims, and those claims incurred but not reported, at September 30, 2018 of $2,849,427 are reflected in the accompanying consolidated balance sheet within accounts payable and accrued expenses.

Advertising Costs

The System expenses advertising costs as incurred, and such costs totaled approximately $1,918,000 for the year ended September 30, 2018.

2. Significant Accounting Policies (Continued)

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), which requires revenue to be recognized when promised goods or services are transferred to customers in amounts that reflect the consideration to which the System expects to be entitled in exchange for those goods and services. ASU 2014-09 will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. ASU 2014-09 is effective for the System on October 1, 2019. ASU 2014-09 permits the use of either the retrospective or cumulative effect transition method. The System is evaluating the impact that ASU 2014-09 will have on its consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (ASU 2016-02). Under ASU 2016-02, at the commencement of a long-term lease, lessees will recognize a liability equivalent to the discounted payments due under the lease agreement, as well as an offsetting right-of-use asset. ASU 2016-02 is effective for the System on October 1, 2020, with early adoption permitted. Lessees (for capital and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees may not apply a full retrospective transition approach. The System is currently evaluating the impact of the pending adoption of ASU 2016-02 on the System's consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities (Topic 958)* (ASU 2016-14). Under ASU 2016-14, the existing three-category classification of net assets (i.e., unrestricted, temporarily restricted and permanently restricted) will be replaced with a simplified model that combines temporarily restricted and permanently restricted into a single category called "net assets with donor restrictions". ASU 2016-14 also enhances certain disclosures regarding board designations, donor restrictions and qualitative information regarding management of liquid resources. In addition to reporting expenses by functional classifications, ASU 2016-14 will also require the financial statements to provide information about expenses by their nature, along with enhanced disclosures about the methods used to allocate costs among program and support functions. ASU 2016-14 is effective for the System's fiscal year ending September 30, 2019, with early adoption permitted. The System is currently evaluating the impact of the pending adoption of ASU 2016-14 on the System's consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force)* (ASU 2016-18), which provides guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. ASU 2016-18 will be effective for the System's fiscal year ended September 30, 2020, and early adoption is permitted. ASU 2016-18 must be applied using a retrospective transition method. The System is currently evaluating the impact of the adoption of this guidance on its consolidated financial statements.

2. Significant Accounting Policies (Continued)

In March 2017, the FASB issued ASU No. 2017-07, *Compensation — Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost* (ASU 2017-07). ASU 2017-07 will require that an employer report the service cost component of net periodic pension cost in the same line item as other compensation costs arising from services rendered by employees during the year. The other components of net periodic pension cost are required to be presented in the income statement separately and outside a subtotal of income from operations, if one is presented. ASU 2017-07 is effective for the System on October 1, 2019, with early adoption permitted. The System adopted ASU 2017-07 during the year ended September 30, 2018.

In June 2018, the FASB issued ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made* (ASU 2018-08). Due to diversity in practice, ASU 2018-08 clarifies the definition of an exchange transaction as well as the criteria for evaluating whether contributions are unconditional or conditional. ASU 2018-08 is effective for the System on October 1, 2019, with early adoption permitted. The System is currently evaluating the impact that ASU 2018-08 will have on its consolidated financial statements.

Subsequent Events

Management of the System evaluated events occurring between the end of the System's fiscal year and February 12, 2019, the date the consolidated financial statements were available to be issued.

3. Net Patient Service Revenue

The following summarizes net patient service revenue for the year ended September 30, 2018:

Gross patient service revenue	$1,341,051,947
Less contractual allowances	(888,541,572)
Less provision for doubtful accounts	(20,334,249)
Net patient service revenue	$ 432,176,126

The System maintains contracts with the Social Security Administration ("Medicare") and the State of New Hampshire Department of Health and Human Services ("Medicaid"). The System is paid a prospectively determined fixed price for each Medicare and Medicaid inpatient acute care service depending on the type of illness or the patient's diagnosis related group classification. Capital costs and certain Medicare and Medicaid outpatient services are also reimbursed on a prospectively determined fixed price. The System receives payment for other Medicaid outpatient services on a reasonable cost basis which are settled with retroactive adjustments upon completion and audit of related cost finding reports.

Differences between amounts previously estimated and amounts subsequently determined to be recoverable or payable are included in net patient service revenues in the year that such amounts become known. The percentage of net patient service revenues earned from the Medicare and Medicaid programs was 39% and 5%, respectively, for the year ended September 30, 2018.

3. Net Patient Service Revenue (Continued)

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The System believes that it is in compliance with all applicable laws and regulations; compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs (Note 14).

The System also maintains contracts with certain commercial carriers, health maintenance organizations, preferred provider organizations and state and federal agencies. The basis for payment under these agreements includes prospectively determined rates per discharge and per day, discounts from established charges and fee screens. The System does not currently hold reimbursement contracts which contain financial risk components.

