Flagler Hospital, Inc. and Subsidiaries
dba Flagler Health+

Consolidated Financial Report
with Additional Information
September 30, 2019

Contents

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Independent Auditor's Report

To the Board of Trustees
Flagler Hospital, Inc. and Subsidiaries
dba Flagler Health+

We have audited the accompanying consolidated financial statements of Flagler Hospital, Inc. and Subsidiaries dba Flagler Health+ (the "System"), which comprise the consolidated balance sheet as of September 30, 2019 and 2018 and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated 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.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated 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 audits 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 auditor's 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 Flagler Hospital, Inc. and Subsidiaries dba Flagler Health+ as of September 30, 2019 and 2018 and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Trustees
Flagler Hospital, Inc. and Subsidiaries
dba Flagler Health+

Emphasis of Matter

As described in Note 2 to the consolidated financial statements, Flagler Hospital, Inc. and Subsidiaries dba Flagler Health+ adopted the provisions of Accounting Standards Codification (ASC) Topic 606, *Revenue from Contracts with Customers*, using the modified retrospective adoption method as of October 1, 2018 and adopted the provisions of ASC Topic 958, *Presentation of Financial Statements of Not-for-Profit Entities*, using the retrospective adoption method as of the year ended September 30, 2019. Our opinion is not modified with respect to these matters.

Plante & Moran, PLLC

January 21, 2020

Consolidated Balance Sheet

September 30, 2019 and 2018

	2019	2018
Assets		
Current Assets		
Cash and cash equivalents	$ 22,012,172	$ 17,594,905
Patient accounts receivable (Note 4)	34,260,395	30,552,765
Supplies	8,662,509	7,949,704
Third-party payor settlements (Note 3)	1,561,855	-
Prepaid expenses and other current assets	6,426,141	5,783,564
Total current assets	72,923,072	61,880,938
Assets Limited as to Use (Note 5)	94,145,990	106,191,050
Investments (Note 5)	33,112,989	33,346,891
Property and Equipment - Net (Note 7)	174,286,211	159,198,697
Goodwill (Note 15)	24,895,534	24,895,534
Other Assets	13,718,422	6,811,004
Total assets	**$ 413,082,218**	**$ 392,324,114**
Liabilities and Net Assets		
Current Liabilities		
Accounts payable	$ 8,951,344	$ 9,496,263
Current portion of long-term debt (Note 8)	7,397,648	6,545,000
Third-party payor settlements (Note 3)	-	882,670
Accrued expenses and other current liabilities	13,197,896	15,353,755
Total current liabilities	29,546,888	32,277,688
Long-term Debt - Net of current portion (Note 8)	132,164,949	123,302,529
Other Liabilities		
Deferred rent	3,951,082	3,587,819
Other long-term liabilities	16,665,879	13,066,069
Total liabilities	182,328,798	172,234,105
Net Assets		
Without donor restrictions	223,711,880	213,882,474
With donor restrictions (Note 9)	7,041,540	6,207,535
Total net assets	230,753,420	220,090,009
Total liabilities and net assets	**$ 413,082,218**	**$ 392,324,114**

See notes to consolidated financial statements.

Consolidated Statement of Operations

Years Ended September 30, 2019 and 2018

	2019	2018
Unrestricted Revenue, Gains, and Other Support		
Net patient service revenue before provision for bad debts		$ 275,940,119
Provision for bad debts		(15,412,732)
Net patient service revenue (Note 3)	$ 278,937,741	260,527,387
Other operating revenue	6,022,636	9,224,982
Net assets released from restrictions	50,243	81,942
Total unrestricted revenue, gains, and other support	285,010,620	269,834,311
Expenses		
Salaries	87,593,940	85,589,103
Supplies	57,861,011	53,202,453
Purchased services	45,873,238	38,490,837
Depreciation and amortization (Note 7)	22,358,329	22,984,608
Employee benefits	20,168,763	22,514,325
Professional services	22,831,212	18,691,479
Lease and rental	6,653,862	5,439,892
Insurance	4,411,597	4,616,767
Interest expense	4,123,415	4,882,020
Other expenses	3,247,512	3,801,847
Indigent tax	3,034,882	3,011,992
Utilities	2,877,192	2,794,459
Total expenses	281,034,953	266,019,782
Operating Income	3,975,667	3,814,529
Nonoperating Income		
Gain on acquisition (Note 15)	-	354,667
Investment income (Note 5)	4,834,473	9,951,643
Other nonoperating income	402,303	52,710
Total nonoperating income	5,236,776	10,359,020
Excess of Revenue Over Expenses	9,212,443	14,173,549
Net Assets Released from Restrictions	616,963	416,082
Increase in Net Assets without Donor Restrictions	**$ 9,829,406**	**$ 14,589,631**

See notes to consolidated financial statements.

Consolidated Statement of Changes in Net Assets

Years Ended September 30, 2019 and 2018

	2019	2018
Net Assets without Donor Restrictions		
Excess of revenue over expenses	$ 9,212,443	$ 14,173,549
Net assets released from restrictions	616,963	416,082
Increase in net assets without donor restrictions	9,829,406	14,589,631
Net Assets with Donor Restrictions		
Restricted contributions	1,447,043	273,811
Restricted investment income	24,839	31,456
Net realized and unrealized gains on investments	29,329	232,497
Net assets released from restrictions	(667,206)	(498,024)
Increase in net assets with donor restrictions	834,005	39,740
Increase in Net Assets	10,663,411	14,629,371
Net Assets - Beginning of year	220,090,009	205,460,638
Net Assets - End of year	**$ 230,753,420**	**$ 220,090,009**

Consolidated Statement of Cash Flows

Years Ended September 30, 2019 and 2018

	2019	2018
Cash Flows from Operating Activities		
Increase in net assets	$ 10,663,411	$ 14,629,371
Adjustments to reconcile increase in net assets to net cash and cash equivalents from operating activities:		
Depreciation and amortization	22,300,934	22,933,252
(Gain) loss on disposal of property and equipment	(26,344)	45,470
Provision for bad debts	-	15,412,732
Net realized and unrealized gains on investments and assets limited as to use	(237,447)	(5,400,900)
Net realized and unrealized gains and investment income on restricted investments	(54,168)	(263,953)
Restricted contributions received	(1,447,043)	(273,811)
Gain on joint ventures	(111,240)	(456,336)
Gain on acquisition	-	(354,667)
Changes in operating assets and liabilities that (used) provided cash and cash equivalents:		
Accounts receivable	(3,707,630)	(18,817,531)
Supplies	(712,805)	(1,229,939)
Prepaid expenses, other current assets, and other assets	(4,434,755)	(961,128)
Third-party payor settlements	(2,444,525)	893,161
Accounts payable, accrued expenses, other current liabilities, and other long-term liabilities	2,020,568	69,752
Net cash and cash equivalents provided by operating activities	21,808,956	26,225,473
Cash Flows from Investing Activities		
Purchase of property and equipment	(21,886,653)	(32,910,115)
Proceeds from disposition of property and equipment	26,344	-
Purchases of investments and assets limited as to use	(9,958,753)	(8,666,376)
Proceeds from sales and maturities of investments and assets limited as to use	19,475,162	50,202,653
Cash paid to joint ventures	(4,000)	(15,000)
Cash paid for goodwill	-	(14,876,263)
Net cash and cash equivalents used in investing activities	(12,347,900)	(6,265,101)
Cash Flows from Financing Activities		
Repayment of long-term debt	(6,545,000)	(7,005,000)
Debt issuance costs	-	(50,679)
Restricted contributions received	1,447,043	273,811
Net realized and unrealized gains on restricted investments	54,168	263,953
Net cash and cash equivalents used in financing activities	(5,043,789)	(6,517,915)
Net Increase in Cash and Cash Equivalents	4,417,267	13,442,457
Cash and Cash Equivalents - Beginning of year	17,594,905	4,152,448
Cash and Cash Equivalents - End of year	**$ 22,012,172**	**$ 17,594,905**
Supplemental Cash Flow Information		
Cash paid during the year for interest	$ 4,332,330	$ 4,235,296
Net change in property and equipment additions in accounts payable	(620,974)	1,205,831
Property and equipment obtained via capital lease	16,180,164	-

See notes to consolidated financial statements.

