BAKER
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NOYES

The Monadnock Community Hospital

Audited Financial Statements

Years Ended September 30, 2018 and 2017
With Independent Auditors' Report

THE MONADNOCK COMMUNITY HOSPITAL

Audited Financial Statements

Years Ended September 30, 2018 and 2017

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
The Monadnock Community Hospital

We have audited the accompanying financial statements of The Monadnock Community Hospital (the Hospital), which comprise the balance sheets as of September 30, 2018 and 2017, and the related statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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 financial statements based on our audits. We conducted our audits 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 financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Hospital as of September 30, 2018 and 2017, and the results of its operations, changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Baker Newman & Noyes LLC

Manchester, New Hampshire
January 10, 2019

THE MONADNOCK COMMUNITY HOSPITAL

BALANCE SHEETS

September 30, 2018 and 2017

ASSETS

	2018	2017
Current assets:		
Cash and cash equivalents	$ 12,271,683	$ 18,432,646
Accounts receivable, net (notes 2 and 4)	9,473,219	8,766,705
Current portion of notes receivable	164,377	170,486
Other receivables (note 10)	444,154	472,058
Current portion of pledges receivable, net (note 5)	95,923	232,033
Inventories	1,410,000	1,414,052
Prepaid expenses	1,103,571	953,606
Total current assets	24,962,927	30,441,586
Assets limited as to use (notes 4, 6, 9 and 16)	67,523,029	54,466,797
Medical office building and related assets, net of accumulated depreciation of $2,075,186 in 2018 and $1,980,189 in 2017	1,344,438	1,439,435
Property and equipment, net (notes 7 and 8)	35,905,953	35,474,846
Notes receivable, less current portion	37,215	135,491
Other:		
Pledges receivable, less current portion, net (note 5)	199,735	204,424
Other assets	197,968	193,509
	397,703	397,933
Total assets	$130,171,265	$122,356,088

LIABILITIES AND NET ASSETS

	2018	2017
Current liabilities:		
Accounts payable and accrued expenses	$ 6,631,553	$ 6,510,158
Accrued payroll and amounts withheld	2,197,969	2,096,692
Estimated third-party payor settlements (note 3)	17,828,486	17,765,166
Current portion of long-term debt and capital lease obligations	717,483	737,298
Total current liabilities	27,375,491	27,109,314
Long-term debt and capital lease obligations, less current portion (note 8)	23,704,690	24,518,615
Interest rate swap agreements (notes 8 and 16)	1,177,576	1,994,001
Total liabilities	52,257,757	53,621,930
Commitments and contingencies (note 12)		
Net assets:		
Unrestricted net assets	64,496,464	56,457,118
Temporarily restricted net assets (note 9)	4,377,657	3,557,821
Permanently restricted net assets (note 9)	9,039,387	8,719,219
Total net assets	77,913,508	68,734,158
Total liabilities and net assets	$130,171,265	$122,356,088

See accompanying notes.

THE MONADNOCK COMMUNITY HOSPITAL

STATEMENTS OF OPERATIONS

Years Ended September 30, 2018 and 2017

	2018	2017
Unrestricted revenue and other support:		
Net patient service revenue, net of contractual allowances and discounts, before disproportionate share funding (notes 3 and 10)	$82,827,389	$ 78,002,504
Disproportionate share funding (notes 3 and 10)	4,100,348	2,100,000
Net patient service revenue, before provision for bad debts	86,927,737	80,102,504
Provision for bad debts (note 10)	(4,966,097)	(4,605,771)
Net patient service revenue, less provision for bad debts	81,961,640	75,496,733
Other revenue (note 10)	6,024,480	6,663,983
Net assets released from restrictions for operations (note 9)	349,362	360,566
Total unrestricted revenue and other support	88,335,482	82,521,282
Expenses (note 14):		
Salaries and benefits (note 11)	44,398,572	41,555,571
Supplies and other (note 12)	34,011,294	30,781,354
Insurance (note 12)	515,518	526,147
Depreciation and amortization (note 7)	4,388,428	4,432,088
Interest (note 8)	1,078,378	1,108,499
New Hampshire Medicaid enhancement tax (note 3)	3,613,664	3,367,222
Total expenses	88,005,854	81,770,881
Income from operations	329,628	750,401
Nonoperating gains (losses):		
Investment income (note 6)	6,797,853	1,124,281
Unrestricted contributions, net of fundraising expenses (note 14)	68,228	(35,100)
Other expense	(285,346)	(211,666)
Grant income	–	45,000
Nonoperating gains, net	6,580,735	922,515
Excess of revenue, support and nonoperating gains over expenses	6,910,363	1,672,916
Net unrealized (losses) gains on investments (note 6)	(103,293)	3,445,760
Increase in fair value of interest rate swap agreements, qualifying as hedges (notes 8 and 16)	816,425	1,184,662
Net assets released from restrictions used to purchase property and equipment	415,851	382,067
Increase in unrestricted net assets	$ 8,039,346	$ 6,685,405

See accompanying notes.

THE MONADNOCK COMMUNITY HOSPITAL

STATEMENTS OF CHANGES IN NET ASSETS

Years Ended September 30, 2018 and 2017

	2018	2017
Unrestricted net assets:		
Excess of revenue, support and nonoperating gains over expenses	$ 6,910,363	$ 1,672,916
Net unrealized (losses) gains on investments (note 6)	(103,293)	3,445,760
Increase in fair value of interest rate swap agreements, qualifying as hedges (notes 8 and 16)	816,425	1,184,662
Net assets released from restrictions used to purchase property and equipment	415,851	382,067
Increase in unrestricted net assets	8,039,346	6,685,405
Temporarily restricted net assets:		
Contributions (note 5)	493,404	205,969
Net investment income (note 6)	66,016	43,414
Net realized gains on investments (note 6)	1,030,446	113,611
Net unrealized (losses) gains on investments (note 6)	(4,817)	596,929
Net assets released from restrictions for operations (note 9)	(349,362)	(360,566)
Net assets released from restrictions used to purchase property and equipment	(415,851)	(382,067)
Increase in temporarily restricted net assets	819,836	217,290
Permanently restricted net assets:		
Net change in perpetual trusts (note 6)	320,168	319,803
Increase in permanently restricted net assets	320,168	319,803
Increase in net assets	9,179,350	7,222,498
Net assets, beginning of year	68,734,158	61,511,660
Net assets, end of year	$77,913,508	$68,734,158

See accompanying notes.