The approximate percentages of patient service revenues, net of contractual allowances and discounts and provision for doubtful accounts for the year ended September 30, 2018 from third-party payors and uninsured patients are as follows:

	Third-Party Payors	Uninsured Patients	Total All Payors
Net patient service revenue, net of contractual allowance and discounts	99.6%	0.4%	100.0%

An estimated breakdown of patient service revenues, net of contractual allowances, discounts and provision for doubtful accounts recognized for the year ended September 30, 2018 from major payor sources, is as follows:

	Gross Patient Service Revenues	Contractual Allowances and Discounts	Provision for Doubtful Accounts	Net Patient Service Revenues Less Provision for Doubtful Accounts
Private payors (includes coin-surance and deductibles)	$ 477,457,407	$(229,413,775)	$ (9,298,563)	$ 238,745,069
Medicaid	137,508,097	(113,364,379)	(651,292)	23,492,426
Medicare	695,141,198	(523,976,071)	(3,140,980)	168,024,147
Self-pay	30,945,245	(21,787,347)	(7,243,414)	1,914,484
	$1,341,051,947	$(888,541,572)	$(20,334,249)	$ 432,176,126

The System recognizes changes in accounting estimates for net patient service revenues and third-party payor settlements as new events occur or as additional information is obtained. For the year ended September 30, 2018, favorable adjustments recorded for changes to prior year estimates were approximately $1,000,000.

3. Net Patient Service Revenue (Continued)

Medicaid Enhancement Tax and Disproportionate Share Payment

Under the State of New Hampshire's (the State) tax code, the State imposes a Medicaid Enhancement Tax (MET) equal to 5.40% of the Medical Center's net patient service revenues in State fiscal year 2018 with certain exclusions. The amount of tax incurred by the Medical Center for the year ended September 30, 2018 was $19,968,497.

In the fall of 2010, in order to remain in compliance with stated federal regulations, the State of New Hampshire adopted a new approach related to Medicaid disproportionate share funding (DSH) retroactive to July 1, 2010. Unlike the former funding method, the State's approach led to a payment that was not directly based on, and did not equate to, the level of tax imposed. As a result, the legislation created some level of losses at certain New Hampshire hospitals, while other hospitals realized gains. DSH payments from the State are recorded in operating revenues and amounted to $17,993,289 for the year ended September 30, 2018, net of reserves referenced below.

The Centers for Medicare and Medicaid Services (CMS) has completed audits of the State's program and the disproportionate share payments made by the State from 2011 through 2014, the first years that those payments reflected the amount of uncompensated care provided by New Hampshire hospitals. It is possible that subsequent years will also be audited by CMS. The System has recorded reserves to address its exposure based on the audit results to date.

4. Property, Plant and Equipment

The major categories of property, plant and equipment are as follows at September 30, 2018:

	Useful Lives	
Land and land improvements	2-40 years	$ 3,630,354
Buildings and improvements	2-40 years	128,776,786
Fixed equipment	3-25 years	46,562,689
Movable equipment	3-25 years	138,314,958
Construction in progress		9,269,135
		326,553,922
Less accumulated depreciation and amortization		(191,956,028)
Net property, plant and equipment		$ 134,597,894

Depreciation expense amounted to $16,092,263 for the year ended September 30, 2018.

The cost of equipment under capital leases was $7,844,527 at September 30, 2018. Accumulated amortization of the leased equipment at September 30, 2018 was $7,059,231. Amortization of assets under capital leases is included in depreciation and amortization expense.

5. Long-Term Debt and Note Payable

Long-term debt consists of the following at September 30, 2018:

New Hampshire Health and Education Facilities Authority (the Authority) Revenue Bonds:	
Series 2012 Bonds with interest ranging from 4.00% to 5.00% per year and principal payable in annual installments ranging from $1,125,000 to $2,755,000 through July 2032	$ 22,450,000
Series 2015A Bonds with interest at a fixed rate of 2.27% per year and principal payable in annual installments ranging from $185,000 to $1,655,000 through July 2040	22,255,000
Series 2015B with variable interest subject to interest rate swap described below and principal payable in annual installments ranging from $195,000 to $665,000 through July 2036	8,260,000
Series 2017 Bonds with interest ranging from 3.38% to 5.00% per year and principal payable in annual installments ranging from $2,900,000 to $7,545,000 beginning in July 2033 through July 2044	61,115,000
	114,080,000
Note payable – see below	8,032,500
Capitalized lease obligations	1,020,278
Unamortized original issue premiums/discounts	5,450,325
Unamortized debt issuance costs	(1,304,187)
	127,278,916
Less current portion	(4,365,199)
	$122,913,717

In December 2012, the Medical Center, in connection with the Authority, issued $35,275,000 of tax-exempt fixed rate revenue bonds (Series 2012). Under the terms of the loan agreements, the Medical Center has granted the Authority a first collateralized interest in all gross receipts and a mortgage lien on existing and future property, plant and equipment. The Medical Center is required to maintain a minimum debt service coverage ratio of 1.20. The Medical Center was in compliance with this covenant as of September 30, 2018. The proceeds of the Series 2012 bond issue were used to advance refund the remaining 2002A Bonds, advance refund certain 2002B Bonds, pay off a short term CAN note and fund certain capital purchases.

On September 3, 2015, the Authority issued $32,720,000 of Revenue Bonds, Catholic Medical Center Issue, Series 2015, consisting of the $24,070,000 aggregate principal amount Series 2015A Bonds and the $8,650,000 aggregate principal amount Series 2015B Bonds sold via direct placement to a financial institution. Although the Series 2015B Bonds were issued, they were not drawn on until July 1, 2016, as discussed below. Under the terms of the loan agreements, the Medical Center has granted the Authority a first collateralized interest in all gross receipts and a mortgage lien on existing and future property, plant and equipment. The Medical Center is required to maintain a minimum debt service coverage ratio of 1.20. The Medical Center was in compliance with this covenant as of September 30, 2018.