Note 1 - Nature of Business

Flagler Hospital, Inc. (the “Hospital”) operates a 335-bed acute care general hospital from an 80-acre site just south of the city limits of St. Augustine, Florida. Flagler Home Care, LLC (Home Care); Outpatient Surgery Center of St. Augustine, LLC (OSC); and Flagler Professional Health Services, Inc. (Professional Services) provide a variety of outpatient healthcare services to the surrounding community. Flagler Health Network, LLC (Health Network) was established to hold the investment in Home Care, which was formed in 2018, and Flagler Health Enterprise, LLC (Health Enterprise) was established to hold the investment in OSC, which was acquired during 2018 (see Note 15). Following the creation of Professional Services, the Hospital assigned its rights, title, interests, and obligations of the professional services, billing and management agreements, and the master lease with First Coast Heart and Vascular to Professional Services. Additionally, Professional Services acquired Flagler Care Center during 2018. Flagler Health Care Foundation (the “Foundation”) serves as a support organization for the Hospital. Flagler Health Services, Inc. (FHS) and Health Park Owners Association (HPOA) own and operate real property on and around the Hospital campus, including four medical office buildings.

The entities described above are collectively referred to as Flagler Health+ or the "System". All intercompany transactions and balances have been eliminated in the consolidated financial statements.

On September 1, 2015, Flagler Hospital, Inc. entered into an affiliation agreement with Baptist Health System, Inc. (Baptist), a Florida nonprofit corporation, and Southeast Georgia Health System, Inc. (SGHS), a Georgia nonprofit corporation, to form Coastal Community Health, a new Florida nonprofit corporation (Coastal). As a result of the agreement, Coastal became the sole corporate member of Flagler Hospital, Inc. The agreement provided for indefinite six-month withdrawal windows after each three-year period from the agreement closing date. If the Hospital were to withdraw after the first three-year withdrawal period, the Hospital would pay $3,000,000 as liquidated damages and, for a period of 12 months following its withdrawal, would be prohibited from affiliating with any other health system. On September 4, 2018, the Hospital notified Coastal and its other members of its intent to withdraw from the affiliation. The representatives of Baptist and SGHS on the Coastal board of directors accepted the Hospital's proposed withdrawal plan, which included a financial settlement that was not material to the consolidated financial statements. Effective November 30, 2018, the Hospital legally reorganized and was relieved of all ownership interests from Coastal.

During 2018, Home Care was established as a joint venture, with the System as the 52 percent owner. The System was determined to have a controlling financial interest in Home Care and, accordingly, consolidated the entity into the accompanying consolidated financial statements. As of September 30, 2019 and 2018, the total noncontrolling interest included within net assets without donor restrictions in the consolidated balance sheet amounted to approximately $247,000 and $295,000, respectively. The System also attributed excess of revenue under expense of approximately $48,000 and $295,000 included within the consolidated statement of operations to the noncontrolling interest during the years ended September 30, 2019 and 2018, respectively.

Note 2 - Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the System and all of its subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

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

Note 2 - Significant Accounting Policies (Continued)

Cash and Cash Equivalents

Cash and cash equivalents include cash and investments in highly liquid investments purchased with an original maturity of three months or less, excluding those amounts included in assets limited as to use. Cash balances held in the bank exceed the federal depository insurance limit. The System's cash is only insured up to the federal depository insurance limit.

Patient Accounts Receivable

Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges, reduced by explicit price concessions provided to third-party payors, discounts provided to qualifying individuals as part of our financial assistance policy, and implicit price concessions provided primarily to self-pay patients. Estimates for explicit price concessions are based on provider contracts, payment terms for relevant prospective payment systems, and historical experience adjusted for economic conditions and other trends affecting the System's ability to collect outstanding amounts.

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 System records significant implicit price concessions 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.

Supplies

Supplies, which consist of medical and surgical supplies and pharmaceutical products, are stated at the lower of cost or net realizable value, determined on a first-in, first-out basis.

Assets Limited as to Use and Investments

The System classifies its partnerships and debt and equity securities as trading securities. All debt and equity securities are required to be reported at fair value, principally based on quoted market prices, in the consolidated balance sheet. The fair value of partnerships is determined by the general partner using the latest available information at the valuation date. Investment income (including realized gains and losses on investments, unrealized gains and losses on trading securities, interest, and dividends) is included in excess of revenue over expenses unless such earnings are subject to donor-imposed restrictions.

Assets whose use is limited include (i) assets set aside by the board of trustees (the "Board") for future capital expenditures, (ii) assets held from donors that are restricted, and (iii) funds held by the bond trustee.

The System's investments are exposed to various risks, such as interest rate, market, and credit risk. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the value of investments, it is at least reasonably possible that changes in the value of investments in the near term could materially affect the amounts reported in the consolidated balance sheet and the consolidated statement of operations.

Property and Equipment

Property and equipment are recorded at cost. The straight-line method is used for computing depreciation. Assets are depreciated over their estimated useful lives. Costs of maintenance and repairs are charged to expense when incurred.

Note 2 - Significant Accounting Policies (Continued)

Impairment of Long-lived Assets

The System reviews the recoverability of long-lived assets when events or changes in circumstances occur that indicate the carrying value of the asset may not be recoverable. The assessment of possible impairment is based on the ability to recover the carrying value of the asset from the expected future pretax cash flows (undiscounted and without interest charges) of the related operations. If these cash flows are less than the carrying value of such asset, an impairment loss is recognized for the difference between estimated fair value and carrying value. The measurement of impairment requires management to make estimates of these cash flows related to long-lived assets, as well as other fair value determinations. There were no such impairment losses recorded during the years ended September 30, 2019 or 2018.

In addition to consideration of impairment upon the events or changes in circumstances described above, management regularly evaluates the remaining lives of its long-lived assets. If estimates are revised, the carrying value of affected assets is depreciated or amortized over the remaining lives.

Goodwill

The recorded amounts of goodwill from business combinations are based on management's best estimates of the fair values of assets acquired and liabilities assumed at the date of acquisition. Goodwill is not amortized, but rather is assessed at least on an annual basis for impairment. The System determined that there was no goodwill impairment for the years ended September 30, 2019 or 2018.

Other Assets

Other assets include long-term notes receivable, investment in joint ventures, deposits, receivables for liability recoveries, and definite-lived intangible assets. The majority of the net balance of definite-lived intangible assets includes a five-year physician noncompete agreement being amortized using the straight-line method.

Professional Liability Contingencies

The System accrues an estimate of the ultimate expense, including litigation and settlement expense, for incidents of potential improper professional service and other liability claims occurring during the year, as well as for those claims that have not been reported at year end.

Classification of Net Assets

Net assets of the System are classified based on the presence or absence of donor-imposed restrictions.

