POLK MEDICAL CENTER, INC.
ROME, GEORGIA

FINANCIAL STATEMENTS

for the years ended June 30, 2019 and 2018

CONTENTS

Draffin Tucker

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Polk Medical Center, Inc.
Rome, Georgia

Report on the Financial Statements

We have audited the accompanying financial statements of Polk Medical Center, Inc. (PMCI), which comprise the balance sheets as of June 30, 2019 and 2018, and the related statements of operations and 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.

Auditor's 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 auditor's 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 PMCI'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 PMCI'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.

Continued

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 Polk Medical Center, Inc. as of June 30, 2019 and 2018, and the results of its operations and changes in net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Changes in Accounting Principle

As discussed in Note 1 to the financial statements, PMCI adopted new accounting guidance, Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606).* Our opinion is not modified with respect to that matter.

As discussed in Note 1 to the financial statements, PMCI adopted new accounting guidance, FASB ASC ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities.* Our opinion is not modified with respect to that matter.

Draffin & Tucker, LLP
Albany, Georgia
October 28, 2019

POLK MEDICAL CENTER, INC.

BALANCE SHEETS
June 30, 2019 and 2018

	2019	2018
ASSETS		
Current assets:		
Cash and cash equivalents	$ 4,877,195	$ 6,380,212
Assets limited as to use, current portion	838,126	838,126
Patient accounts receivable, net	6,279,828	8,146,009
Supplies	311,879	298,048
Other current assets	1,954,938	2,053,080
Total current assets	14,261,966	17,715,475
Assets limited as to use:		
By board for capital improvements	38,629,519	21,513,064
Under indenture agreement - held by trustee	836,207	838,126
Less amount required to meet current obligations	838,126	838,126
Noncurrent assets limited as to use	38,627,600	21,513,064
Property, plant and equipment, net	24,629,973	27,389,056
Total assets	$ 77,519,539	$ 66,617,595

	2019	2018
LIABILITIES AND NET ASSETS		
Current liabilities:		
Current portion of long-term debt	$ 152,299	$ 152,299
Accounts payable	582,348	550,274
Accrued salary	230,064	187,526
Accrued benefits	833,732	800,234
Other accrued expenses	1,355,016	1,487,915
Estimated third-party payor settlements	1,624,000	1,265,000
Due to Floyd Healthcare Management, Inc.	1,672,120	1,360,209
Total current liabilities	6,449,579	5,803,457
Long-term debt, net of current portion	36,251,396	36,608,759
Total liabilities	42,700,975	42,412,216
Net assets without donor restrictions	34,818,564	24,205,379
Total liabilities and net assets	$ 77,519,539	$ 66,617,595

See auditor's report and notes to financial statements.

POLK MEDICAL CENTER, INC.

STATEMENTS OF OPERATIONS
AND CHANGES IN NET ASSETS
for the years ended June 30, 2019 and 2018

	2019	2018
Operating revenues:		
Net patient service revenue	$ 32,213,785	$ 33,057,454
Other operating revenue	11	92,336
Total operating revenues	32,213,796	33,149,790
Expenses:		
Operating expenses	20,222,508	21,101,750
Interest	1,423,907	1,428,071
Depreciation	2,843,083	2,848,319
Total expenses	24,489,498	25,378,140
Operating income	7,724,298	7,771,650
Nonoperating income:		
Investment income	2,056,559	480,536
Contributions	805,402	227,953
Total nonoperating income	2,861,961	708,489
Excess revenues	10,586,259	8,480,139
Contributions for capital improvement and expansion	26,926	-
Increase in net assets without donor restrictions	10,613,185	8,480,139
Net assets, beginning of year	24,205,379	15,725,240
Net assets, end of year	$ 34,818,564	$ 24,205,379

See auditor’s report and notes to financial statements.

POLK MEDICAL CENTER, INC.