5. Long-Term Debt and Note Payable (Continued)

The Series 2015A Bonds were issued to provide funds for the purpose of (i) advance refunding a portion of the outstanding 2006 Bonds in an amount of $20,655,000 to the first call date of July 1, 2016, (ii) funding certain construction projects and equipment purchases in an amount of approximately $3,824,000, and (iii) paying the costs of issuance related to the Series 2015 Bonds.

The Series 2015B Bonds were structured as drawdown bonds. On July 1, 2016, the full amount available under the Series 2015B Bonds totaling $8,650,000 was drawn upon and the proceeds in combination with cash contributed by the Medical Center totaling $555,000 were used to currently refund the remaining balance of the Series 2006 Bonds totaling $9,205,000.

On September 1, 2017, the Authority issued $61,115,000 of Revenue Bonds, Catholic Medical Center Issue, Series 2017. The Series 2017 Bonds were issued to fund various construction projects and equipment purchases, as well as pay certain costs of issuance related to the Series 2017 Bonds. Under the terms of the loan agreements, the Medical Center has granted the Authority a first collateralized interest in all gross receipts and a mortgage lien on existing and future property, plant and equipment. The Medical Center is required to maintain a minimum debt service coverage ratio of 1.20. The Medical Center was in compliance with this covenant as of September 30, 2018.

The Medical Center has an agreement with the Authority, which provides for the establishment of various funds, the use of which is generally restricted to the payment of debt, as well as a construction fund related to the Series 2017 Bonds. These funds are administered by a trustee, and income earned on certain of these funds is similarly restricted.

Interest paid by the System totaled $4,351,405 (including capitalized interest of $251,490) for the year ended September 30, 2018.

The aggregate principal payments due on the revenue bonds, capital lease obligations and other debt obligations for each of the five years ending September 30 and thereafter are as follows:

2019	$ 4,365,199
2020	4,158,079
2021	2,624,000
2022	2,704,000
2023	2,924,000
Thereafter	106,357,500
	$123,132,778

The fair value of the System's long-term debt is estimated using discounted cash flow analysis, based on the System's current incremental borrowing rate for similar types of borrowing arrangements. The fair value of the System's long-term debt, excluding capitalized lease obligations, was $122,000,000 at September 30, 2018.

5. Long-Term Debt and Note Payable (Continued)

MOB LLC Notes Payable

During 2007, MOB LLC (a subsidiary of Enterprises) established a nonrevolving line of credit for $9,350,000 with a bank in order to fund construction of a medical office building. The line of credit bore interest at the LIBOR lending rate plus 1%. Payments of interest only were due on a monthly basis until the completed construction of the medical office. During 2008, the building construction was completed and the line of credit was converted to a note payable with payments of interest (at the one-month LIBOR rate plus 1.4%) and principal due on a monthly basis, with all payments to be made no later than April 1, 2018.

On March 27, 2018, the MOB LLC note payable discussed above was refinanced to a term loan totaling $8,130,000. Interest is fixed at 3.71% and is payable monthly. Principal payments of $19,500 are due in monthly installments beginning May 1, 2018, and continuing until March 27, 2028, at which time the remaining unpaid principal and interest shall be due in full. Under the terms of the loan agreement, the Medical Center and MOB LLC (the Obligated Group) has granted the bank a first collateralized interest in all gross receipts and a mortgage lien on existing and future property, plant and equipment. The Medical Center and the System also guarantee the note payable. The Obligated Group is required to maintain a minimum debt service coverage ratio of 1.20. The Obligated Group was in compliance with this covenant as of September 30, 2018.

Derivatives

The System uses derivative financial instruments principally to manage interest rate risk. During 2007, MOB LLC entered into an interest rate swap agreement with an initial notional amount of $9,350,000 in connection with its line of credit. Under this agreement, MOB LLC pays a fixed rate equal to 5.21%, and receives a variable rate of the one-month LIBOR rate. The interest rate swap agreement terminated April 1, 2018. The change in fair value of this interest swap agreement totaled $184,767 during 2018, which amount has been included within nonoperating investment income within the consolidated statement of operations.

In January 2016, the Medical Center entered into an interest rate swap agreement with an initial notional amount of $8,650,000 in connection with its Series 2015B Bond issuance. The swap agreement hedges the Medical Center's interest exposure by effectively converting interest payments from variable rates to a fixed rate. The swap agreement is designated as a cash flow hedge of the underlying variable rate interest payments, and changes in the fair value of the swap agreement are reported as a change in unrestricted net assets. Under this agreement, the Medical Center pays a fixed rate equal to 1.482%, and receives a variable rate of 69.75% of the one-month LIBOR rate (2.11% at September 30, 2018). Payments under the swap agreement began August 1, 2016 and the agreement will terminate August 1, 2025.