Net assets without donor restrictions: Net assets that are not subject to donor-imposed restrictions or for which the donor-imposed restrictions have expired or been fulfilled. Net assets in this category may be expended for any purpose in performing the primary objectives of the System.

Net assets with donor restrictions: Net assets subject to stipulations imposed by donors and grantors. Some donor restrictions are temporary in nature; those restrictions will be met by actions of the System or by the passage of time. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity.

Earnings, gains, and losses on donor-restricted net assets are classified as net assets without donor restrictions unless specifically restricted by the donor or by applicable state law.

Excess of Revenue Over Expenses

The consolidated statement of operations includes excess of revenue over expenses. Changes in net assets without donor restrictions, which are excluded from excess of revenue over expenses, consistent with industry practice, include contributions of long-lived assets (including assets acquired using contributions that by donor restriction were to be used for the purposes of acquiring such assets).

Note 2 - Significant Accounting Policies (Continued)

Revenue Recognition - Patient Service Revenue

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

Performance obligations are determined based on the nature of the services provided by the System. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. The System believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in our hospital receiving inpatient acute care services or patients receiving services in our outpatient centers or other clinical settings. The System measures the performance obligation from admission into the hospital, or the commencement of an outpatient services or other visit, to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge or completion of the outpatient services or other visit.

Because all of its performance obligations relate to contracts with a duration of less than one year, the System has elected to apply the optional exemption provided in Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 606-10-50-14-(a) and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

The System determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with the System's policy, and implicit price concessions provided to uninsured patients. The System determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. The System determines its estimate of implicit price concessions based on its historical collection experience with this class of patients.

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. The System also provides services to uninsured patients and offers those uninsured patients a discount, either by policy or law, from standard charges. The System estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. For the years ended September 30, 2019 and 2018, changes in the estimates of implicit price concessions, discounts, and contractual adjustments for performance obligations satisfied in prior years were not significant. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense.

Note 2 - Significant Accounting Policies (Continued)

Consistent with the System's mission, care is provided to patients regardless of their ability to pay. Therefore, the System has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts the System expects to collect based on its collection history with those patients.

Patients who meet the System's criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue. Charity care provided by the System, based on cost, was approximately $7,207,000 and $7,412,000 for the years ended September 30, 2019 and 2018, respectively. The cost of charity care was determined based on direct and indirect costs of providing services to the patients.

The System has elected the practical expedient allowed under FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the System's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, the System does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Donor-restricted Contributions

Unconditional promises to give cash and other assets to the System are reported at fair value on the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value on the date the gift is received. The gifts are reported as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statement of 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 contributions without donor restrictions in the accompanying financial statements.

Income Taxes

The Hospital and the Foundation are not-for-profit organizations and are exempt from tax under the provisions of Internal Revenue Code Section 501(c)(3). The remaining members of the System are for-profit subsidiaries and are subject to federal income tax on their earnings.

At September 30, 2019 and 2018, FHS had available net operating loss carryforwards for tax purposes of approximately $1,227,000 and $1,302,000, respectively, which expire through 2025, and, accordingly, no provision for income taxes has been recognized. Management believes the retained deficit of its other for-profit subsidiaries is not significant.

Note 2 - Significant Accounting Policies (Continued)

Change in Accounting Principles

Effective October 1, 2018, the System adopted Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, using a modified retrospective method of application to all contracts existing on October 1, 2018. The core principle of the guidance in ASU No. 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The adoption of ASU No. 2014-09 resulted in changes to the System’s presentation for disclosure of revenue primarily related to uninsured or underinsured patients. Prior to the adoption of ASU No. 2014-09, a significant portion of the System's provision for bad debts related to self-pay patients, as well as copays, coinsurance, and amounts and deductibles owed by patients with insurance. Under ASU No. 2014-09, the estimated uncollectible amounts due from these patients are generally considered implicit price concessions that are a direct reduction to operating revenue, with a corresponding material reduction in the amounts presented separately as provision for bad debts. For the year ended September 30, 2019, the System recorded approximately $16,759,000 of implicit price concessions as a direct reduction of net patient service revenue that would have been recorded as provision for bad debts prior to the adoption of ASU No. 2014-09. At September 30, 2019, the System recorded approximately $16,659,000 as a direct reduction of accounts receivable that would have been reflected as allowance for uncollectible accounts prior to the adoption of ASU No. 2014-09. The adoption of ASU No. 2014-09 also resulted in changes to the System's presentation and disclosure of customer contract assets and liabilities and the assessment of variable consideration under customer contracts, which are further discussed in Notes 3 and 4.

Effective for the year ended September 30, 2019, the System adopted ASU No. 2016-14, *Not-for-Profit Entities*. This standard requires net assets to be classified in two categories, net assets without donor restrictions and net assets with donor restrictions, rather than the three previous classifications. This standard also requires changes in the way certain information is aggregated and reported by the System, including disclosures of quantitative and qualitative information about the liquidity and availability of resources and the presentation of expenses by both functional and natural classification. The standard also clarifies the definition of management and general and prohibits certain expenses from being allocated out of management and general. As a result of the adoption of this standard, the financial information for the year ended September 30, 2018 has been restated to reclassify net assets of $2,197,908 previously reported as temporarily restricted net assets and net assets of $4,009,627 previously reported as permanently restricted net assets as net assets with donor restrictions. In addition, total program costs of $218,727,818, general and administrative costs of $47,291,964, and total fundraising costs of $0 previously reported for the year ended September 30, 2018 have been restated as $220,377,948, $46,639,478, and $310,973, respectively.

Note 2 - Significant Accounting Policies (Continued)

Upcoming Accounting Pronouncement

The Financial Accounting Standards Board issued ASU No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the System's year ending September 30, 2020 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented or the beginning of the year of adoption. The new lease standard is expected to have a significant effect on the System’s consolidated financial statements as a result of the leases for equipment and facilities classified as operating leases. The expected impact on the consolidated balance sheet is a significant increase in long-term assets and lease liabilities. The effects on the results of operations are not expected to be significant, as recognition and measurement of expenses and cash flows for leases will be substantially the same under the new standard.

Subsequent Events

The financial statements and related disclosures include evaluation of events up through and including January 21, 2020, which is the date the financial statements were available to be issued.

Note 3 - Patient Service Revenue

The System has agreements with third-party payors that provide payments at amounts less than established charges. A summary of the basis of the payment arrangements with major third-party payors follows:

- **Medicare** - Inpatient acute-care services and rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Outpatient services related to Medicare beneficiaries are reimbursed based on a prospectively determined amount per episode of care.

- **Medicaid** - Inpatient acute-care services rendered to Medicaid program beneficiaries are paid using an AP-DRG grouping reimbursement methodology. Outpatient services related to Medicaid beneficiaries are reimbursed on an established fee-for-service methodology. The System was designated a rural provider for Medicaid on July 1, 2017.

- **Other** - The System has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined per diem rates.

Cost report settlements result from the adjustment of interim payments to final reimbursement under the Medicare, Medicaid, and HMO programs that are subject to audit by fiscal intermediaries.

Note 3 - Patient Service Revenue (Continued)

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various healthcare entities have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in entities entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge the System's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon the System. In addition, the contracts the System has with commercial payors also provide for retroactive audit and review of claims.

Settlements with third-party payors for retroactive adjustments due to audits, reviews, or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor, and the System's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available) or as years are settled or are no longer subject to such audits, reviews, and investigations. Adjustments arising from a change in the transaction price were not significant in 2019 or 2018.