STATEMENTS OF CASH FLOWS
for the years ended June 30, 2019 and 2018

	2019	2018
Cash flows from operating activities:		
Changes in net assets	$ 10,613,185	$ 8,480,139
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Proceeds from contributions for capital improvements and expansion	(26,926)	-
Depreciation and amortization	2,638,020	2,642,712
Unrealized gain on investment	(1,367,235)	(144,414)
Realized loss on investment	-	16,253
Changes in:		
Patient accounts receivable	1,866,181	(2,309,247)
Supplies	(13,831)	(60,902)
Other current assets	98,142	(1,513,259)
Accounts payable and accrued expenses	(24,789)	746,738
Due to Floyd Healthcare Management, Inc.	292,205	(101,138)
Estimated third-party payor settlements	359,000	553,260
Net cash provided by operating activities	14,433,952	8,310,142
Cash flows from investing activities:		
Purchase of property and equipment	(64,294)	(41,526)
Proceeds from sale of investments	836,271	834,157
Purchase of investments	(16,583,572)	(10,205,209)
Net cash used by investing activities	(15,811,595)	(9,412,578)
Cash flows from financing activities:		
Payments on long-term debt	(152,300)	(154,146)
Proceeds from the contributions for capital improvements and expansion	26,926	-
Net cash used by financing activities	(125,374)	(154,146)
Net decrease in cash and cash equivalents	(1,503,017)	(1,256,582)
Cash and cash equivalents, beginning of year	6,380,212	7,636,794
Cash and cash equivalents, end of year	$ 4,877,195	$ 6,380,212
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of capitalized interest	$ 1,629,000	$ 1,636,000

See auditor’s report and notes to financial statements.

1. Summary of Significant Accounting Policies

Organization

Polk Medical Center, Inc. (PMCI) is a Georgia not-for-profit corporation. On November 6, 2014, PMCI entered into a lease agreement with Cedartown-Polk County Hospital Authority (Cedartown-Polk Authority) to lease all of the assets associated with Polk Medical Center, a critical access hospital providing inpatient and outpatient services. This lease has an original 35-year term. Floyd Healthcare Management, Inc. (Corporation) is the sole member of PMCI.

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 investments in highly liquid debt instruments with an original maturity of three months or less.

Supplies

Supplies are stated at the lower of cost and net realizable value, using the first-in, first-out method.

Assets Limited As To Use

Assets limited as to use include assets set aside by the Board for future capital improvements, over which the Board retains control and may at its discretion subsequently use for other purposes, and assets held by trustees under indenture agreements. Amounts required to meet current liabilities of PMCI have been reclassified in the balance sheet at June 30, 2019 and 2018.

Assets limited as to use invested in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheet. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in excess revenues unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from excess revenues unless the investments are trading securities.

Continued

1. Summary of Significant Accounting Policies, Continued

Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed on the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation expense in the financial statements.

Gifts of long-lived assets such as land, buildings, or equipment are reported as increases in net assets without donor restrictions, and are excluded from excess revenues, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash and other assets that must be used to acquire long-lived assets are reported as increases in net assets with donor restrictions. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Impairment of Long-Lived Assets

PMCI evaluates on an ongoing basis the recoverability of its assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is required to be recognized if the carrying value of the asset exceeds the undiscounted future net cash flows associated with that asset. The impairment loss to be recognized is the amount by which the carrying value of the long-lived asset exceeds the asset's fair value. In most instances, the fair value is determined by discounted estimated future cash flows using an appropriate interest rate. PMCI has not recorded any impairment charges in the accompanying statements of operations and changes in net assets for the years ended June 30, 2019 and 2018.

Costs of Borrowing

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Deferred Financing Cost

Costs related to the issuance of the 2016 Revenue Certificates were deferred and are being amortized using the effective interest method over the life of the related debt. Debt issuance costs related to a recognized debt liability are presented in the balance sheets as a direct deduction from the carrying amount of the related debt liability.

Continued

1. Summary of Significant Accounting Policies, Continued

Net Assets

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

Net assets without donor restrictions – net assets available for use in general operations and not subject to donor imposed restrictions. The Board of Directors has discretionary control over these resources. Designated amounts represent those net assets that the Board has set aside for a particular purpose. All revenue not restricted by donors and donor restricted contributions whose restrictions are met in the same period in which they are received are accounted for in net assets without donor restrictions.

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

Donor Restricted Gifts

Unconditional promises to give cash and other assets to PMCI are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as increases in the appropriate categories of net assets in accordance with donor restrictions.

Net Patient Service Revenue

PMCI has agreements with third-party payors that provide for payments to PMCI at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the amount that reflects the consideration to which PMCI expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors, and others and includes variable consideration for retroactive revenue adjustments under reimbursement arrangements with third-party payors. Retroactive adjustments are included in the determination of the estimated transaction price and adjusted in future periods as settlements are determined.

Continued

1. Summary of Significant Accounting Policies, Continued

Charity Care

PMCI provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because PMCI does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenues.

Excess Revenues

The statement of operations and changes in net assets includes excess revenues as a performance indicator. Changes in net assets without donor restrictions which are excluded from the performance indicator, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purpose of acquiring such assets).

Risk Management

PMCI is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses and natural disasters. PMCI has purchased insurance to mitigate the risk of loss for these types of damages. See Notes 8 and 9 for more information.

Income Taxes

PMCI is a not-for-profit corporation that has been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code.