The fair value of the Medical Center's interest rate swap agreement amounted to an asset of $262,725 as of September 30, 2018, which amount has been included within intangible assets and other in the accompanying consolidated balance sheet. The increase in the fair value of this derivative of $302,826 has been included within the consolidated statement of changes in net assets as a change in unrestricted net assets for the year ended September 30, 2018.

6. Operating Leases

The System has various noncancelable agreements to lease various pieces of medical equipment. The System also has noncancelable leases for office space and its physician practices. Rental expense under all leases for the year ended September 30, 2018 was $4,857,031.

Estimated future minimum lease payments under noncancelable operating leases are as follows:

2019	$ 3,114,865
2020	3,078,624
2021	3,047,441
2022	3,074,008
2023	3,050,839
Thereafter	8,597,980
	$23,963,757

7. Investments and Assets Whose Use is Limited

Investments and assets whose use is limited are comprised of the following at September 30, 2018:

	Fair Value	Cost
Cash and cash equivalents	$ 16,525,946	$ 16,525,946
U.S. federated treasury obligations	36,950,913	36,957,749
Marketable equity securities	44,031,227	39,959,906
Fixed income securities	57,757,424	58,911,509
Private investment funds	55,530,346	25,886,418
	$210,795,856	$178,241,528

Investment income and realized gains/losses and unrealized appreciation are summarized as follows for the year ended September 30, 2018:

Unrestricted:	
Nonoperating investment income	$3,168,746
Realized gains on sales of investments, net	2,918,048
Change in unrealized appreciation on investments	2,325,151
	$8,411,945
Restricted:	
Investment income	$ 27,373
Change in unrealized appreciation on investments	61,431
Changes in interest in perpetual trust	341,439
	$ 430,243

7. Investments and Assets Whose Use is Limited (Continued)

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. In determining fair value, the use of various valuation approaches, including market, income and cost approaches, is permitted.

A fair value hierarchy has been established based on whether the inputs to valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from sources independent of the reporting entity and unobservable inputs reflect the entity's own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used by the System for financial instruments measured at fair value on a recurring basis. The three levels of inputs are as follows:

Level 1 — Observable inputs such as quoted prices in active markets;

Level 2 — Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and

Level 3 — Unobservable inputs in which there is little or no market data.

Assets and liabilities measured at fair value are based on one or more of three valuation techniques. The three valuation techniques are as follows:

- *Market approach* – Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities;
- *Cost approach* – Amount that would be required to replace the service capacity of an asset (i.e., replacement cost); and
- *Income approach* – Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques).

In determining the appropriate levels, the System performs a detailed analysis of the assets and liabilities. There have been no changes in the methodologies used at September 30, 2018.

The following is a description of the valuation methodologies used:

7. Investments and Assets Whose Use is Limited (Continued)

U.S. Federated Treasury Obligations and Fixed Income Securities

The fair value is determined by using broker or dealer quotations, external pricing providers, or alternative pricing sources with reasonable levels of price transparency. The System holds fixed income mutual funds and exchange traded funds, governmental and federal agency debt instruments, municipal bonds, corporate bonds, and foreign bonds which are primarily classified as Level 1 within the fair value hierarchy.

Marketable Equity Securities

Marketable equity securities are valued based on stated market prices and at the net asset value of shares held by the System at year end, which generally results in classification as Level 1 within the fair value hierarchy.

Private Investment Funds

The System invests in private investment funds that consist primarily of limited partnership interests in investment funds, which, in turn, invest in diversified portfolios predominantly comprised of equity and fixed income securities, as well as options, futures contracts, and some other less liquid investments. Management has approved procedures pursuant to the methods in which the System values these investments, which ordinarily will be the amount equal to the pro-rata interest in the net assets of the limited partnership, as such value is supplied by, or on behalf of, each investment manager from time to time, usually monthly and/or quarterly.

System management is responsible for the fair value measurements of investments reported in the consolidated financial statements. Such amounts are generally determined using audited financial statements of the funds and/or recently settled transactions. Because of inherent uncertainty of valuation of certain private investment funds, the estimate of the fund manager or general partner may differ from actual values, and differences could be significant. Management believes that reported fair values of its private investment funds at the consolidated balance sheet dates are reasonable.

7. Investments and Assets Whose Use is Limited (Continued)

Fair Value on a Recurring Basis

The following table presents information about the System's assets and liabilities measured at fair value on a recurring basis based upon the lowest level of significant input to the valuations at September 30, 2018:

	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	$ 16,525,946	$ –	$ –	$ 16,525,946
U.S. federated treasury obligations	36,950,913	–	–	36,950,913
Marketable equity securities	44,031,227	–	–	44,031,227
Fixed income securities	57,757,424	–	–	57,757,424
Interest rate swap agreement	–	–	262,725	262,725
	$155,265,510	$ –	$ 262,725	155,528,235
Investments measured at net asset value:				
Private investment funds				55,530,346
Total assets at fair value				$211,058,581

The following table presents the assets (liabilities) carried at fair value as of September 30, 2018 that are classified within Level 3 of the fair value hierarchy. The table reflects gains and losses for the year ended September 30, 2018. Additionally, both observable and unobservable inputs may be used to determine the fair value of positions that the System has classified within the Level 3 category. As a result, the unrealized gains and losses for assets within Level 3 may include changes in fair value that were attributable to both observable and unobservable inputs.