THE MONADNOCK COMMUNITY HOSPITAL

STATEMENTS OF CASH FLOWS

Years Ended September 30, 2018 and 2017

	2018	2017
Cash flows from operating activities:		
Increase in net assets	$ 9,179,350	$ 7,222,498
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	4,388,428	4,432,088
Bond issuance costs amortization	22,546	26,268
Gain on disposal of property and equipment	–	(1,233)
Realized and unrealized gains on investments and perpetual trusts, net	(7,162,444)	(5,093,102)
Interest rate swap agreements	(816,425)	(1,184,662)
Decrease in interest rate swap loan	(48,000)	(48,000)
Provision for bad debts	4,966,097	4,605,771
Restricted contributions and investment income	(559,420)	(249,383)
Changes in operating assets and liabilities:		
Accounts receivable	(5,672,611)	(4,868,204)
Inventories	4,052	(251,324)
Prepaid expenses	(149,965)	(191,149)
Notes and other receivables	132,289	(28,763)
Other assets	(4,459)	(4,605)
Accounts payable and accrued expenses	121,395	942,066
Accrued payroll and amounts withheld	101,277	(9,105)
Estimated third-party payor settlements	63,320	3,841,809
Net cash provided by operating activities	4,565,430	9,140,970
Cash flows from investing activities:		
Purchases of property and equipment	(4,724,538)	(3,609,488)
Proceeds from sale of property and equipment	–	1,300
Proceeds on sale of investments	30,652,397	317,791
Purchases of investments	(36,546,185)	(771,308)
Net cash used by investing activities	(10,618,326)	(4,061,705)
Cash flows from financing activities:		
Principal payments on long-term debt and capital lease obligations	(689,297)	(729,058)
Bond issuance costs	(118,989)	–
Restricted contributions and investment income	700,219	489,248
Net cash used by financing activities	(108,067)	(239,810)
Net (decrease) increase in cash and cash equivalents	(6,160,963)	4,839,455
Cash and cash equivalents at beginning of year	18,432,646	13,593,191
Cash and cash equivalents at end of year	$ 12,271,683	$18,432,646
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	$ 1,055,832	$ 1,082,231

See accompanying notes.

1. Description of Organization and Summary of Significant Accounting Policies

Organization

The Monadnock Community Hospital (the Hospital) is a not-for-profit, acute care hospital located in Peterborough, New Hampshire.

On December 30, 2016, the Hospital became affiliated with Catholic Medical Center (CMC), a 330-bed acute care hospital in Manchester, New Hampshire, and Huggins Hospital (HH), a 25-bed critical access hospital in Wolfeboro, 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 the Hospital and HH and co-member of CMC, along with CMC Healthcare System, Inc. 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 financial statements do not include the accounts and activity of GraniteOne, HH and CMC.

Basis of Accounting

The accompanying financial statements have been prepared on an accrual basis of accounting.

Use of Estimates

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

Cash and Cash Equivalents

Cash and cash equivalents include all demand deposit accounts and investments with original maturities of three months or less when purchased, excluding assets limited as to use. The Hospital maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Hospital has not experienced any losses on such accounts.

1. Description of Organization and Summary of Significant Accounting Policies (Continued)

Accounts Receivable and the Allowance for Doubtful Accounts

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectibility of accounts receivable, the Hospital analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Hospital records a provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Inventories

Inventories of supplies and pharmaceuticals are carried at the lower of cost or net realizable value. Costs are determined on the first-in, first-out (FIFO) basis.

Assets Limited as to Use

Assets limited as to use include assets held by trustees under indenture agreements, 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.

Investments

Investments are carried at fair value in the accompanying balance sheets. The Hospital has recorded net unrealized gains/losses on investments in the accompanying statements of operations and changes in net assets as a component of the change in net assets, but not as a component of the excess of revenue, support and nonoperating gains over expenses. Declines in fair value below the cost of investments are evaluated to determine if they are other-than-temporary. If such declines are determined to be other-than-temporary, an impairment charge is recognized within nonoperating losses. Realized gains and losses are determined on the specific identification method, however, mutual fund realized gains and losses are determined on the average cost method.

1. Description of Organization and Summary of Significant Accounting Policies (Continued)

Investment Policies

The Hospital'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.

Specific purpose 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 to increase, with minimum risk, the inflation adjusted principal and income of the endowment funds over the long term. The Hospital targets a diversified asset allocation that places emphasis on achieving its long-term return objectives within prudent risk constraints.

Property and Equipment

Property and equipment, including the medical office building, is stated at cost or, if donated, at fair value at the date of donation, less accumulated depreciation. The Hospital's policy is to capitalize expenditures for major improvements and charge maintenance and repairs currently for expenditures which do not extend the life of the related assets. When assets are retired or disposed of, the assets and related accumulated depreciation are eliminated from the accounts and any resulting gain or loss is reflected in the accompanying statements of operations.

Depreciation is computed using the straight-line method in a manner intended to amortize the cost of the assets over their estimated useful lives. Costs of construction and acquisition of assets not yet placed in service are included in capital improvements and no depreciation expense is recorded.

Bond Issuance Costs

Bond issuance costs are being amortized to interest expense using straight-line method, which approximates the effective interest method, over the life of the respective bonds. Bond issuance costs are presented as a component of long-term debt.