PMCI applies accounting policies that prescribe when to recognize and how to measure the financial statement effects of income tax positions taken or expected to be taken on its income tax returns. These rules require management to evaluate the likelihood that, upon examination by the relevant taxing jurisdictions, those income tax positions would be sustained. Based on that evaluation, PMCI only recognizes the maximum benefit of each income tax position that is more than 50% likely of being sustained. To the extent that all or a portion of the benefits of an income tax position are not recognized, a liability would be recognized for the unrecognized benefits, along with any interest and penalties that would result from disallowance of the position. Should any such penalties and interest be incurred, they would be recognized as operating expenses.

Based on the results of management’s evaluation, no liability is recognized in the accompanying balance sheet for unrecognized income tax positions. Further, no interest or penalties have been accrued or charged to expense as of June 30, 2019 and 2018 or for the years then ended. PMCI’s tax returns are subject to possible examination by the taxing authorities. For federal income tax purposes, the tax returns essentially remain open for possible examination for a period of three years after the respective filing deadlines of those returns.

Continued

1. Summary of Significant Accounting Policies, Continued

Fair Value Measurements

FASB ASC 820, *Fair Value Measurement and Disclosures* defines fair value as the amount that would be received for an asset or paid to transfer a liability (i.e., an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. FASB ASC 820 describes the following three levels of inputs that may be used:

- Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets and liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

- Level 2: Observable prices that are based on inputs not quoted on active markets but corroborated by market data.

- Level 3: Unobservable inputs when there is little or no market data available, thereby requiring an entity to develop its own assumptions. The fair value hierarchy gives the lowest priority to Level 3 inputs.

Recently Adopted Accounting Pronouncements

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities.* This comprehensive standard provides guidance on net asset classification and required disclosures on liquidity and availability of resources, requires expanded disclosure about expense and investment returns, and eliminates the requirement to present or disclose the indirect method reconciliation if using the direct method when presenting cash flows. The standard is effective for annual periods beginning after December 15, 2017. PMCI has adjusted the presentation of these financial statements for all periods presented, except for the disclosures around liquidity and availability of resources. Those disclosures have been presented for 2019 only, as allowed by ASU No. 2016-14.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is a new comprehensive revenue recognition standard. The core principle of the revenue model is that an entity recognizes 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. PMCI adopted ASU No. 2014-09 on July 1, 2018 using the full retrospective method of transition with practical expedients in FASB ASC 606-10-65-1(f) with no significant impact. PMCI performed an analysis of revenue streams and transactions under ASU No. 2014-09. In particular, for net patient service revenue, PMCI performed an analysis into the application of the portfolio approach as a

Continued

1. Summary of Significant Accounting Policies, Continued

Recently Adopted Accounting Pronouncements, Continued

practical expedient to group patient contracts with similar characteristics, such that revenue for a given portfolio would not be materially different than if it were evaluated on a contract-by-contract basis. Upon adoption, the majority of what was previously classified as provision for bad debts (representing approximately $22 million for the year ended June 30, 2018) and presented as a reduction to net patient service revenue on the statements of operations is now treated as a price concession that reduces the transaction price, which is reported as net patient service revenue. Changes in credit issues not assessed at the date of service, are recognized as bad debt expense and included as a component of operating expenses on the statement of operations. The new standard also requires enhanced disclosures related to the disaggregation of revenue and significant judgments made in measurement and recognition. The adoption of this guidance did not materially impact total operating revenues, excess revenues, or net assets.

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958) Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made.* The update assists entities in determining when a transaction should be accounted for as a contribution or as an exchange transaction and provides additional guidance about how to determine whether a contribution is conditional. PMCI adopted the new guidance for the year ending June 30, 2019 and adoption did not have a material impact on the financial statements.

Accounting Pronouncements Not Yet Adopted

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. The new guidance requires equity investments (except those accounted for under the equity method or those that result in consolidation) to be measured at fair value, with changes in fair value recognized in net income; simplifies the impairment assessment of equity investments without readily determinable fair values; and amends certain disclosure requirements associated with the fair value of financial instruments. The standard is effective for annual periods beginning after December 15, 2018. PMCI expects to adopt the new guidance for the year ending December 31, 2019 and is continuing to evaluate the impact the guidance will have on the financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which is a new comprehensive lease accounting model. The new standard clarifies the definition of a lease and requires lessees to recognize right-of-use assets and related lease liabilities for all leases with terms greater than twelve months. The new guidance, including subsequent amendments, is effective for PMCI as of July 1, 2019. PMCI is continuing to evaluate the impact the guidance will have on the financial statements.