	Fair Value Measurement Using Significant Unobservable Inputs (Level 3) Interest Rate Swap Agreements
Balance at September 30, 2017	$ (224,868)
Unrealized gains	487,593
Balance at September 30, 2018	$ 262,725

There were no significant transfers between Levels 1, 2 or 3 for the year ended September 30, 2018.

7. Investments and Assets Whose Use is Limited (Continued)

Net Asset Value Per Share

The following table discloses the fair value and redemption frequency of those assets whose fair value is estimated using the net asset value per share practical expedient at September 30, 2018:

Category	Fair Value	Unfunded Commitments	Redemption Frequency	Notice Period
Private investment funds	$52,108,790	$ –	Daily/monthly	2-30 day notice
Private investment funds	3,421,556	–	Quarterly	10-30 day notice*

* One fund allows redemptions quarterly, with certain restrictions.

Investment Strategies

U.S. Federated Treasury Obligations and Fixed Income Securities

The primary purpose of these investments is to provide a highly predictable and dependable source of income, preserve capital, reduce the volatility of the total portfolio, and hedge against the risk of deflation or protracted economic contraction.

Marketable Equity Securities

The primary purpose of equity investments is to provide appreciation of principal and growth of income with the recognition that this requires the assumption of greater market volatility and risk of loss. The total equity portion of the portfolio will be broadly diversified according to economic sector, industry, number of holdings and other characteristics, including style and capitalization. The System may employ multiple equity investment managers, each of whom may have distinct investment styles. Accordingly, while each manager's portfolio may not be fully diversified, it is expected that the combined equity portfolio will be broadly diversified.

Private Investment Funds

The primary purpose of private investment funds is to provide further portfolio diversification and to reduce overall portfolio volatility by investing in strategies that are less correlated with traditional equity and fixed income investments. Private investment funds may provide access to strategies otherwise not accessible through traditional equities and fixed income such as derivative instruments, real estate, distressed debt and private equity and debt.

7. Investments and Assets Whose Use is Limited (Continued)

Fair Value of Other Financial Instruments

Other financial instruments consist of accounts receivable, accounts payable and accrued expenses, amounts payable to third-party payors and long-term debt. The fair value of all financial instruments other than long-term debt approximates their relative book values as these financial instruments have short-term maturities or are recorded at amounts that approximate fair value. See Note 5 for disclosure of the fair value of long-term debt.

8. Retirement Benefits

A reconciliation of the changes in the Catholic Medical Center Pension Plan, the Medical Center's Supplemental Executive Retirement Plan and the New Hampshire Medical Laboratories Retirement Income Plan projected benefit obligations and the fair value of assets for the year ended September 30, 2018, and a statement of funded status of the plans as of September 30, 2018 is as follows:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Changes in benefit obligations:			
Projected benefit obligations at beginning of year	$ (284,200,778)	$ (4,567,286)	$ (3,062,398)
Service cost	(1,500,000)	–	(25,000)
Interest cost	(10,628,197)	(140,414)	(104,714)
Benefits paid	7,117,759	411,692	171,828
Actuarial gain	17,666,264	155,253	173,565
Expenses paid	1,430,445	–	16,756
Projected benefit obligations at end of year	(270,114,507)	(4,140,755)	(2,829,963)
Changes in plan assets:			
Fair value of plan assets at beginning of year	181,485,201	–	2,144,861
Actual return on plan assets	12,074,468	–	141,614
Employer contributions	403,125	411,692	42,936
Benefits paid	(7,117,759)	(411,692)	(171,828)
Expenses paid	(1,430,445)	–	(16,756)
Fair value of plan assets at end of year	185,414,590	–	2,140,827
Funded status of plan at September 30, 2018	$ (84,699,917)	$ (4,140,755)	$ (689,136)

8. Retirement Benefits (Continued)

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Amounts recognized in the consolidated balance sheet consist of:			
Current liability	$ –	$ (398,750)	$ –
Noncurrent liability	(84,699,917)	(3,742,005)	(689,136)
Net amount recognized	$ (84,699,917)	$ (4,140,755)	$ (689,136)

The net loss for the defined benefit pension plans that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year is $2,900,988.

The current portion of accrued pension costs included in the above amounts for the System amounted to $398,750 at September 30, 2018 and has been included in accounts payable and accrued expenses.

The amounts recognized in unrestricted net assets consist of the following at September 30, 2018:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Amounts recognized in the consolidated balance sheet – total plan:			
Unrestricted net assets:			
Net loss	$(105,860,712)	$ (2,102,034)	$ (1,492,143)
Net amount recognized	$(105,860,712)	$ (2,102,034)	$ (1,492,143)

Net periodic pension cost includes the following components at September 30, 2018:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Service cost	$ 1,500,000	$ –	$ 25,000
Interest cost	10,628,197	140,414	104,714
Expected return on plan assets	(13,110,637)	–	(153,960)
Amortization of actuarial loss	3,275,000	147,466	67,898
Net periodic pension cost	$ 2,292,560	$ 287,880	$ 43,652

8. Retirement Benefits (Continued)

Other changes in plan assets and benefit obligations recognized in unrestricted net assets consist of the following at September 30, 2018:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Net gain	$ (16,630,095)	$ (155,253)	$ (161,219)
Amortization of actuarial loss	(3,275,000)	(147,466)	(67,898)
Net amount recognized	$ (19,905,095)	$ (302,719)	$ (229,117)

The investments of the plans are comprised of the following at September 30, 2018:

	Target Allocation	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Marketable equity securities	70.0%	66.2%	0.0%	66.2%
Fixed income securities	20.0	23.7	0.0	23.7
Other	10.0	10.1	0.0	10.1
	100.0%	100.0%	0.0%	100.0%

The assumption for the long-term rate of return on plan assets has been determined by reflecting expectations regarding future rates of return for the investment portfolio, with consideration given to the distribution of investments by asset class and historical rates of return for each individual asset class.