The System has determined that the nature, amount, timing, and uncertainty of revenue and cash flows are affected primarily by payor. The composition of net patient service revenue by primary payor for the years ended September 30, 2019 and 2018 is approximately as follows:

	2019	2018
Medicare	$ 150,068,000	$ 136,202,000
Medicaid	18,968,000	19,880,000
Commercial	99,581,000	95,683,000
Other	9,205,000	7,539,000
Self-pay	1,116,000	1,223,000
Total	$ 278,938,000	$ 260,527,000

Revenue from patients' deductibles and coinsurance is included in the categories presented above based on the primary payor. The System recognizes patient service revenue over time as patients simultaneously receive and consume benefits provided as care is administered.

Note 4 - Patient Accounts Receivable

Patient accounts receivable are based on the estimated transaction price for completed contracts, which total $34,260,395 at September 30, 2019. Prior to the adoption of ASU No. 2014-09, patient accounts receivable at September 30, 2018 were composed of $46,472,912 less allowances for uncollectible accounts of $15,920,147.

Note 4 - Patient Accounts Receivable (Continued)

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

	2019	2018
Medicare	40 %	39 %
Medicaid	7	8
Commercial	33	35
Other	10	8
Self-pay	10	10
Total	100 %	100 %

Note 5 - Assets Limited as to Use and Investments

The detail of board-designated assets limited as to use is summarized in the following schedule:

	2019	2018
Cash and cash equivalents	$ 3,257,587	$ 17,292,312
U.S. government obligations	11,641,732	6,945,268
Corporate bonds	14,608,887	16,696,023
Mutual funds	59,695,797	58,017,883
Limited partnerships	4,826,515	7,093,946
Interest receivable	115,472	145,618
Total	$ 94,145,990	$ 106,191,050

The detail of investments is summarized in the following schedule:

	2019	2018
Cash and cash equivalents	$ 155,474	$ 100,382
U.S. government obligations	2,950,563	1,982,330
Corporate bonds	3,771,660	3,754,237
Mutual funds	24,816,094	26,031,980
Limited partnerships	1,387,435	1,438,715
Interest receivable	31,763	39,247
Total	$ 33,112,989	$ 33,346,891

The uses of investments and assets limited as to use are as follows:

	2019	2018
Investments without restrictions	$ 33,112,989	$ 33,346,891
Assets limited as to use:		
By board for capital expenditures	86,676,395	83,074,311
Assets received from donors	7,041,540	6,207,535
Assets held by bond trustee	428,055	16,909,204
Total assets limited as to use	94,145,990	106,191,050
Total	$ 127,258,979	$ 139,537,941

Note 5 - Assets Limited as to Use and Investments (Continued)

Investment income, reported within nonoperating income in the consolidated statement of operations, for the years ended September 30, 2019 and 2018 is as follows:

	2019	2018
Interest and dividends	$ 4,597,026	$ 4,550,743
Realized losses and gains on sales of investments	2,986,428	2,614,329
Change in net unrealized gains and losses on investments	(2,748,981)	2,786,571
Total	$ 4,834,473	$ 9,951,643

Note 6 - Liquidity

The following reflects the System's financial assets as of September 30, 2019, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of the consolidated balance sheet date:

Cash and cash equivalents	$ 22,012,172
Patient accounts receivable	34,260,395
Third-party payor settlements	1,561,855
Investments and assets limited as to use	127,258,979
Other financial assets	7,083,147
Financial assets - At year end	192,176,548
Less those unavailable for general expenditures within one year due to:	
Contractual or donor-imposed restrictions:	
Restricted by donor with time or purpose restrictions	7,041,540
Held by bond trustee	428,055
Long-term assets	1,808,289
Board designations - For capital expenditures	86,676,395
Financial assets available to meet cash needs for general expenditures within one year	$ 96,222,269

The System has certain board-designated and donor-restricted assets limited as to use, which are more fully described in Note 5. These amounts are not available for general expenditure within the next year. However, the board-designated amounts could be made available, if necessary.

The System structures its financial assets to be available as its general expenditures, liabilities, and other obligations come due. As part of the System's liquidity management program, cash in excess of daily requirements is invested in short-term investments.

The System also realizes there could be unanticipated liquidity needs.

Note 7 - Property and Equipment

Property and equipment are summarized as follows:

	2019	2018	Depreciable Life - Years
Land and land improvements	$ 18,730,894	$ 18,835,779	5-25
Buildings and improvements	181,313,782	184,148,178	10-40
Equipment	195,031,995	203,446,546	3-5
Capital leases	16,180,164	-	20
Construction in progress	9,429,115	8,095,163	-
Total cost	420,685,950	414,525,666	
Accumulated depreciation	246,399,739	255,326,969	
Net property and equipment	$ 174,286,211	$ 159,198,697	

Depreciation expense for the years ended September 30, 2019 and 2018 was approximately $22,358,000 and $22,985,000, respectively. Construction in progress at September 30, 2019 and 2018 consists of construction and system renovation projects not yet completed. The System had construction commitments in the amount of approximately $12,000,000 as of September 30, 2019.

On November 15, 2018, the System entered into a transaction with an unrelated party (the "Lessor") in order to construct and develop various outpatient facilities. The project was developed on land that is owned by the System and was leased to the Lessor for a term of 76 years. Total rent under the lease agreement was approximately $500,000, which was payable upon execution of the lease. The System has classified the ground lease as an operating lease and has recorded the unearned lease income as deferred rent in the consolidated balance sheet, which will be recognized over the life of the lease on a straight-line basis.

Through the terms of a construction agency agreement, the System acted as the construction agent during the development of the facilities. The System paid for construction costs as they were incurred and was subsequently reimbursed by the Lessor up to a maximum allowance of $16,375,000 per the agency agreement. The System incurred costs of approximately $1 million in excess of the project allowance, which have been reflected as building improvements in the consolidated balance sheet. The Lessor reimbursed the System for all costs up to the project allowance limit prior to September 30, 2019.

The Lessor leased the constructed facilities to the System for an initial 20-year period ending on September 30, 2039. After the initial term, there are four separate, optional five-year renewal periods. The System has classified this transaction as a capital lease, which is discussed further in Note 8.

Note 8 - Long-term Debt

A summary of long-term debt at September 30, 2019 and 2018 is as follows:

	2019	2018
St. Johns County, Industrial Development Authority Hospital Revenue Bonds, Series 2012A, with a fixed interest rate of 1.869 percent	$ -	$ 3,000,000
St. Johns County, Industrial Development Authority Hospital Revenue Bonds, Series 2012B, with a fixed interest rate of 3.60 percent	12,000,000	12,000,000
2014 bank loan with a fixed interest rate of 3.42 percent	12,085,000	12,085,000
St. Johns County, Industrial Development Authority Hospital Revenue Bonds, Series 2017A, with a fixed rate of interest of 5 percent	32,575,000	32,575,000
St. Johns County, Industrial Development Authority Hospital Revenue and Refunding Bonds, Series 2017B, with a fixed rate of interest of 2.44 percent	64,540,000	67,885,000
2017C bank loan with fixed interest rate of 3.57 percent	3,430,000	3,630,000
Capital lease with implicit interest rate of 4.29 percent	16,180,164	-
Unamortized debt issuance costs	(1,247,567)	(1,327,471)
Long-term debt less unamortized debt issuance costs	139,562,597	129,847,529
Less current portion	7,397,648	6,545,000
Long-term portion	$ 132,164,949	$ 123,302,529

On April 4, 2012, the St. Johns County Industrial Development Authority issued $18,000,000 of Hospital Revenue Bonds (Series 2012A) and $12,000,000 of Hospital Revenue Bonds (Series 2012B). The proceeds of the Series 2012A and 2012B were used to reimburse the System for certain renovation projects; implementation of a new electronic medical record, clinical, and billing system; and other equipment. The Series 2012A and Series 2012B Bonds are "non-bank qualified." The Series 2012A Bonds matured in 2019, and the Series 2012B Bonds mature in 2022.