Continued

1. Summary of Significant Accounting Policies, Continued

Accounting Pronouncements Not Yet Adopted, Continued

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows – Restricted Cash*, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The provisions of ASU 2016-18 are effective for annual periods beginning after December 15, 2018. PMCI is continuing to evaluate the impact the guidance will have on the financial statements.

Prior Year Reclassification

Certain reclassifications have been made to the fiscal year 2018 financial statements to conform to the fiscal year 2019 presentation. These reclassifications had no impact on the change in net assets in the accompanying financial statements.

Subsequent Events

In preparing these financial statements, PMCI has evaluated events and transactions for potential recognition or disclosure through October 28, 2019, the date the financial statements were issued.

2. Net Patient Service Revenue

Net patient service revenue is reported at the amount that reflects the consideration to which PMCI 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 includes variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, PMCI bills the patients and third-party payors several days after the services are performed and/or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

Continued

2. Net Patient Service Revenue, Continued

Performance obligations are determined based on the nature of the services provided by PMCI. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. PMCI 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 receiving inpatient acute care services. PMCI measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. These services are considered to be a single performance obligation and have a duration of less than one year. Revenue for performance obligations satisfied at a point in time is recognized when services are provided and PMCI does not believe it is required to provide additional services to the patient.

Because all of its performance obligations relate to contracts with a duration of less than one year, PMCI has elected to apply the optional exemption provided in FASB 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.

PMCI is utilizing the portfolio approach practical expedient in ASC 606 for contracts related to net patient service revenue. PMCI accounts for the contracts within each portfolio as a collective group, rather than individual contracts, based on the payment pattern expected in each portfolio category and the similar nature and characteristics of the patients within each portfolio. As a result, PMCI has concluded that revenue for a given portfolio would not be materially different than if accounting for revenue on a contract-by-contract basis.

PMCI has arrangements with third-party payors that provide for payments to PMCI at amounts different from its established rates. For uninsured patients that do not qualify for charity care, PMCI recognizes revenue on the basis of its standard rates, subject to certain discounts and implicit price concessions as determined by PMCI. PMCI determines the transaction price based on standard charges for services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with PMCI's policy, and implicit price concessions provided to uninsured patients. Implicit price concessions represent the difference between amounts billed and the estimated consideration PMCI expects to receive from patients, which are determined based on historical collection experience, current market conditions, and other factors. PMCI determines its estimates of contractual adjustments and discounts based on contractual agreements, discount policies, and historical experience.

Continued

2. Net Patient Service Revenue, Continued

Agreements with third-party payors typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payors follows:

- Medicare

  PMCI has been granted Critical Access Hospital (CAH) designation by the Medicare Program. The CAH designation places certain restrictions on daily acute care inpatient census and an annual, average length of stay of acute care inpatients. Inpatient acute care and outpatient services rendered to Medicare program beneficiaries are paid based on a cost reimbursement methodology.

  PMCI is paid for certain cost reimbursable items at a tentative rate, with final settlement determined after submission of annual cost reports by PMCI and audits thereof by the Medicare Administrative Contractor (MAC). PMCI’s classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with PMCI. PMCI’s Medicare cost reports have been audited by the MAC through June 30, 2016.

- Medicaid

  Inpatient acute care services are paid at prospectively determined rates per discharge based on clinical, diagnostic and other factors. Outpatient services are paid based upon cost reimbursement methodologies. PMCI is paid for certain cost reimbursable items at a tentative rate, with final settlement determined after submission of annual cost reports by PMCI and audits thereof by the Medicaid fiscal intermediary. PMCI’s Medicaid cost reports have been audited by the Medicaid fiscal intermediary through June 30, 2015.

  PMCI has also entered into contracts with certain managed care organizations to receive reimbursement for providing services to selected enrolled Medicaid beneficiaries. Payment arrangements with these managed care organizations consist primarily of prospectively determined rates per discharge, discounts from established charges, or prospectively determined per diems.

  Long-term care services are reimbursed by the Medicaid program based on a prospectively determined per diem. The per diem is determined by the facility's historical allowable operating costs adjusted for certain incentives and inflation factors.

  PMCI participates in the Georgia Indigent Care Trust Fund (ICTF) Program. PMCI receives ICTF payments for treating a disproportionate number of Medicaid and other indigent patients. ICTF payments are based on PMCI’s estimated uncompensated cost of services to Medicaid and uninsured patients. The amount of ICTF payments recognized in net patient service revenue was approximately $1,600,000 and $1,600,000 for the years ended June 30, 2019 and 2018, respectively.