The weighted-average assumptions used to determine the defined benefit pension plan obligations at September 30, 2018 are as follows:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Discount rate	4.23%	3.93%	4.10%
Rate of compensation increase	N/A	N/A	N/A

8. Retirement Benefits (Continued)

The weighted-average assumptions used to determine the defined benefit pension plan net periodic benefit costs are as follows at September 30, 2018:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
Discount rate	3.79%	3.22%	3.52%
Rate of compensation increase	N/A	N/A	N/A
Expected long-term return on plan assets	7.30%	N/A	7.30%

The System expects to make employer contributions totaling $5,000,000 to the Catholic Medical Center Pension Plan for the fiscal year ending September 30, 2019. Expected contributions to the Pre-1987 Supplemental Executive Retirement Plan and New Hampshire Medical Laboratories Retirement Income Plan for the fiscal year ending September 30, 2019 are not expected to be significant.

The benefits, which reflect expected future service, as appropriate, expected to be paid for the years ending September 30 are as follows:

	Catholic Medical Center Pension Plan	Pre-1987 Supplemental Executive Retirement Plan	New Hampshire Medical Laboratories Retirement Income Plan
2019	$ 8,409,949	$ 406,510	$181,739
2020	9,225,819	394,940	191,472
2021	9,970,846	382,785	197,799
2022	10,796,864	370,020	197,567
2023	11,627,944	356,615	197,824
2024 - 2028	69,395,428	1,557,963	951,232

The System contributed $403,125, $411,692 and $42,936 to the Catholic Medical Center Pension Plan, Pre-1987 Supplemental Executive Retirement Plan and the New Hampshire Medical Laboratories Retirement Income Plan, respectively, for the year ended September 30, 2018. The System plans to make any necessary contributions during the upcoming fiscal 2019 year to ensure the plans continue to be adequately funded given the current market conditions.

8. Retirement Benefits (Continued)

The following fair value hierarchy table presents information about the financial assets of the above plans measured at fair value on a recurring basis based upon the lowest level of significant input valuation as of September 30, 2018:

	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 2,160,634	$ –	$ –	$ 2,160,634
Marketable equity securities	39,221,636	–	–	39,221,636
Fixed income securities	44,497,162	–	–	44,497,162
	$85,879,432	$ –	$ –	85,879,432
Investments measured at net asset value:				
Private investment funds				101,675,985
Total assets at fair value				$187,555,417

9. Community Benefits

The System rendered charity care in accordance with its formal charity care policy, which, at established charges, amounted to $21,671,846 for the year ended September 30, 2018. Also, the System provides community service programs, without charge, such as the Medication Assistance Program, Community Education and Wellness, Patient Transport, and the Parish Nurse Program. The costs of providing these programs amounted to $983,861 for the year ended September 30, 2018.

10. Functional Expenses

The System provides general health care services to residents within its geographic location including inpatient, outpatient and emergency care. Expenses related to providing these services are as follows at September 30, 2018:

Health care services	$367,226,914
General and administrative	100,350,824
	$467,577,738

11. Concentration of Credit Risk

The System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors is as follows at September 30, 2018:

Medicare	44%
Medicaid	12
Commercial insurance and other	23
Patients (self pay)	8
Anthem Blue Cross	13
	100%

12. Endowments

In July 2008, the State of New Hampshire enacted a version of UPMIFA (the Act). The new law, which had an effective date of July 1, 2008, eliminates the historical dollar threshold and establishes prudent spending guidelines that consider both the duration and preservation of the fund. As a result of this enactment, subject to the donor's intent as expressed in a gift agreement or similar document, a New Hampshire charitable organization may now spend the principal and income of an endowment fund, even from an underwater fund, after considering the factors listed in the Act.

At September 30, 2018, the endowment net asset composition by type of fund consisted of the following:

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total
Donor-restricted funds	$ –	$1,190,721	$9,236,097	$ 10,426,818
Board-designated funds	107,832,023	–	–	107,832,023
Total funds	$107,832,023	$1,190,721	$9,236,097	$118,258,841

12. Endowments (Continued)

Changes in endowment net assets consisted of the following for the year ended September 30, 2018:

	Unrestricted Net Assets	Temporarily Restricted Net Assets	Permanently Restricted Net Assets	Total
Balance at September 30, 2017	$102,045,292	$ 924,871	$8,801,136	$111,771,299
Investment return:				
Investment income	1,645,491	5,421	21,952	1,672,864
Net appreciation (realized and unrealized)	4,012,640	–	402,870	4,415,510
Total investment gain	5,658,131	5,421	424,822	6,088,374
Contributions	–	616,466	30,458	646,924
Appropriation for operations	–	(227,437)	(20,319)	(247,756)
Appropriation for capital	128,600	(128,600)	–	–
Balance at September 30, 2018	$107,832,023	$1,190,721	$9,236,097	$118,258,841

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the System to retain as a fund of perpetual duration. There were no such deficiencies as of September 30, 2018.