On October 29, 2014, the System borrowed $14,000,000 from a bank in the form of a commercial loan. The proceeds of the loan were applied towards the purchase of certain assets of an ambulatory surgery center located in the System's primary service area. The loan bears a fixed interest rate with varying annual principal payments through final maturity on October 1, 2024.

On September 28, 2017, the St. Johns County Industrial Development Authority issued $32,575,000 of Hospital Revenue Bonds (Series 2017A) and $71,400,000 of Hospital Revenue and Refunding Bonds (Series 2017B). The proceeds of the Series 2017A Bonds were used to reimburse the System for certain hospital facilities, improvements, renovations, equipment, fixtures, furnishings, and other routine capital expenditures. They also were used to fund certain outpatient facilities to be developed near World Golf Village, including land, buildings, furniture, fixtures, and equipment. The purpose of the Series 2017B Bonds is financing, refinancing, and reimbursing the cost of the acquisition, renovation, construction, equipping, and installation of certain healthcare facilities. As part of the 2017 bond issuance, both the Series 2010A and Series 2010B Bonds were paid in full on September 28, 2017. The Series 2017A Bonds mature in 2047, but are subject to mandatory sinking fund redemption beginning in 2033. The Series 2017B mature in 2032, but were subject to mandatory sinking fund redemption beginning in 2018.

On September 28, 2017, the System also borrowed $3,630,000 from a bank in the form of a commercial loan. The proceeds of the loan were applied towards the payoff of the derivative financial instrument. The loan requires varying annual principal repayments beginning in 2019 through final maturity on August 15, 2029.

Note 8 - Long-term Debt (Continued)

During 2019, the System entered into a capital lease, which is discussed further in Note 7. The first lease payment was due on October 1, 2019. The agreement requires monthly payments, including interest at an implicit rate of 4.29 percent. Payments required under the lease for the first year amount to $84,195 monthly, with a 2 percent increase effective each October 1.

The System's debt instruments (bonds and loans) are joint and several obligations of the Hospital and the Foundation, the two members of the "Obligated Group." Bonds issued by St. Johns Industrial Development Authority and the 2014 and 2017 loans are secured by a security interest in the Obligated Group's gross revenue and a mortgage on the main hospital campus. All such debt instruments are additionally secured by a security interest in certain fixtures and equipment until the maturity of the Series 2012A Bonds in 2019. The primary debt covenant for all debt instruments consists of a maximum annual debt service coverage ratio of 1.20, measured annually, and a minimum of 90 unrestricted days cash and investments on hand, measured semiannually, both as defined in the master indenture.

The balance of the above debt matures as follows:

Years Ending September 30	Amount
2020	$ 7,397,648
2021	7,534,699
2022	7,816,860
2023	7,671,037
2024	8,015,627
Thereafter	102,374,293
Total	$ 140,810,164

Future minimum lease payments on the capital lease obligations are summarized as follows:

Years Ending September 30	Amount
2020	$ 1,010,337
2021	1,030,544
2022	1,051,155
2023	1,072,178
2024	1,093,621
Thereafter	19,290,709
Total	24,548,544
Interest payments	(8,368,380)
Present value	$ 16,180,164

Note 9 - Net Assets with Donor Restrictions

Net assets that are restricted by donors consist of amounts held for future capital acquisitions and designated healthcare services. As of September 30, 2019 and 2018, restricted net assets that may be used subsequent to the passage of time or other stipulated activities total $2,977,340 and $2,197,908, respectively.

Net assets restricted by donors that are perpetual in nature at September 30, 2019 and 2018 are restricted to the following:

	2019	2018
Investments to be held in perpetuity, 6 percent of the value of the corpus is to be expended annually toward employee scholarships	$ 208,531	$ 208,531
Investments to be held in perpetuity	3,855,669	3,801,096
Total	$ 4,064,200	$ 4,009,627

FASB Accounting Standards Codification Subtopic 958-205, *Not-for-Profit Entities - Presentation of Financial Statements*, provides guidance on the net asset classification of donor-restricted endowment funds for not-for-profit organizations that are subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) and also requires enhanced disclosures about an organization's endowment funds and donor-restricted and board-designated endowment funds.

Pursuant to ASC 958-205, the System has interpreted UPMIFA, as adopted by Florida on July 1, 2012, as requiring the preservation of fair value of donor-restricted endowment gifts as of the gift date, absent explicit donor stipulations to the contrary. The System's endowment consists of three individual funds established for a variety of purposes. The endowments are all donor restricted and internally controlled. The System has no board-designated endowments. As required by relevant accounting literature, net assets associated with endowment funds are classified and reported based on the existence of donor-imposed restrictions. There are restrictions on the use of the related income of all endowments. The endowment investments have a target allocation of approximately 47.5 percent domestic equity, 12.5 percent international equity, 10.0 percent other assets, and 30.0 percent fixed-income investments.

The System classifies as net assets with perpetual donor restrictions the original value of gifts donated to the permanent endowment and the original value of subsequent gifts to the permanent endowment. During 2019, the permanent endowment increased by $54,573 as the result of additional perpetual contributions. There was no change in the permanent endowment amount during 2018.

Endowment funds consist of the following at September 30, 2019 and 2018:

	2019	2018
Permanently donor-restricted endowment funds	$ 4,064,200	$ 4,009,627

Note 10 - Commitments and Contingencies

Professional Liability

The System is involved in litigation arising from the ordinary course of business. Claims alleging malpractice have been asserted against the System and are currently in various stages of litigation. The System has maintained coverage during 2019 and 2018 with a self-insured retention of $2,000,000 per occurrence and an aggregate limit of $6,000,000, eroded at the amount of the indemnity payment and has no inner aggregate deductible.

Note 10 - Commitments and Contingencies (Continued)

The System also has secured excess liability coverage for these periods with limits of $30,000,000 per occurrence and $30,000,000 in the aggregate per policy period. Coverage under this, as well as the System's previous policies, is on a claims-made basis. The System has established a liability to estimate losses from reported claims and other incidents not reported during the current coverage period not covered by insurance. In the opinion of management, after consultation with legal counsel, these matters will be resolved within its insurance coverage and accruals without a material adverse effect to the System's financial position.

The estimated accrual for self-insured professional liability risks was approximately $14,956,000 and $11,665,000 at September 30, 2019 and 2018, respectively, and is included within other long-term liabilities in the accompanying consolidated balance sheet. The estimated insurance recovery related to professional liability risks was approximately $3,909,000 and $1,867,000 at September 30, 2019 and 2018, respectively, and is included within other long-term assets in the accompanying consolidated balance sheet. Operating expenses for malpractice insurance premiums and other professional liability expenses for the years ended September 30, 2019 and 2018 were approximately $3,432,000 and $3,763,000, respectively.

The System maintains a line-of-credit agreement in the amount of $2,000,000, which is restricted to the System's self-insurance program pursuant to Section 766.105(2)(c) of the Florida Statutes. The agreement matures on September 30, 2020. There were no draws on the line of credit as of September 30, 2019 or 2018.