Continued

2. Net Patient Service Revenue, Continued

- Medicaid, Continued

  The Medicare, Medicaid and SCHIP Benefits Improvement and Protection Act of 2000 (BIPA) provides for payment adjustments to certain facilities based on the Medicaid Upper Payment Limit (UPL). The UPL payment adjustments are based on a measure of the difference between Medicaid payments and the amount that could be paid based on Medicare payment principles. The net amount of UPL payment adjustments recognized in net patient service revenue was approximately $80,000 and $130,000 for the years ended June 30, 2019 and 2018, respectively.

- Other Arrangements

  Payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations provide for payment using prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

- Uninsured Patients

  PMCI has a Financial Assistance Policy (FAP) in accordance with Internal Revenue Code Section 501(r). Based on the FAP, following a determination of financial assistance eligibility, an individual will not be charged more than the Amounts Generally Billed (AGB) for emergency or other medical care provided to individuals with insurance covering that care. AGB is calculated by reviewing claims that have been paid in full (including deductibles and coinsurance paid by the patient) to PMCI for medically necessary care by Medicare and private health insurers during a 12-month look-back period.

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 health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge PMCI'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 PMCI. In addition, the contracts PMCI has with commercial payors also provide for retroactive audit and review of claims.

Continued

2. Net Patient Service Revenue, Continued

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 PMCI'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.

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. PMCI also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. PMCI 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. Adjustments arising from a change in the transaction price were not significant for the years ending June 30, 2019 and 2018. 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. Bad debt expense for the years ended June 30, 2019 and 2018 was not significant.

Consistent with PMCI's mission, care is provided to patients regardless of their ability to pay. Therefore, PMCI has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles).

Patients who meet PMCI'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.

Continued

2. Net Patient Service Revenue, Continued

Net patient service revenue by major payor source for the years ended June 30, 2019 and 2018 is as follows:

	2019	2018
Medicare	$ 18,764,156	$ 16,528,572
Medicaid	1,944,433	3,371,230
Third-party payors	8,641,979	11,753,472
Self-pay	2,863,217	1,404,180
Net patient service revenue	$ 32,213,785	$ 33,057,454

Net patient service revenue by facility, line of business, and timing of revenue recognition for the years ended June 30, 2019 and 2018 is as follows:

	Net Patient Service Revenue for the years ended June 30	
	2019	2018
Hospital	$ 32,213,785	$ 33,057,454
Timing of revenue and recognition:		
Services transferred over time	$ 32,213,785	$ 33,057,454

Hospital net patient service revenue includes a variety of services mainly covering inpatient acute care services requiring overnight stays, outpatient procedures that require anesthesia or use of PMCI's diagnostic and surgical equipment, and emergency care services. Performance obligations for the hospital's patient services are satisfied over time as the patient simultaneously receives and consumes the benefits PMCI performs. Requirements to recognize revenue for inpatient services are generally satisfied over periods that average approximately five days and for outpatient services are generally satisfied over a period of less than one day.

Continued

2. Net Patient Service Revenue, Continued

PMCI 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 PMCI'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, PMCI 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.

PMCI has applied the practical expedient provided by FASB ASC 340-40-25-4 and all incremental customer contract acquisition costs are expensed as they are incurred as the amortization period of the asset that PMCI otherwise would have recognized is one year or less in duration.

3. Uncompensated Services

PMCI was compensated for services at amounts less than its established rates. Net patient service revenue includes amounts, representing the transaction price, based on standard charges reduced by variable considerations such as contractual adjustments, discounts, and implicit price concessions. The charges for these uncompensated services for 2019 and 2018 were approximately $99,200,000 and $84,100,000, respectively.

Uncompensated care includes charity and indigent care services of approximately $5,500,000 and $5,400,000 in 2019 and 2018, respectively. Charity and indigent care services provided to Polk County residents in 2019 and 2018 were approximately $4,600,000 and $4,100,000, respectively. The cost of charity and indigent care services provided during 2019 and 2018 was approximately $1,000,000 and $1,000,000, respectively computed by applying a total cost factor to the charges foregone.

Continued

3. Uncompensated Services, Continued

The following is a summary of uncompensated charges and a reconciliation of gross patient charges to net patient service revenue for 2019 and 2018:

	2019	2018
Gross patient charges	$ 131,377,133	$ 117,152,897
Uncompensated charges:		
Charity and indigent care	5,501,984	5,424,179
Medicare	25,555,032	22,950,007
Medicaid	26,624,788	23,245,138
Other third-party payors	16,132,082	10,598,821
Price concessions	25,349,462	21,877,298
Total uncompensated charges	99,163,348	84,095,443
Net patient service revenue	$ 32,213,785	$ 33,057,454

4. Concentration of Credit Risk

PMCI grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The mix of net receivables from patients and third-party payors was as follows at June 30, 2019 and 2018:

	2019	2018
Medicare	38%	37%
Medicaid	6%	4%
Other third-party payors	56%	59%
Total	100%	100%

PMCI maintains deposits with financial institutions which exceed the Federal Depository insurance limits. At June 30, 2019, management believes the credit risk associated with these deposits is minimal.