Earned Time

The Hospital provides and accrues for paid time off for vacation, holiday and sick leave under an earned time system for nonexempt employees. Hours earned, but not used, are capped and vested with the employee.

1. Description of Organization and Summary of Significant Accounting Policies (Continued)

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital has been limited by donors to a specified time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Hospital in perpetuity. Investment income, as well as realized and unrealized gains from permanently restricted net assets, is available for various uses as prescribed by the donors.

In accordance with the *Uniform Prudent Management of Institutional Funds Act* (UPMIFA), the Hospital 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 Policy for Appropriation of Assets for Expenditure

The Finance Committee of the Board of Trustees of the Hospital determines the method to be used to appropriate endowment funds for expenditure. As a guideline, approximately 4% of the total value of the three year quarterly average of available funds is intended to be distributed annually. The Finance Committee has the ability to distribute up to 5.99% of the total market value of the three-year quarterly average of available funds. Distributions of 6% or over must be approved by a vote of the Board of Trustees. The corresponding calculated spending allocations are distributed in equal quarterly installments from the current net total or accumulated net total investment returns for individual endowment funds. In establishing this policy, the Board of Trustees considered the expected long term rate of return on its endowment.

Donor-Restricted Contributions

Donated investments, supplies and equipment are reported at fair value at the date of receipt. Unconditional promises to give cash and other assets are reported at fair value at the date of the receipt of the promise. All gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of donated assets. When a donor restriction expires, that is, 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 accompanying statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying financial statements.

Excess of Revenue, Support and Nonoperating Gains Over Expenses

The accompanying statements of operations include excess of revenue, support and nonoperating gains over expenses. Changes in unrestricted net assets which are excluded from excess of revenue, support and nonoperating gains over expenses, consistent with industry practice, include net assets released from restrictions used for the purposes of acquiring long-lived assets, net unrealized gains/losses on investments and the changes in the fair value of interest rate swap agreements deemed to be effective hedges.

1. Description of Organization and Summary of Significant Accounting Policies (Continued)

Net Patient Service Revenue

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 period the related services are rendered and adjusted in future periods as final settlements are determined. Changes in these estimates are reflected in the accompanying financial statements in the year in which they occur. During 2018 and 2017, net patient service revenue in the accompanying statements of operations increased (decreased) approximately $641,000 and $(791,000), respectively, due to changes in prior year estimates. Services rendered to individuals from whom payment is expected and ultimately not received is written off and included as part of the provision for bad debts.

The Hospital 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 Hospital provides a discount approximately equal to that of its largest private insurance payors. On the basis of historical experience, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital records a significant provision for bad debts related to uninsured patients in the period the services are provided.

Activities directly associated with services related to acute and ancillary care services are considered to be operating activities and are included as patient service revenue. Revenue which is not related to patient medical care and which is normal to the day-to-day operations of the Hospital is included in other revenue.

Financial Assistance Program

The Hospital accepts all patients regardless of their ability to pay. A patient is classified as a financial assistance patient by reference to certain established policies of the Hospital. Essentially, these policies define the financial assistance program as those services for which no payment is anticipated. In assessing a patient's inability to pay, the Hospital utilizes federally established poverty guidelines. The financial assistance program is measured based on the Hospital's established rates. These charges are not included in net patient service revenue. The costs and expenses incurred in providing these services are included in operating expenses. The cost is estimated by utilizing a ratio of cost to gross charges applied to the gross uncompensated charges associated with providing charity care. See note 15.

Self-Insurance Programs

The Hospital self-insures its employee health and dental benefits and has estimated and accrued amounts to meet its expected obligations under the program. 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 Hospital recognizes revenue for services provided to employees of the Hospital during the year. Stop loss insurance coverage is in effect which mitigates the Hospital's exposure to loss on an individual and aggregate basis. Estimated unpaid claims, and those claims incurred but not reported at September 30, 2018 and 2017, have been recorded as a liability of approximately $300,000 within accrued payroll and amounts withheld in the accompanying balance sheets.

1. Description of Organization and Summary of Significant Accounting Policies (Continued)

Income Taxes

The Hospital is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. Management evaluated the Hospital's tax positions and concluded the Hospital 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 or disclosure in the accompanying financial statements.

Advertising Costs

The Hospital expenses advertising costs as incurred, and such costs totaled approximately $83,000 and $74,000 for the years ended September 30, 2018 and 2017, respectively.

Derivatives and Hedging Activities

The interest rate swap agreements held by the Hospital meet the definition of derivative instruments and, consequently, the Hospital is required to record as an asset or liability the fair value of the interest rate swap agreements described in Note 8. The Hospital is exposed to repayment loss equal to any net amounts receivable under the swap agreements (not the notional amounts) in the event of nonperformance of the other parties to the swap agreements. However, the Hospital does not anticipate nonperformance and does not obtain collateral from the other parties.

Related Party Activity

The Hospital has engaged in various transactions with GraniteOne and CMC. The Hospital recognized revenue from these related parties of approximately $340,000 for the year ended September 30, 2018 and $215,000 from the date of affiliation, December 30, 2016 through September 30, 2017, which is reflected within other revenue in the accompanying statements of operations. The Hospital also incurred expenses to these related parties of approximately $3.1 million for the year ended September 30, 2018 and $2.2 million from the date of affiliation, December 30, 2016 through September 30, 2017, which is reflected within operating expenses in the accompanying statements of operations. The effect of these transactions resulted in a net amount due to related parties of approximately $187,000 and $437,000 as of September 30, 2018 and 2017, respectively, which is reflected within accounts payable and accrued expenses in the accompanying balance sheets.

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 Hospital 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 Hospital on October 1, 2019. ASU 2014-09 permits the use of either the retrospective or cumulative effect transition method. The Hospital is evaluating the impact that ASU 2014-09 will have on its financial statements and related disclosures.