Workers' Compensation

The System is self-insured with respect to employee workers' compensation claims at $550,000 self-insured retention per claim for fiscal years 2019 and 2018, with no aggregate limit.

The System has contracted with an insurance carrier to cover those claims in excess of these limits. The System has established a liability for reported incidents and a liability related to loss development based on estimates from its claims administrator. The estimated accrual for self-insured workers' compensation included in accrued expenses and other long-term liabilities is approximately $2,672,000 and $2,833,000 as of September 30, 2019 and 2018, respectively. At September 30, 2019 and 2018, insurance recoveries in the amount of approximately $1,710,000 and $1,401,000, respectively, were recorded in other assets.

Prior to becoming self-insured for workers' compensation, the System was a member of the Florida System Workers' Compensation Self-Insurance Trust Fund (the "Trust Fund"), a self-insurance risk management trust fund in which members jointly and severally agree to pay the obligations of the Trust Fund. As a prior member of the Trust Fund, the System is subject to assessments in the event that the total amount of premiums for a year in which it was a member is not sufficient to satisfy claims. Assessments that have been levied against the System by the Trust Fund have been reflected in the accompanying consolidated financial statements as of September 30, 2019 and 2018. Management is not aware of any potential future assessments as of September 30, 2019.

Health Insurance Claims

The System is self-insured with respect to employee health insurance claims covering up to $200,000 per claim. The System has contracted with an insurance carrier to cover claims in excess of the self-insurance retention amounts. The estimated accrual for self-insured health insurance claims included in accrued expenses and other current liabilities is approximately $1,119,000 and $1,465,000 as of September 30, 2019 and 2018, respectively.

Note 10 - Commitments and Contingencies (Continued)

Operating Leases

The System is obligated under various short-term operating leases for equipment and office space. Future minimum annual commitments under these operating leases are as follows:

Years Ending		Amount
2020	$	4,035,639
2021		2,230,399
2022		2,004,628
2023		409,783
2024		165,918
Thereafter		15,033
Total	$	8,861,400

Note 11 - Retirement Plan

The System has a noncontributory retirement plan covering substantially all employees. During 2019 and 2018, the System contributed 4 percent of the employees' total annual compensation plus an additional 3 percent for compensation in excess of $55,000.

Total retirement expense for the years ended September 30, 2019 and 2018 was approximately $2,980,000 and $2,912,000, respectively.

Note 12 - Transactions with Affiliated Organizations

On May 1, 2013, the System and certain community physicians formed First Coast Health Alliance, LLC (FCHA). FCHA is a physician hospital organization created to develop and operate a clinically integrated network of providers serving St. Johns County. The System owns 50 percent of FCHA and does have significant influence but not control over the partnership. The System has determined that the equity method of accounting is appropriate. The investment balance was $515,000 and $399,000 as of September 30, 2019 and 2018, respectively, and is included in other assets in the consolidated balance sheet. Effective June 4, 2013, the System committed to provide FCHA with a working capital line of credit for two years, not to exceed $1,750,000. The working capital line of credit converted to a note payable on July 1, 2015, with a repayment term of seven years, and with an interest rate equivalent to the System's current cost of capital. The outstanding balance on the note payable was approximately $350,000 and $919,000 as of September 30, 2019 and 2018, respectively, which is included in other assets in the consolidated balance sheet.

Note 13 - Functional Expenses

The System provides inpatient and outpatient healthcare services to patients within its geographical area. The consolidated financial statements report certain categories of expenses that are attributable to more than one program or supporting function; these expenses require an allocation on a reasonable basis that is consistently applied. Employee benefits are allocated based on the amount of salaries attributable to the various functional categories. The allocations of interest expense and depreciation and amortization are based on the ratio of total expenses by category before employee benefits, interest expense, and depreciation and amortization.

Note 13 - Functional Expenses (Continued)

Expenses related to providing these services for the years ended September 30, 2019 and 2018 are as follows:

	2019			
	Program Services	Management and General	Fundraising	Total
Salaries	$ 74,390,031	$ 13,651,355	$ -	$ 88,041,386
Supplies	57,295,364	565,647	-	57,861,011
Purchased services	22,634,738	23,262,574	-	45,897,312
Depreciation and amortization	17,573,431	4,750,230	34,668	22,358,329
Employee benefits	17,041,474	3,127,289	-	20,168,763
Professional services	21,292,100	1,774,039	-	23,066,139
Lease and rental	2,364,875	4,288,988	210,285	6,864,148
Insurance	3,539,425	872,172	-	4,411,597
Interest expense	3,240,965	876,057	6,393	4,123,415
Other	1,222,030	2,352,878	155,101	3,730,009
Indigent tax	3,034,882	-	-	3,034,882
Utilities	2,614,091	263,101	-	2,877,192
Total	$ 226,243,406	$ 55,784,330	$ 406,447	$ 282,434,183

	2018			
	Program Services	Management and General	Fundraising	Total
Salaries	$ 72,930,193	$ 12,827,256	$ -	$ 85,757,449
Supplies	52,478,539	723,914	-	53,202,453
Purchased services	21,545,940	16,964,461	-	38,510,401
Depreciation and amortization	18,892,790	4,062,622	29,196	22,984,608
Employee benefits	19,146,722	3,367,603	-	22,514,325
Professional services	17,311,054	1,499,277	-	18,810,331
Lease and rental	1,744,130	3,731,652	234,756	5,710,538
Insurance	3,869,620	747,147	-	4,616,767
Interest expense	4,012,902	862,917	6,201	4,882,020
Other	2,865,488	1,626,748	40,820	4,533,056
Indigent tax	3,011,992	-	-	3,011,992
Utilities	2,568,578	225,881	-	2,794,459
Total	$ 220,377,948	$ 46,639,478	$ 310,973	$ 267,328,399

The expense information shown in the tables above includes $1,399,230 and $1,308,617 of expenses that are reported within other nonoperating income in the accompanying consolidated statement of operations for the years ended September 30, 2019 and 2018, respectively.

Note 14 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following tables present information about the System's assets measured at fair value on a recurring basis at September 30, 2019 and 2018 and the valuation techniques used by the System to determine those fair values.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the System has the ability to access.

Note 14 - Fair Value Measurements (Continued)

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs, such as interest rates and yield curves, that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques, taking into account the characteristics of the asset.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The System's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

Investments that are measured at fair value using net asset value (NAV) per share (or its equivalent) as a practical expedient are not classified in the fair value hierarchy below:

	Assets Measured at Fair Value on a Recurring Basis at September 30, 2019			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2019
Assets				
Investments and assets limited as to use:				
Cash and cash equivalents	$ 3,413,061	$ -	$ -	$ 3,413,061
Interest receivable	147,235	-	-	147,235
U.S. government obligations	-	14,592,295	-	14,592,295
Corporate bonds	-	18,380,547	-	18,380,547
Mutual funds:				
Small/Mid U.S. equity	19,978,211	-	-	19,978,211
Global equity	12,713,173	-	-	12,713,173
Global fixed income	11,457,809	-	-	11,457,809
Large U.S. equity	40,362,698	-	-	40,362,698
Total	$ 88,072,187	$ 32,972,842	$ -	121,045,029
Investments measured at NAV - Real estate limited partnership				6,213,950
Total assets				$ 127,258,979

Note 14 - Fair Value Measurements (Continued)

	Assets Measured at Fair Value on a Recurring Basis at September 30, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2018
Assets				
Investments and assets limited as to use:				
Cash and cash equivalents	$ 17,392,694	$ -	$ -	$ 17,392,694
Interest receivable	184,865	-	-	184,865
U.S. government obligations	-	8,927,598	-	8,927,598
Corporate bonds	-	20,450,260	-	20,450,260
Mutual funds:				
Small/Mid U.S. equity	20,161,812	-	-	20,161,812
Global equity	11,968,122	-	-	11,968,122
Global fixed income	11,011,333	-	-	11,011,333
Large U.S equity	40,908,596	-	-	40,908,596
Total	$ 101,627,422	$ 29,377,858	$ -	131,005,280
Investments measured at NAV - Real estate limited partnership				8,532,661
Total assets				$ 139,537,941

The fair value of U.S. government obligations and corporate bonds at September 30, 2019 and 2018 was determined primarily based on Level 2 inputs. The System estimates the fair value of these investments using quoted prices for similar assets in active markets. The fair value of the assets was determined primarily based on quoted market prices from the investment custodians.