Continued

5. Assets Limited As To Use

The composition of assets limited as to use as of June 30, 2019 and 2018 is set forth in the following table. Assets limited as to use are trading securities.

	2019	2018
Assets limited as to use:		
By board for capital improvements:		
Cash and cash equivalents	$ 9,557	$ 2,004
Mutual funds - equity	10,631,471	6,454,883
Mutual funds - fixed income	16,037,127	8,697,344
Mutual funds - international	5,519,063	3,279,039
Mutual funds - real estate	1,511,731	913,561
US government index fund	4,920,570	2,166,233
	38,629,519	21,513,064
Under indenture agreement - held by trustee:		
Cash and cash equivalents	836,207	838,126
Total assets limited as to use	$ 39,465,726	$ 22,351,190

Investment income and gains and losses for assets limited as to use and cash and cash equivalents, are comprised of the following for the years ending June 30, 2019 and 2018:

	2019	2018
Income:		
Interest and dividend income	$ 689,324	$ 352,375
Unrealized gain on trading securities	1,367,235	144,414
Realized loss on trading securities	-	(16,253)
Total income less investment expenses	$ 2,056,559	$ 480,536

PMCI’s investments are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying financial statements.

Continued

6. Property, Plant and Equipment

A summary of property, plant and equipment at June 30, 2019 and 2018 follows:

	2019	2018
Land	$ 838,635	$ 838,635
Land improvements	50,508	50,509
Buildings	28,399,491	28,399,491
Fixed equipment	42,135	17,458
Major movable equipment	11,809,649	11,587,329
Building under capital lease	3,072,000	3,072,000
	44,212,418	43,965,422
Less accumulated depreciation	19,582,445	16,576,366
Construction-in-progress	-	-
Property, plant and equipment, net	$ 24,629,973	$ 27,389,056

Depreciation expense for the years ended June 30, 2019 and 2018 amounted to approximately $2,800,000 and $2,800,000, respectively. Accumulated amortization for a building under a capital lease obligation was $576,000 for 2019 and $422,000 for 2018.

7. Long-Term Debt

Long-term debt for the years ended June 30, 2019 and 2018 follows:

	2019	2018
Revenue certificates, PMCI Series 2016 payable in installments ranging from $35,000 to $5,515,000 each July 1, until 2039. The certificates are guaranteed by the gross revenues of Floyd Healthcare Management, Inc., the Hospital Authority of Floyd County and Polk Medical Center, Inc. The certificates bear interest rates per annum ranging from 3.125% to 5.00%.	$ 30,245,000	$ 30,325,000

Continued

7. Long-Term Debt, Continued

	2019	2018
Capital lease obligation with an interest rate of 3.99% and monthly payments ranging from $14,798 to $25,193.	$ 2,835,297	$ 2,907,597
Total long-term debt	33,080,297	33,232,597
Unamortized bond premium	3,599,184	3,821,265
Less: unamortized bond issuance costs	275,786	292,804
Less: current maturities of long-term debt	152,299	152,299
Long-term debt, net of current maturities	$ 36,251,396	$ 36,608,759

Scheduled principal repayments on long-term debt and payments on capital lease obligations for the next five years are as follows:

	Long-term Debt	Capital Lease Obligation
2020	$ 80,000	$ 192,631
2021	70,000	198,410
2022	80,000	204,362
2023	75,000	210,494
2024	65,000	216,808
Thereafter	29,875,000	2,935,215
	30,245,000	3,957,920
Less amount representing interest under capital lease obligation	-	1,122,623
Total	$ 30,245,000	$ 2,835,297

Revenue Anticipation Certificates, PMCI Series 2016 were issued to (i) refund the $35 million Bridge Loan Agreement, (ii) finance certain renovation projects; and (iii) pay costs of issuance of the PMCI Series 2016 Certificates. PMCI, the Hospital Authority of Floyd County, and the Corporation are members of the Obligated Group of the Revenue Anticipation Certificates, PMCI Series 2016.

Under the terms of the PMCI Series 2016 indentures, PMCI is required to maintain certain deposits with a trustee. Such deposits are included with assets limited as to use. The indentures also place limits on the incurrence of additional borrowings and require that PMCI satisfy certain measures of financial performance as long as the Certificates are outstanding. In the opinion of management, all measures of financial performance have been satisfied.