1. Description of Organization and Summary of Significant Accounting Policies (Continued)

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 Hospital 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 Hospital is currently evaluating the impact of the pending adoption of ASU 2016-02 on the Hospital's 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 Hospital's fiscal year ending September 30, 2019, with early adoption permitted. The Hospital is currently evaluating the impact of the pending adoption of ASU 2016-14 on the Hospital's 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 Hospital's fiscal year ended September 30, 2020, and early adoption is permitted. ASU 2016-18 must be applied using a retrospective transition method. The Hospital is currently evaluating the impact of the adoption of this guidance on its financial statements.

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 Hospital on October 1, 2019, with early adoption permitted. The Hospital is currently evaluating the impact that ASU 2018-08 will have on its financial statements.

Subsequent Events

Management has evaluated subsequent events occurring between the end of its fiscal year and January 10, 2019, the date the financial statements were available to be issued.

2. Accounts Receivable

Accounts receivable are stated net of estimated contractual allowances and allowances for doubtful accounts. Accounts receivable consists of the following at September 30:

	2018	2017
Gross accounts receivable	$24,239,257	$23,019,453
Estimated contractual allowances	(8,305,416)	(8,045,374)
Estimated allowance for doubtful accounts	(6,460,622)	(6,207,374)
Accounts receivable, net	$ 9,473,219	$ 8,766,705

The Hospital's allowance for doubtful accounts for collection trends increased from 90% of self-pay accounts receivable at September 30, 2017 to 91% of self-pay accounts receivable at September 30, 2018. The Hospital's bad debt writeoffs increased $486,689 from $4,226,360 in 2017 to $4,713,049 in 2018. The increase in bad debt writeoffs was primarily a result of collection trends.

3. Estimated Third-Party Settlements

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare

The Hospital was granted critical access hospital (CAH) designation on December 27, 2004. As a result of this designation, the Hospital is entitled to cost-based reimbursement from Medicare for services provided to Medicare beneficiaries. Inpatient acute care services rendered to Medicare program beneficiaries are paid under a cost reimbursement methodology. Outpatient services are paid based on a combination of rate schedules and reimbursed cost. The Hospital is reimbursed for cost reimbursable items at an interim rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. As of the date of these financial statements, the Hospital's Medicare cost reports have been settled through September 30, 2013.

Medicaid

Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement methodology subject to certain limitations. The Hospital is reimbursed at an interim rate with final settlement determined after submission of annual costs reported by the Hospital and audits thereof by the State of New Hampshire Division of Audit. As of the date of these financial statements, the Hospital's Medicaid cost reports have been final settled through September 30, 2012.

Anthem

Inpatient and outpatient services rendered to Anthem subscribers are reimbursed at submitted charges less a discount withholding or through a per diem or fee schedule. The amounts paid to the Hospital are not subject to any retroactive adjustments.

3. Estimated Third-Party Settlements (Continued)

Other

The Hospital has also entered into payment agreements with certain commercial insurance carriers and health maintenance organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, per diems and discounts from established charges.

The Hospital has made a provision in the financial statements for estimated final settlements to be paid as a result of the retroactive provision for third-party reimbursement programs. Actual results could differ from those estimates.

Medicaid Enhancement Tax and Medicaid Disproportionate Share

Under the State of New Hampshire's tax code, the State imposes a MET equal to 5.4% of net patient service revenue in State fiscal years 2018 and 2017, with certain exclusions. The amount of tax incurred by the Hospital for fiscal 2018 and 2017 was $3,613,664 and $3,367,222, respectively. The Hospital has accrued $948,566 and $841,806 in MET at September 30, 2018 and 2017, respectively, within accounts payable and accrued expenses in the accompanying balance sheets.

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. In 2018 and 2017, the Hospital recognized disproportionate share revenues (net of related reserves) totaling $4,100,348 and $2,100,000, respectively, in the accompanying statements of operations. Currently, the State of New Hampshire makes disproportionate share hospital payments to support up to 75% of the actual uncompensated care costs for New Hampshire's hospitals with critical access designation.

CMS has completed audits of the State's program and the DSH 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 Hospital has recorded reserves to address its potential exposure based on the audit results to date.

4. Concentration of Credit Risk

Financial instruments which subject the Hospital to credit risk consist of cash and cash equivalents, accounts receivable and investments. The risk with respect to cash equivalents is minimized by the Hospital's policy of investing in financial instruments with short-term maturities issued by highly rated financial institutions. Investments that exceeded 10% of investments include the Vanguard Total Stock Market Index Fund and the Vanguard Total International Stock Index Fund as of September 30, 2018. There were no investments that exceeded 10% of total investments as of September 30, 2017.

4. Concentration of Credit Risk Continued)

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The Hospital's accounts receivable are primarily due from third-party payors, and amounts are presented net of expected contractual allowances and uncollectible amounts. The mix of gross patient accounts receivable at September 30, 2018 and 2017 was as follows:

	2018	2017
Medicare	33%	36%
Medicaid	4	4
Anthem	10	7
Other third-party payors	28	25
Patients	25	28
	100%	100%

5. Pledges Receivable

Pledges receivable consist of unconditional promises for contributions receivable in subsequent years. The following represents amounts promised to be contributed to the Hospital during the years ended September 30:

	2018	2017
In one year or less	$ 207,967	$ 404,456
Between one and five years	325,121	430,120
	533,088	834,576
Present value discount	(39,759)	(86,840)
Allowance for uncollectible pledges ($112,044 and $172,423 of which is allocated to the current portion of pledges receivable at September 30, 2018 and 2017, respectively)	(197,671)	(311,279)
	$ 295,658	$ 436,457

6. Assets Limited as to Use and Restricted Funds

The composition of assets limited as to use at September 30, 2018 and 2017 is set forth in the following table. Investments are stated at fair value.