Investments in Entities that Calculate Net Asset Value per Share

The System holds shares in a real estate investment fund (the "Fund") at year end whereby the fair value of the investment held is estimated based on the net asset value per share (or its equivalent) of the Fund. The Fund's purpose is to actively manage a core portfolio of primarily equity real estate investments located in the United States.

The Fund's fair values are provided by third-party appraisers. Generally, each of the Fund's real property interests is appraised every quarter after the investment is made unless certain factors or economic conditions warrant an additional appraisal. Third-party debt not secured by a property is reviewed on a quarterly basis for any impact that debt may have on gross asset value. The Fund employs an independent valuation consultant to administer the Fund's valuation program, including assisting in the engagement and rotation of third-party appraisers, coordinating the quarterly appraisal process, and reviewing appraisals. The independent valuation consultant reviews the independent appraisals for reasonableness of assumptions, consistency of methodology, compliance with the engagement, and confirmation of value.

Note 14 - Fair Value Measurements (Continued)

At year end, the fair value, unfunded commitments, and redemption rules of those investments are as follows:

	Investments Held at September 30, 2019			
	Fair Value	Unfunded Commitments	Redemption Frequency, if Eligible	Redemption Notice Period
Real estate limited partnership	$ 6,213,950	$ -	Quarterly	60 days

	Investments Held at September 30, 2018			
	Fair Value	Unfunded Commitments	Redemption Frequency, if Eligible	Redemption Notice Period
Real estate limited partnership	$ 8,532,661	$ -	Quarterly	60 days

Note 15 - Acquisitions and Goodwill

Flagler Surgery Center

On October 30, 2014, the System acquired 100 percent of an ambulatory surgery center, now referred to as the Flagler Surgery Center (FSC), located in St. Augustine, Florida from St. Augustine Surgery Center, LLC. The results of FSC's operations have been included in the System's consolidated financial statements since that date. The goodwill of $10,019,271 at September 30, 2019 and 2018 arising from the acquisition relates to excess of the purchase price over the fair value of the surgery center assets and liabilities purchased.

Outpatient Surgery Center of St. Augustine, LLC

On December 1, 2017, through a securities purchase agreement, the System acquired the remaining 89.32 percent ownership interest in Outpatient Surgery Center of St. Augustine, LLC (OSC), a for-profit entity in which the System previously held a 10.68 percent ownership stake. Under the terms of the purchase agreement, the System paid $14,775,000 for the remaining interest. As a result of the transaction, the System is the sole corporate member of OSC. The results of OSC's operations have been included in the System's consolidated financial statements since that date. Pursuant to the purchase agreement, the System obtained title to certain components of OSC's working capital as of the acquisition date. The System recorded the acquired working capital at fair value, determining the fair value of assumed supplies to be $195,766 and the fair value of assumed equipment to be $158,901. The goodwill of $14,420,333 at September 30, 2019 and 2018 arising from the acquisition relates to the excess of the purchase price over the fair value of the assets purchased.

As of the same date, the System entered into a separate purchase agreement to acquire the land and real estate used in OSC's operations from the owners of the property. Under the terms of the agreement, the System paid $9,300,000 for the property. Through the use of a third-party appraisal, the System allocated approximately $7,300,000 of the purchase to building and approximately $2,000,000 to land.

Note 15 - Acquisitions and Goodwill (Continued)

The amount of operating revenue and increase in net assets without donor restrictions related to OSC included within the accompanying consolidated statement of operations during the year ended September 30, 2018 amounted to approximately $4,114,000 and $1,447,000, respectively. The System is required to disclose the unaudited pro forma financial statement that presents the combined results of operations of the System and the entities for the year ended September 30, 2018 as though the acquisition had occurred on October 1, 2016. The unaudited pro forma financial information for the year ended September 30, 2018 for operating revenue and excess of revenue over expense was approximately $270,795,000 and $14,508,000, respectively. The unaudited pro forma financial information for the year ended September 30, 2017 for operating revenue and excess of expense over revenue was approximately $232,216,000 and $(2,785,000), respectively. This pro forma financial information is not necessarily indicative of the results of the operations that would have occurred had the System and the entity constituted a single entity during those periods, nor is it indicative of future results.

Other

The remaining goodwill of $455,930 at September 30, 2019 and 2018 arose from additional acquisitions during 2018 that relate to the excess of the purchase price over the fair value of the assets and liabilities purchased.

Additional Information

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Independent Auditor's Report on Additional Information

To the Board of Trustees
Flagler Hospital, Inc. and Subsidiaries
dba Flagler Health+

We have audited the consolidated financial statements of Flagler Hospital, Inc. and Subsidiaries dba Flagler Health+ as of and for the year ended September 30, 2019 and have issued our report thereon dated January 21, 2020, which contained an unmodified opinion on those consolidated financial statements. Our audit was performed for the purpose of forming an opinion on the 2019 consolidated financial statements as a whole. The consolidating balance sheet as of September 30, 2019 and consolidating statement of operations for the year then ended are presented for the purpose of additional analysis rather than to present the financial position, results of operations, and cash flows of the individual companies and are 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 2019 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the 2019 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 2019 consolidated financial statements as a whole.