Continued

7. Long-Term Debt, Continued

Capital Lease Obligation

In 2016, PMCI entered into a capital lease agreement with the Corporation under which PMCI leases space in a medical office building. The lease term ends in September 2026, with three five-year extensions.

8. Employee Health Insurance

PMCI is included in the Corporation's employee health self-insurance program. The Corporation has a self-insurance program for employee health insurance under which a third-party administrator processes and pays claims. The Corporation reimburses the third-party administrator monthly for claims incurred and paid to other providers. The charges, less any deductibles and coinsurance for covered services provided to employees by the Corporation, are written off against gross patient service revenue. In addition, the Corporation has entered into a loss financing agreement with ten Georgia hospitals through a program developed by Georgia ADS, LLC. The program is designed to provide for the financing and payment of covered claims between $150 thousand and $500 thousand. The program also buys a reinsurance policy to cover claims reaching $1 million. Further, the Corporation purchased additional insurance to cover claims up to $2 million. Under this self-insurance program, PMCI expensed from allocations of the Corporation approximately $1,574,000 and $1,269,000 for the years ended June 30, 2019 and 2018, respectively.

9. Malpractice Insurance

PMCI is covered by a claims-made general and professional liability insurance policy with a specified deductible of $50,000 per incident and excess coverage on a claims-made basis. Liability limits related to this policy in 2019 are $1 million per occurrence and $3 million in aggregate. In addition, PMCI is covered by the Corporation's umbrella policy that covers malpractice claims up to $20 million in aggregate. PMCI uses a third-party administrator to review and analyze incidents that may result in a claim against PMCI. In conjunction with the third-party administrator, incidents are assigned reserve amounts for the ultimate liability that may result from an asserted claim.

Various claims and assertions have been made against PMCI in its normal course of providing services. In addition, other claims may be asserted arising from services provided to patients in the past. In the opinion of management, adequate provision has been made for losses which may occur from such asserted and unasserted claims that are not covered by liability insurance.

Continued

10. Commitments and Contingencies

Litigation

PMCI is involved in litigation arising in the course of business. Pursuant to the Lease described in Note 1, all liabilities resulting from litigation not covered under Polk's insurance policy have been assumed by the Corporation. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on PMCI's future financial position or results from operations.

Compliance Plan

The healthcare industry has been subjected to increased scrutiny from governmental agencies at both the federal and state level with respect to compliance with regulations. Areas of noncompliance identified at the national level include Medicare and Medicaid, Internal Revenue Service, and other regulations governing the healthcare industry. In addition, the Reform Legislation includes provisions aimed at reducing fraud, waste, and abuse in the healthcare industry. These provisions allocate significant additional resources to federal enforcement agencies and expand the use of private contractors to recover potentially inappropriate Medicare and Medicaid payments. PMCI has implemented a compliance plan focusing on such issues. There can be no assurance that PMCI will not be subjected to future investigations with accompanying monetary damages.

Operating Leases

PMCI leases various equipment and facilities under operating leases. Total rental expense in 2019 and 2018 for all operating leases was approximately $69,000 and $75,000, respectively.

Health Care Reform

There has been increasing pressure on Congress and some state legislatures to control and reduce the cost of healthcare at the national and the state levels. Legislation has been passed that includes cost controls on healthcare providers, insurance market reforms, delivery system reforms and various individual and business mandates among other provisions. The costs of these provisions are and will be funded in part by reductions in payments by government programs, including Medicare and Medicaid. There can be no assurance that these changes will not adversely affect PMCI.

Continued

11. Functional Expenses

PMCI provides general health care services to residents in Northwest Georgia. Expenses related to providing these services in 2019 are as follows:

	Patient Care Services	General and Administrative	Total
Salaries and wages	$ 9,076,963	$ 1,222,473	$ 10,299,436
Employee health and welfare	3,110,928	71,902	3,182,830
Professional fees	81,781	270,611	352,392
Supplies and other	4,210,404	2,177,446	6,387,850
Depreciation	2,462,253	380,830	2,843,083
Interest	1,208,547	215,360	1,423,907
Total	$ 20,150,876	$ 4,338,622	$ 24,489,498

Expenses related to providing these services in 2018 are as follows:

	Patient Care Services	General and Administrative	Total
Salaries and wages	$ 8,873,551	$ 1,169,407	$ 10,042,958
Employee health and welfare	3,028,776	189,134	3,217,910
Professional fees	38,138	271,776	309,914
Supplies and other	3,754,448	3,776,520	7,530,968
Depreciation	2,450,834	397,485	2,848,319
Interest	1,209,892	218,179	1,428,071
Total	$ 19,355,639	$ 6,022,501	$ 25,378,140

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

12. Contribution to City of Cedartown

PMCI agreed to make an annual contribution to the City of Cedartown in relation to the construction of new water and sewer infrastructure for the new hospital. Pursuant to the agreement, PMCI will make payments for 20 years. PMCI made a contribution in the amount of $310,000 during 2019 and 2018.