	2018	2017
Board designated, donor restricted and long-term investments:		
Cash and cash equivalents	$ 1,038,519	$ 1,384,854
Marketable equity securities	29,504,809	35,367,826
Mutual funds	31,116,523	609,842
U.S. Treasury obligations	1,043,233	12,604,498
Interests in perpetual trusts	4,819,945	4,499,777
	$67,523,029	$54,466,797

As a result of bequests, the Hospital is the beneficiary of two trust funds, one of which is administered by an outside trustee and the other administered by the Hospital. The terms of the perpetual trusts require that income or a percentage of income be paid to the Hospital in perpetuity; however, distribution of principal is not permitted under the terms of the trusts. The amounts recorded in the accompanying balance sheets represent the fair values of the assets upon notification of the trusts' existence, which are adjusted annually to reflect the appreciation or depreciation in the fair value of the assets. Offsetting amounts are included in permanently restricted net assets. Income distributed to the Hospital from these trusts is included in the accompanying statements of operations as investment income.

Investment income and realized and unrealized (losses) gains on investments are summarized as follows:

	2018	2017
Unrestricted:		
Investment income	$ 877,913	$ 507,282
Net realized gains on investments	5,919,940	616,999
Net unrealized (losses) gains on investments	(103,293)	3,445,760
	6,694,560	4,570,041
Restricted:		
Investment income	66,016	43,414
Net realized gains on investments	1,030,446	113,611
Net unrealized (losses) gains on investments	(4,817)	596,929
Net change in perpetual trusts	320,168	319,803
	1,411,813	1,073,757
	$8,106,373	$5,643,798

During fiscal year 2018, the Hospital sold a significant portion of its investment portfolio. The Hospital subsequently reinvested the proceeds from that sale into new investments in 2018.

6. Assets Limited as to Use and Restricted Funds (Continued)

The following table summarizes the aggregate unrealized losses on investments held at September 30, 2018 and 2017:

	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
2018						
Marketable equity securities	$ 1,047,737	$ (90,250)	$ –	$ –	$ 1,047,737	$ (90,250)
Mutual funds	16,150,652	(870,927)	–	–	16,150,652	(870,927)
Fixed income	391,215	(4,636)	552,832	(20,239)	944,047	(24,875)
	$17,589,604	$(965,813)	$552,832	$(20,239)	$18,142,436	$(986,052)
2017						
Mutual funds	$ 118,190	$ (1,521)	$ 12,407	$ (140)	$ 130,597	$ (1,661)
Fixed income	568,250	(4,821)	99,770	(531)	668,020	(5,352)
	$ 686,440	$ (6,342)	$112,177	$ (671)	$ 798,617	$ (7,013)

Unrealized losses within marketable equity securities of $90,250 at September 30, 2018, due mainly to market fluctuations, consist of two securities, none of which had unrealized losses for more than twelve months. Unrealized losses within mutual funds of $870,927 at September 30, 2018, due mainly to market fluctuations, consist of ten funds, none of which had unrealized losses for more than twelve months. Other unrealized losses in the Hospital's fixed income portfolio of $24,875 at September 30, 2018 consist of ten funds, six of which had unrealized losses for more than twelve months, and are attributed to market fluctuations and the impact movements in market interest rates have had in comparison to the underlying yields on these securities.

Management of the Hospital, in addition to considering current trends and economic conditions that may affect the quality of individual securities within the Hospital's investment portfolio, also considers the Hospital's ability and intent to hold such securities to maturity or recovery. Management does not believe any of the Hospital's securities with unrealized losses as described above are other than temporarily impaired at September 30, 2018 and 2017.

7. Property and Equipment

Property and equipment consists of the following at September 30:

	2018	2017
Land and land improvements	$ 4,686,848	$ 4,686,848
Building and building improvements	28,242,378	28,242,378
Equipment, including capital leases	59,374,059	55,273,355
Capital improvements in progress	1,114,597	864,871
	93,417,882	89,067,452
Less accumulated depreciation and amortization	(57,511,929)	(53,592,606)
	$ 35,905,953	$ 35,474,846

7. Property and Equipment (Continued)

The cost of assets recorded under capital leases totaled $679,756 at September 30, 2018 and 2017. The cost of these assets has been included with property and equipment, and accumulated amortization included with accumulated depreciation. Accumulated amortization associated with assets recorded under capital leases was $600,451 and $464,500 at September 30, 2018 and 2017, respectively.

8. Long-Term Debt and Capital Lease Obligations

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

	2018	2017
New Hampshire Business Finance Authority (NHBFA) in conjunction with Revenue Bonds Series 2013 with variable rate interest, amended and restated as of June 27, 2018, as described below	$24,399,669	$24,947,152
Interest rate swap loan (see below)	92,000	140,000
Capital lease obligations with interest rates of 3.25%, due in monthly installments of $12,290, maturity date is May 2019, collateralized by equipment (note 7)	97,132	238,946
	24,588,801	25,326,098
Less unamortized bond issuance costs	(166,628)	(70,185)
Less current portion	(717,483)	(737,298)
	$23,704,690	$24,518,615

On January 1, 2013, the Hospital refinanced its existing 2007 Series Bonds outstanding in the amount of $17,810,000 and its 2009 Series Bonds outstanding in the amount of $9,424,908 through the issuance of $27,240,000 in 2013 Series Bonds with NHBFA. The initial interest rate on the bonds through January 1, 2023 was a variable rate equal to 75% of the one-month LIBOR plus 1.3125%. The final maturity of the bonds was January 1, 2043 and on January 1, 2023, the bonds were required to be remarketed upon a stipulated mandatory redemption.

On June 27, 2018, the 2013 Series Revenue Bonds with NHBFA were amended and restated. The original bonds were exchanged for amended bonds and the original bond issuance was cancelled. The amended 2013 Series Bonds with NHBFA were issued in the amount of $24,584,872, which was the amount of the outstanding balance of the original 2013 Series Bonds at the time of closing. The initial interest rate on the amended bonds through July 1, 2028 is a variable rate equal to 81.5% of the one-month LIBOR plus 1.45%. The interest rate at September 30, 2018 was 2.90%. The final maturity of the amended bonds remained January 1, 2043. On January 1, 2028, the amended bonds must be remarketed upon a stipulated mandatory redemption. The Hospital is also required to comply with certain financial and other covenants and has granted as security all gross receipts, together with all real and personal property, as defined. The amended Series 2013 Bonds require the same debt service payments as the original 2013 Series Bonds with payments ranging from $408,605 to $1,589,792 per year.