13. Investments in Joint Ventures

AAS has a 44% ownership interest in the Bedford Ambulatory Surgical Center. AAS accounts for its investment in this joint venture under the equity method.

AAS has a 50% ownership interest in the Alliance Urgent Care Services, LLC. AAS accounts for its investment in this joint venture under the equity method.

The Medical Center, along with four other participating hospitals and Tufts Health Plan, formed Tufts Health Freedom Plan (THFP), a joint venture. THFP is a health insurance company which began operations as of January 1, 2016. The Medical Center has an approximate 12% ownership interest in this joint venture.

Selected financial information relating to the above entities for the year ended September 30, 2018 is not shown as such amounts are not significant to the consolidated financial statements.

14. Commitments and Contingencies

Litigation

Various legal claims, generally incidental to the conduct of normal business, are pending or have been threatened against the System. The System intends to defend vigorously against these claims. While ultimate liability, if any, arising from any such claim is presently indeterminable, it is management's opinion that the ultimate resolution of these claims will not have a material adverse effect on the financial condition of the System.

Regulatory

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. Government activity continues with respect to investigations and allegations concerning possible violations by health care providers of fraud and abuse statutes and regulations, which could result in the imposition of significant fines and penalties as well as significant repayments for patient services previously billed. Compliance with such laws and regulations are subject to government review and interpretations as well as regulatory actions unknown or unasserted at this time.

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INDEPENDENT AUDITORS' REPORT
ON OTHER FINANCIAL INFORMATION

Board of Trustees
CMC Healthcare System, Inc.

We have audited the consolidated financial statements of CMC Healthcare System, Inc. (the System) as of and for the year ended September 30, 2018, and have issued our report thereon, which contains an unmodified opinion on those consolidated financial statements. See page 1. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information is presented for purposes of additional analysis rather than to present the financial position, results of operations and cash flows of the individual entities 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, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Baker Newman & Noyes LLC

Manchester, New Hampshire
February 12, 2019

CMC HEALTHCARE SYSTEM, INC.

CONSOLIDATING BALANCE SHEET

September 30, 2018

ASSETS

	Catholic Medical Center	Physician Practice Associates	Alliance Enterprises	Alliance Resources	Alliance Ambu-latory Services	Alliance Health Services	Doctors Medical Association	Saint Peter's Home	Elimi-nations	Consolidated
Current assets:										
Cash and cash equivalents	$ 57,668,500	$ 22,273	$ 2,745,448	$ 332,128	$ 376,706	$ 166,645	$ 76,949	$ 460,671	$ –	$ 61,849,320
Short-term investments	29,009,260	–	–	–	–	–	–	–	–	29,009,260
Accounts receivable, net	54,074,988	–	–	–	–	1,251,998	–	–	–	55,326,986
Inventories	3,583,228	–	–	–	–	–	–	–	–	3,583,228
Other current assets	9,150,610	3,750	2,537	57,365	286,666	1,139,687	1,608	22,734	–	10,664,957
Total current assets	153,486,586	26,023	2,747,985	389,493	663,372	2,558,330	78,557	483,405	–	160,433,751
Property, plant and equipment, net	109,898,233	–	8,858,160	14,585,192	–	111,130	–	1,145,179	–	134,597,894
Other assets:										
Intangible assets and other	10,875,302	–	–	–	6,706,247	–	–	–	–	17,581,549
Assets whose use is limited:										
Pension and insurance obligations	17,859,458	–	–	–	–	–	–	–	–	17,859,458
Board designated and donor restricted investments and restricted grants	119,411,378	1,488	–	–	–	–	–	7,854,219	–	127,267,085
Held by trustee under revenue bond agreements	36,660,053	–	–	–	–	–	–	–	–	36,660,053
	173,930,889	1,488	–	–	–	–	–	7,854,219	–	181,786,596
Total assets	$448,191,010	$ 27,511	$11,606,145	$14,974,685	$7,369,619	$2,669,460	$ 78,557	$9,482,803	$ –	$494,399,790