Plante & Moran, PLLC

January 21, 2020

Consolidating Balance Sheet

September 30, 2019

	Foundation	Hospital	Eliminating Entries	Obligated Group	Flagler Health Services	HPOA	Health Network	Home Care	Health Enterprise	OSC	Professional Services	Eliminating Entries	Total
Assets													
Current Assets													
Cash and cash equivalents	$ 51,448	$ 18,290,609	$ -	$ 18,342,057	$ 1,182,533	$ 8,517	$ -	$ 300,061	$ -	$ 1,185,758	$ 993,246	$ -	$ 22,012,172
Patient accounts receivable	-	30,364,575	-	30,364,575	25,835	-	-	815,470	-	624,177	2,430,338	-	34,260,395
Supplies	-	8,054,794	-	8,054,794	-	-	-	5,556	-	203,353	398,806	-	8,662,509
Due from affiliates	-	30,203,881	(61,106)	30,142,775	65,454	259	-	-	-	-	6,668	(30,215,156)	-
Third-party payor settlements	-	1,561,855	-	1,561,855	-	-	-	-	-	-	-	-	1,561,855
Prepaid expenses and other current assets	394,675	3,994,948	-	4,389,623	84,981	-	-	389,580	-	32,796	1,529,161	-	6,426,141
Total current assets	446,123	92,470,662	(61,106)	92,855,679	1,358,803	8,776	-	1,510,667	-	2,046,084	5,358,219	(30,215,156)	72,923,072
Assets Limited as to Use	7,041,542	87,104,448	-	94,145,990	-	-	-	-	-	-	-	-	94,145,990
Investments	33,112,989	-	-	33,112,989	-	-	-	-	-	-	-	-	33,112,989
Property and Equipment - Net	335,233	170,852,198	-	171,187,431	2,394,860	566,339	-	118,635	-	123,124	67,975	(172,153)	174,286,211
Goodwill	-	10,019,271	-	10,019,271	-	-	-	-	14,420,333	-	455,930	-	24,895,534
Other Assets	1,345,212	11,991,423	-	13,336,635	18,602	-	267,789	355,385	1,968,949	-	7,800	(2,236,738)	13,718,422
Total assets	**$ 42,281,099**	**$ 372,438,002**	**$ (61,106)**	**$ 414,657,995**	**$ 3,772,265**	**$ 575,115**	**$ 267,789**	**$ 1,984,687**	**$ 16,389,282**	**$ 2,169,208**	**$ 5,889,924**	**$ (32,624,047)**	**$ 413,082,218**
Liabilities and Net Assets													
Current Liabilities													
Accounts payable	$ -	$ 7,765,219	$ -	$ 7,765,219	$ (34,795)	$ -	$ -	$ 58,672	$ -	$ 113,912	$ 1,048,336	$ -	$ 8,951,344
Current portion of long-term debt	-	7,397,648	-	7,397,648	-	-	-	-	-	-	-	-	7,397,648
Accrued expenses and other current liabilities	162,358	12,851,344	(61,106)	12,952,596	136,044	10,105	385,000	1,411,035	13,775,000	86,348	14,656,924	(30,215,156)	13,197,896
Total current liabilities	162,358	28,014,211	(61,106)	28,115,463	101,249	10,105	385,000	1,469,707	13,775,000	200,260	15,705,260	(30,215,156)	29,546,888
Long-term Debt - Net of current portion	-	132,164,949	-	132,164,949	-	-	-	-	-	-	-	-	132,164,949
Other Liabilities													
Deferred rent	-	3,951,082	-	3,951,082	-	-	-	-	-	-	-	-	3,951,082
Other long-term liabilities	-	16,665,879	-	16,665,879	-	-	-	-	-	-	-	-	16,665,879
Total liabilities	162,358	180,796,121	(61,106)	180,897,373	101,249	10,105	385,000	1,469,707	13,775,000	200,260	15,705,260	(30,215,156)	182,328,798
Net Assets													
Without donor restrictions	35,077,201	191,641,881	-	226,719,082	3,671,016	565,010	(117,211)	514,980	2,614,282	1,968,948	(9,815,336)	(2,408,891)	223,711,880
With donor restrictions	7,041,540	-	-	7,041,540	-	-	-	-	-	-	-	-	7,041,540
Total net assets	42,118,741	191,641,881	-	233,760,622	3,671,016	565,010	(117,211)	514,980	2,614,282	1,968,948	(9,815,336)	(2,408,891)	230,753,420
Total liabilities and net assets	**$ 42,281,099**	**$ 372,438,002**	**$ (61,106)**	**$ 414,657,995**	**$ 3,772,265**	**$ 575,115**	**$ 267,789**	**$ 1,984,687**	**$ 16,389,282**	**$ 2,169,208**	**$ 5,889,924**	**$ (32,624,047)**	**$ 413,082,218**

Consolidating Statement of Operations

Year Ended September 30, 2019

	Foundation	Hospital	Eliminating Entries	Obligated Group	Flagler Health Services	HPOA	Health Network	Home Care	Health Enterprise	OSC	Professional Services	Eliminating Entries	Total
Unrestricted Revenue, Gains, and Other Support													
Net patient service revenue	$ -	$ 257,507,759	$ -	$ 257,507,759	$ -	$ -	$ -	$ 1,303,838	$ -	$ 4,894,228	$ 15,231,916	$ -	$ 278,937,741
Other operating revenue	-	5,050,964	(37,054)	5,013,910	1,820,607	55,617	-	-	-	409	81	(867,988)	6,022,636
Net assets released from restrictions	50,243	-	-	50,243	-	-	-	-	-	-	-	-	50,243
Total unrestricted revenue, gains, and other support	50,243	262,558,723	(37,054)	262,571,912	1,820,607	55,617	-	1,303,838	-	4,894,637	15,231,997	(867,988)	285,010,620
Expenses													
Salaries	-	84,092,226	-	84,092,226	444,749	-	-	634,089	-	778,515	1,644,361	-	87,593,940
Supplies	-	53,988,736	-	53,988,736	32,057	-	-	25,728	-	1,562,084	2,252,406	-	57,861,011
Purchased services	-	40,089,202	-	40,089,202	257,005	51,802	-	480,776	-	290,721	4,703,732	-	45,873,238
Depreciation and amortization	-	21,923,437	-	21,923,437	339,228	-	-	11,536	-	50,931	33,197	-	22,358,329
Employee benefits	-	19,153,355	-	19,153,355	107,210	-	-	159,004	-	214,743	534,451	-	20,168,763
Professional services	-	14,437,266	-	14,437,266	-	-	-	16,770	-	-	8,377,176	-	22,831,212
Lease and rental	-	3,279,053	-	3,279,053	69,650	-	-	27,324	-	381,966	3,763,857	(867,988)	6,653,862
Insurance	-	4,335,414	-	4,335,414	66,523	-	-	-	-	9,660	-	-	4,411,597
Interest expense	-	4,123,415	-	4,123,415	-	-	-	-	-	-	-	-	4,123,415
Other expenses	-	3,038,254	-	3,038,254	75,995	1,848	-	48,287	-	23,398	59,730	-	3,247,512
Indigent tax	-	3,034,882	-	3,034,882	-	-	-	-	-	-	-	-	3,034,882
Utilities	-	2,607,841	-	2,607,841	206,115	2,509	-	-	-	60,543	184	-	2,877,192
Total expenses	-	254,103,081	-	254,103,081	1,598,532	56,159	-	1,403,514	-	3,372,561	21,369,094	(867,988)	281,034,953
Operating Income (Loss)	50,243	8,455,642	(37,054)	8,468,831	222,075	(542)	-	(99,676)	-	1,522,076	(6,137,097)	-	3,975,667
Nonoperating Income (Expense)													
Investment income (loss)	1,239,770	3,594,703	-	4,834,473	-	-	(51,832)	-	1,522,077	-	-	(1,470,245)	4,834,473
Other nonoperating (expense) income	(466,406)	831,655	37,054	402,303	-	-	-	-	-	-	-	-	402,303
Total nonoperating income (expense)	773,364	4,426,358	37,054	5,236,776	-	-	(51,832)	-	1,522,077	-	-	(1,470,245)	5,236,776
Excess of Revenue Over (Under) Expenses	823,607	12,882,000	-	13,705,607	222,075	(542)	(51,832)	(99,676)	1,522,077	1,522,076	(6,137,097)	(1,470,245)	9,212,443
Transfer to Affiliate	-	-	-	-	-	-	-	-	-	(1,000,000)	-	1,000,000	-
Net Assets Released from Restrictions	616,963	-	-	616,963	-	-	-	-	-	-	-	-	616,963
Increase (Decrease) in Net Assets without Donor Restrictions	**$ 1,440,570**	**$ 12,882,000**	**$ -**	**$ 14,322,570**	**$ 222,075**	**$ (542)**	**$ (51,832)**	**$ (99,676)**	**$ 1,522,077**	**$ 522,076**	**$ (6,137,097)**	**$ (470,245)**	**$ 9,829,406**