8. Long-Term Debt and Capital Lease Obligations (Continued)

Concurrent with the 2009 NHBFA bond issuance, the Hospital executed an interest rate swap agreement to hedge its exposure to the volatility of interest payments on its variable rate Series 2009 Revenue Bonds. During 2013, the Series 2009 Revenue Bonds were refinanced through the issuance of Series 2013 Revenue Bonds, as previously discussed. All existing terms of the swap remained in effect. At September 30, 2017, an interest rate swap agreement was outstanding at a notional amount totaling approximately $8.5 million. The swap agreement hedged the Hospital's interest exposure by effectively converting interest payments from variable rates to a fixed rate of 2.9%. The swap agreement was designated as a cash flow hedge of the underlying variable rate interest payments, and changes in the fair value of the swap agreement were reported as a change in unrestricted net assets. The swap agreement had a fair value of $(303,044) as of September 30, 2017. As a part of the 2013 Series Bonds amendment previously discussed, this swap agreement was terminated during 2018.

Concurrent with the 2007 NHBFA bond issuance, the Hospital executed an interest rate swap agreement to hedge its exposure to the volatility of interest payments on a portion of its variable rate Series 2007 Revenue Bonds. During 2013, the Series 2007 Revenue Bonds were refinanced through the issuance of Series 2013 Revenue Bonds, as previously discussed. All existing terms of the swap remained in effect. At September 30, 2018, an interest rate swap agreement was outstanding at a notional amount totaling approximately $8.9 million. The swap agreement hedged the Hospital's interest exposure by effectively converting interest payments from variable rates to a fixed rate of 3.57%. The swap agreement, which expires in October 2033, 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. The swap agreement had a fair value of $(1,005,561) and $(1,555,551) as of September 30, 2018 and 2017, respectively.

The Hospital had a third interest rate swap agreement with a financial institution, which was originally issued in connection with the 2004 New Hampshire Health and Education Facilities Authority (NHHEFA) bonds, which were refunded during 2008. During 2010, the Hospital replaced this 2004 swap agreement with a new 2010 swap agreement that effectively hedged a portion of the 2007 NHBFA bonds. This newly issued swap agreement contained an additional interest rate spread, which in turn provided that the issuing bank make a cash payment to fund the payoff of the 2004 swap agreement on behalf of the Hospital. Accordingly, the Hospital recognized an interest rate swap loan liability of $480,000 during 2010, which represents the fair value of the 2004 swap at the time it was replaced. This loan is being amortized by the Hospital over the life of the new swap agreement. At September 30, 2017, an interest rate swap agreement was outstanding relating to the 2010 swap at a notional amount totaling approximately $6.2 million. The 2010 swap agreement hedged the Hospital's interest exposure by effectively converting interest payments from variable rates to a fixed rate of 2.76%. The swap agreement was designated as a cash flow hedge of the underlying variable rate interest payments, and changes in the fair value of the swap agreement were reported as a change in unrestricted net assets. The swap agreement had a fair value of $(135,406) as of September 30, 2017. As a part of the 2013 Series Bonds amendment previously discussed, this swap agreement was terminated during 2018.

8. Long-Term Debt and Capital Lease Obligations (Continued)

Concurrent with the amended and restated 2013 Series Revenue Bonds, the Hospital executed an interest rate swap agreement effective July 1, 2018 to hedge its exposure to the volatility of interest payments on a portion of its variable rate on the amended and restated 2013 Series Revenue Bonds. At September 30, 2018, an interest rate swap agreement was outstanding at a notional amount totaling approximately $14.1 million. The swap agreement hedges the Hospital's interest exposure by effectively converting interest payments from variable rates to a fixed rate of 2.64%. The swap agreement, which expires July 1, 2028, is designated as a cash flow hedge of the underlying variable interest payments, and changes in the fair value of the swap agreement are reported as a change in unrestricted net assets. The swap agreement had a fair value of $(172,015) as of September 30, 2018.

During the year, the Hospital pays or receives the difference between the fixed and variable rates applied to the notional amounts of the above interest rate swap agreements. During 2018 and 2017, such charges were $383,554 and $553,989, respectively.

In connection with the amended and restated 2013 Series Revenue Bonds, the Hospital is required to comply with certain restrictive financial covenants including, but not limited to, debt service coverage and debt to equity ratios. At September 30, 2018, the Hospital was in compliance with these restrictive covenants.

The scheduled maturities on long-term debt for the next five years are as follows:

	Long-Term Debt	Capital Lease Obligations	Total
2019 (included in current liabilities)	$ 620,351	$ 97,132	$ 717,483
2020	642,346	–	642,346
2021	625,522	–	625,522
2022	653,933	–	653,933
2023	683,634	–	683,634
Thereafter	21,265,883	–	21,265,883
	$24,491,669	$ 97,132	$ 24,588,801

The Hospital also has an available $3,000,000 revolving demand line of credit with a financial institution. The line of credit bears no interest unless drawn at the Hospital's option in which case the rate is equal to the prime rate or 1, 2 or 3 month LIBOR plus 2.5% (5.25% at September 30, 2018). There was no balance outstanding under this agreement at September 30, 2018 or 2017. The line of credit is subject to renewal on May 31, 2019.

9. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available for the following purposes or periods at September 30:

	2018	2017
Health care services:		
Purchase of equipment	$ 6,522	$ 18,670
Health education	550,489	363,686
Pledges receivable	295,658	436,457
Capital appreciation on endowment funds:		
Accumulated realized gains	1,705,910	675,464
Unrealized gains	2,298,376	2,303,193
Amounts released under spending policy	(479,298)	(239,649)
	$4,377,657	$3,557,821

Permanently restricted net assets of $9,039,387 and $8,719,219 at September 30, 2018 and 2017, respectively, are to be held in perpetuity and include two perpetual trusts (Note 6). The income and dividends on permanently restricted net assets are generally expendable to support health care services and capital purchases at the discretion of the Hospital and are principally recorded as net assets released from restrictions for the purchase of property and equipment.

Activity in fiscal 2018 and 2017 related to endowment funds was as follows:

	Temporarily Restricted Net Assets	Permanently Restricted Net Assets
2018		
Balances, beginning of year	$2,739,008	$ 4,220,482
Interest and dividends	124,169	–
Realized and unrealized gains on investments	1,025,629	–
Amounts released under spending policy	(239,649)	–
Appropriation for expenditure	(124,169)	–
Balances, end of year	$3,524,988	$ 4,220,482
2017		
Balances, beginning of year	$2,268,117	$ 4,220,482
Interest and dividends	82,894	–
Realized and unrealized gains on investments	710,540	–
Amounts released under spending policy	(239,649)	–
Appropriation for expenditure	(82,894)	–
Balances, end of year	$2,739,008	$ 4,220,482

10. Net Patient Service Revenue

Net patient service revenue, before provision for bad debts, consists of the following for the years ended September 30:

	2018	2017
Gross patient service charges:		
Routine services	$ 18,920,316	$ 17,153,803
Ancillary services	143,010,656	129,706,691
	161,930,972	146,860,494
Deductions from revenue:		
Contractual adjustments and administrative write offs	(77,370,032)	(67,200,742)
Financial assistance program	(1,733,551)	(1,657,248)
Disproportionate share funding (note 3)	4,100,348	2,100,000
	(75,003,235)	(66,757,990)
Net patient service revenue, before provision for bad debts	$ 86,927,737	$ 80,102,504

An estimated breakdown of patient service revenue, net of contractual allowances, discounts and provision for bad debts recognized in 2018 and 2017 from these major payor sources, is as follows:

	Gross Patient Service Revenue	Contractual Allowances and Discounts	Provision for Bad Debts	Net Patient Service Revenue Less Provision for Bad Debts
2018				
Private payors (includes coinsurance and deductibles)	$ 68,650,215	$(28,779,974)	$ (3,875,381)	$35,994,860
Medicaid	10,188,961	(6,923,199)	(44,230)	3,221,532
Medicare	77,148,328	(36,411,872)	(221,566)	40,514,890
Self-pay	5,943,468	(2,888,190)	(824,920)	2,230,358
	$161,930,972	$(75,003,235)	$(4,966,097)	$81,961,640
2017				
Private payors (includes coinsurance and deductibles)	$ 64,794,078	$(25,417,525)	$ (3,346,944)	$36,029,609
Medicaid	9,714,866	(6,752,441)	(52,494)	2,909,931
Medicare	66,812,333	(32,079,748)	(327,833)	34,404,752
Self-pay	5,539,217	(2,508,276)	(878,500)	2,152,441
	$146,860,494	$(66,757,990)	$(4,605,771)	$75,496,733

10. Net Patient Service Revenue (Continued)

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, 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.

Other Revenue

During 2017, the Hospital received approximately $1.1 million under a risk retention policy settlement. This amount is recorded as other revenue for the year ended September 30, 2017 in the accompanying statements of operations.

11. Employee Benefit Plans

The Hospital has a tax-sheltered annuity plan covering substantially all of its employees. Participating employees become eligible for employer contributions following the completion of two years of service, as defined, and attainment of age 21. Employer contributions are determined based on a percentage of employees' salaries. Benefit expense related to this plan for the years ended September 30, 2018 and 2017 amounted to approximately $502,000 and $486,000, respectively.

The Hospital also offers to certain physicians the option to participate in an Internal Revenue Code Section 457 deferred compensation plan to which the Hospital may make a discretionary contribution. The Hospital made no contributions to the Plan for the years ended September 30, 2018 and 2017.

12. Commitments and Contingencies

Operating Leases

The Hospital has various operating leases relative to certain equipment and various office facilities. Future annual minimum lease payments under these noncancellable leases as of September 30, 2018 are as follows:

Year ending September 30:	
2019	$272,960
2020	152,339
2021	143,068
2022	113,791
2023	73,904

Rent expense was approximately $559,000 and $488,000 for the years ended September 30, 2018 and 2017, respectively.

12. Commitments and Contingencies (Continued)

Malpractice Loss Contingencies

The Hospital maintains malpractice insurance coverage on a claims-made basis. The claims-made policies, which are subject to retrospective adjustment and renewal on an annual basis, cover only claims made during the term of the policies, but not those occurrences for which claims may be made after expiration of the policies. The Hospital intends to renew its coverage and has no reason to believe that it will be prevented from renewing such coverage.

In accordance with ASU No. 2010-24, *"Health Care Entities" (Topic 954): Presentation of Insurance Claims and Related Recoveries*, the Hospital is required to record a liability related to estimated professional liability losses and also a receivable related to estimated recoveries under insurance coverage for recoveries of potential losses. At September 30, 2018 and 2017, management of the Hospital estimated that the Hospital did not have any significant exposure arising from estimated professional liability losses or significant estimated recoveries under insurance coverage for recoveries of potential losses.

13. Volunteer Services (Unaudited)

In 2018 and 2017, total volunteer service hours received by the Hospital were approximately 11,900. The volunteers provide nonspecialized services to the Hospital, none of which have been recognized as revenue or expense in the statements of operations.