LIABILITIES AND NET ASSETS

	Catholic Medical Center	Physician Practice Associates	Alliance Enterprises	Alliance Resources	Alliance Ambu-latory Services	Alliance Health Services	Doctors Medical Association	Saint Peter's Home	Elimi-nations	Consolidated
Current liabilities:										
Accounts payable and accrued expenses	$ 28,743,870	$ 68,143	$ 90,029	$ 17,169	$ –	$1,660,520	$ 5,590	$ 203,832	$ –	$ 30,789,153
Accrued salaries, wages and related accounts	18,755,583	3,791,797	–	–	–	–	–	126,109	–	22,673,489
Amounts payable to third-party payors	14,643,104	–	–	–	–	–	–	–	–	14,643,104
Due to (from) affiliates	1,477,267	(1,392,988)	16,867	(80,123)	–	2,986	(23,609)	(400)	–	–
Current portion of long-term debt	4,131,199	–	234,000	–	–	–	–	–	–	4,365,199
Total current liabilities	67,751,023	2,466,952	340,896	(62,954)	–	1,663,506	(18,019)	329,541	–	72,470,945
Accrued pension and other liabilities, less current portion	115,111,279	6,183,094	706,541	71,465	–	390,851	–	–	–	122,463,230
Long-term debt, less current portion	115,229,329	–	7,684,388	–	–	–	–	–	–	122,913,717
Total liabilities	298,091,631	8,650,046	8,731,825	8,511	–	2,054,357	(18,019)	329,541	–	317,847,892
Net assets (deficit):										
Unrestricted	139,672,561	(8,622,535)	2,874,320	14,966,174	7,369,619	615,103	96,576	9,153,262	–	166,125,080
Temporarily restricted	1,190,721	–	–	–	–	–	–	–	–	1,190,721
Permanently restricted	9,236,097	–	–	–	–	–	–	–	–	9,236,097
Total net assets (deficit)	150,099,379	(8,622,535)	2,874,320	14,966,174	7,369,619	615,103	96,576	9,153,262	–	176,551,898
Total liabilities and net assets	$448,191,010	$ 27,511	$11,606,145	$14,974,685	$7,369,619	$2,669,460	$ 78,557	$9,482,803	$ –	$494,399,790

CMC HEALTHCARE SYSTEM, INC.

CONSOLIDATING STATEMENT OF OPERATIONS

Year Ended September 30, 2018

	Catholic Medical Center	Physician Practice Associates	Alliance Enterprises	Alliance Resources	Alliance Ambu-latory Services	Alliance Health Services	Doctors Medical Association	Saint Peter's Home	Eliminations	Consolidated
Net patient service revenues, net of contractual allowances and discounts	$436,357,697	$ –	$ –	$ –	$ –	$16,152,678	$ –	$ –	$ –	$452,510,375
Provision for doubtful accounts	(19,593,714)	–	–	–	–	(740,535)	–	–	–	(20,334,249)
Net patient service revenues less provision for doubtful accounts	416,763,983	–	–	–	–	15,412,143	–	–	–	432,176,126
Other revenue	12,515,169	24,664,782	2,026,051	1,306,175	2,685,142	572,119	131,102	3,090,287	(27,536,141)	19,454,686
Disproportionate share funding	17,993,289	–	–	–	–	–	–	–	–	17,993,289
Total revenues	447,272,441	24,664,782	2,026,051	1,306,175	2,685,142	15,984,262	131,102	3,090,287	(27,536,141)	469,624,101
Expenses:										
Salaries, wages and fringe benefits	217,868,046	55,518,048	25,000	–	–	14,377,316	–	3,020,016	(23,995,148)	266,813,278
Supplies and other	153,527,155	2,191,509	752,790	1,016,430	–	5,867,844	142,023	333,456	(3,540,993)	160,290,214
New Hampshire Medicaid enhancement tax	19,968,497	–	–	–	–	–	–	–	–	19,968,497
Depreciation and amortization	14,972,724	–	333,910	594,149	–	41,518	–	194,683	–	16,136,984
Interest	3,933,617	–	435,148	–	–	–	–	–	–	4,368,765
Total expenses	410,270,039	57,709,557	1,546,848	1,610,579	–	20,286,678	142,023	3,548,155	(27,536,141)	467,577,738
Income (loss) from operations	37,002,402	(33,044,775)	479,203	(304,404)	2,685,142	(4,302,416)	(10,921)	(457,868)	–	2,046,363
Nonoperating gains (losses):										
Investment income	2,846,375	–	158,797	6	3,429	–	–	160,139	–	3,168,746
Net realized gains on sale of investments	2,853,325	–	–	–	–	–	–	64,723	–	2,918,048
Net periodic pension cost, other than service cost	(1,023,371)	(57,068)	(18,653)	–	–	–	–	–	–	(1,099,092)
Unrestricted contributions	629,198	–	–	–	–	–	–	–	–	629,198
Development costs	(635,408)	–	–	–	–	–	–	–	–	(635,408)
Other nonoperating (loss) gain	(511,679)	–	8,285	–	–	–	–	14,100	–	(489,294)
Total nonoperating gains, net	4,158,440	(57,068)	148,429	6	3,429	–	–	238,962	–	4,492,198
Excess (deficiency) of revenues over expenses	41,160,842	(33,101,843)	627,632	(304,398)	2,688,571	(4,302,416)	(10,921)	(218,906)	–	6,538,561
Unrealized appreciation on investments	2,184,604	–	–	–	–	–	–	140,547	–	2,325,151
Change in fair value of interest rate swap agreement	302,826	–	–	–	–	–	–	–	–	302,826
Assets released from restriction used for capital	128,600	–	–	–	–	–	–	–	–	128,600
Pension-related changes other than net periodic pension cost	18,843,760	1,364,053	229,118	–	–	–	–	–	–	20,436,931
Net transfers (to) from affiliates	(35,782,824)	31,967,000	223,054	1,112,760	(1,650,000)	4,130,000	–	10	–	–
Increase (decrease) in unrestricted net assets	$ 26,837,808	$ 229,210	$1,079,804	$ 808,362	$ 1,038,571	$ (172,416)	$(10,921)	$ (78,349)	$ –	$ 29,732,069