14. Functional Expenses

The Hospital provides general health care services to residents within its geographic location. Expenses, excluding the New Hampshire Medicaid enhancement tax, related to providing these services are as follows for the years ended September 30, 2018 and 2017:

	2018	2017
Health care services	$75,127,027	$69,362,960
General and administrative, including interest	9,265,163	9,040,699
	$84,392,190	$78,403,659

Fundraising related expenses were approximately $458,000 and $448,000 for the years ended September 30, 2018 and 2017, respectively.

15. Financial Assistance Program and Community Benefits (Unaudited)

The Hospital maintains records to identify and monitor the level of financial assistance it provides. These records include the amount of charges foregone for services and supplies furnished under its financial assistance program, the estimated cost of those services and supplies, and equivalent service statistics. The following information measures the level of financial assistance provided during the years ended September 30, 2018 and 2017:

	2018	2017
Charges foregone, based on established rates (note 1)	$1,734,000	$1,657,000
Estimated costs incurred to provide financial assistance	$ 992,000	$ 971,000
Equivalent percentage of financial assistance services to all services	1.07%	1.13%

In addition to the financial assistance identified above, the Hospital does not receive full payment from the Medicare and Medicaid programs for the cost of services to certain poor and elderly patients served. In 2018 and 2017, the Hospital incurred costs in excess of payments in these programs amounting to approximately $4,420,000 and $5,344,000, respectively.

The Hospital also provides other services to the community at no cost or reduced cost, such as screenings, clinics, etc. The cost of providing these services was approximately $3,350,000 and $3,288,000 for the years ended September 30, 2018 and 2017, respectively.

The Hospital also has direct subsidies of approximately $4,355,000 and $3,600,000 for primary care and various specialty practices for the years ended September 30, 2018 and 2017, respectively.

16. Fair Value of Financial Instruments

Fair value of a financial instrument is defined 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. In determining fair value, the Hospital uses various methods including market, income and cost approaches. Based on these approaches, the Hospital often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs. The Hospital utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques, the Hospital is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

Level 1 – Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury and federal agency securities and federal agency mortgage-backed securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

16. Fair Value of Financial Instruments (Continued)

Level 2 – Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or similar assets or liabilities.

Level 3 – Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

In determining the appropriate levels, the Hospital performs a detailed analysis of the assets and liabilities that are subject to fair value measurements. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3.

For the fiscal year ended September 30, 2018, the application of valuation techniques applied to similar assets and liabilities has been consistent with prior years.

The following presents the balances of assets and liabilities measured at fair value on a recurring basis at September 30:

	Total	Level 1	Level 2	Level 3
2018				
Assets:				
Assets limited as to use:				
Cash and cash equivalents	$ 1,038,519	$ 548,393	$ 490,126	$ –
U.S. Treasury obligations	1,043,233	1,043,233	–	–
U.S. common stock:				
Technology	8,485,427	8,485,427	–	–
Healthcare	3,276,072	3,276,072	–	–
Consumer goods	6,847,685	6,847,685	–	–
Industrial goods	2,315,356	2,315,356	–	–
Services	7,228,649	7,228,649	–	–
Financial	639,320	639,320	–	–
Utilities	712,300	712,300	–	–
Mutual funds:				
Domestic	10,568,725	10,568,725	–	–
International	6,391,702	6,391,702	–	–
Fixed income	14,156,096	14,156,096	–	–
Investments in perpetual trusts	4,819,945	–	4,819,945	–
	$67,523,029	$62,212,958	$5,310,071	$ –
Liabilities:				
Interest rate swap agreements	$ 1,177,576	$ –	$ –	$1,177,576

16. Fair Value of Financial Instruments (Continued)

The following presents the balances of assets and liabilities measured at fair value on a recurring basis at September 30:

	Total	Level 1	Level 2	Level 3
2017				
Assets:				
Assets limited as to use:				
Cash and cash equivalents	$ 1,384,854	$ 372,829	$ 1,012,025	$ –
U.S. Treasury obligations	12,604,498	12,604,498	–	–
U.S. common stock:				
Technology	9,403,131	9,403,131	–	–
Healthcare	4,661,826	4,661,826	–	–
Consumer goods	10,991,710	10,991,710	–	–
Industrial goods	2,245,640	2,245,640	–	–
Services	6,987,270	6,987,270	–	–
Financial	492,048	492,048	–	–
Utilities	586,201	586,201	–	–
Mutual funds:				
Domestic	300,786	300,786	–	–
International	71,999	71,999	–	–
Fixed income	237,057	237,057	–	–
Investments in perpetual trusts	4,499,777	–	4,499,777	–
	$54,466,797	$48,954,995	$5,511,802	$ –
Liabilities:				
Interest rate swap agreements	$ 1,994,001	$ –	$ –	$1,994,001

The valuation of the interest rate swap agreements is estimated by a third party based on the anticipated cash flows under the swap agreements over their duration at market interest rates at September 30, 2018 and 2017.

The following presents the change in Level 3 instruments for the years ended September 30:

	Interest Rate Swaps 2018	Interest Rate Swaps 2017
Balance, beginning of year	$ (1,994,001)	$ (3,178,663)
Total unrealized gains, included in changes in unrestricted net assets	816,425	1,184,662
Balance, end of year	$ (1,177,576)	$ (1,994,001)

Investments, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. As such, it is reasonably possible that changes in the fair value of investments will occur in the near term and that such changes could materially affect the amounts reported in the accompanying balance sheets and statements of operations.

16. Fair Value of Financial Instruments (Continued)

The following methods and assumptions were used by the Hospital in estimating the "fair value" of other financial instruments in the accompanying financial statements and notes thereto:

Cash and cash equivalents: The carrying amounts reported in the accompanying statements of financial position for these financial instruments approximate their fair values.

Accounts and other receivables, pledges receivable, notes receivable, accounts payable and estimated third-party payor settlements: The carrying amounts reported in the accompanying statements of financial position approximate their respective values as these financial instruments have short-term maturities or are recorded at amounts that approximate fair value.

Long-term debt: The fair value of substantially all long-term debt approximates its carrying value due to the variable rate interest terms.