Continued

13. Related Party Transactions

PMCI is a wholly owned member of the Corporation and the Corporation makes all payments to employees and vendors on behalf of PMCI. PMCI reimburses the Corporation for these expenditures.

In addition, on October 1, 2015, PMCI entered into a capital lease with the Corporation to lease a portion of the Medical Office Building to PMCI. See Note 7 for a description of the capital lease. PMCI made payments to the Corporation of approximately $187,020 and $181,573 in fiscal years 2019 and 2018, respectively.

14. Fair Value of Financial Instruments

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

- *Cash and cash equivalents, accounts payable, accrued expenses, and estimated third-party payor settlements*: The carrying amount reported in the balance sheet approximates its fair value due to the short-term nature of these instruments.

- *Assets limited as to use*: Amounts reported in the balance sheet are at fair value. See Note 15 for fair value measurement disclosures.

- *Long-term debt*: The fair value of PMCI's long-term debt is estimated based on the quoted market value for same or similar debt instruments. Based on inputs used in determining the estimated fair value, PMCI's long-term debt would be classified as Level 2 in the fair value hierarchy.

The carrying amounts and fair values of PMCI's long-term debt at June 30, 2019 and 2018 are as follows:

	2019		2018	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt	$ 33,844,184	$ 34,080,369	$ 34,146,265	$ 33,055,969

Continued

15. Fair Value Measurement

Fair value of assets measured on a recurring basis at June 30, 2019 and 2018 are as follows:

	Assets at Fair Value as of June 30, 2019			
	(Level 1)	(Level 2)	(Level 3)	Total
Assets:				
Capital improvements:				
Cash and cash equivalents	$ 9,557	$ -	$ -	$ 9,557
Mutual funds - equity	10,631,471	-	-	10,631,471
Mutual funds - fixed income	16,037,127	-	-	16,037,127
Mutual funds - international	5,519,063	-	-	5,519,063
Mutual funds - real estate	1,511,731	-	-	1,511,731
US government index fund	4,920,570	-	-	4,920,570
Under indenture agreement:				
Cash and cash equivalents	836,207	-	-	836,207
Total assets	$ 39,465,726	$ -	$ -	$ 39,465,726

	Assets at Fair Value as of June 30, 2018			
	(Level 1)	(Level 2)	(Level 3)	Total
Assets:				
Capital improvements:				
Cash and cash equivalents	$ 2,004	$ -	$ -	$ 2,004
Mutual funds - equity	6,454,883	-	-	6,454,883
Mutual funds - fixed income	8,697,344	-	-	8,697,344
Mutual funds - international	3,279,039	-	-	3,279,039
Mutual funds- real estate	913,561	-	-	913,561
US government index fund	2,166,233	-	-	2,166,233
Under indenture agreement:				
Cash and cash equivalents	838,126	-	-	838,126
Total assets	$ 22,351,190	$ -	$ -	$ 22,351,190

Continued

15. Fair Value Measurement, Continued

Financial assets valued using Level 1 inputs are based on unadjusted quoted market prices within active markets. Valuation techniques utilized to determine fair value are consistently applied. All assets have been valued using a market approach.

16. Defined Contribution Plan

PMCI participates in the Corporation's 401(k) retirement plan. The plan is a defined contribution 401(k) profit sharing plan covering full-time employees over the age of eighteen who are not participating in the defined benefit pension plan. Employees may immediately contribute between 1% and 25% of their salary, subject to the maximum dollar limit allowed by the IRS. The Corporation will match 100% of the employee's contributions up to 3% of their salary plus 50% of the next 2% of the employee's contributions for all participating employees with at least one year of service and over 1,000 hours worked in a calendar year.

17. Liquidity and Availability

As of June 30, 2019, PMCI has a working capital (current assets minus current liabilities) of $7,812,387 and average days (based on normal expenditures) cash on hand of 82 days.

Financial assets available for general expenditure within one year of the balance sheet date, consists of the following at June 30, 2019:

Cash and cash equivalents	$ 4,877,195
Patient accounts receivable, net	6,279,828
Other current assets	1,510,647
Assets limited as to use:	
Board designated for capital improvements	38,629,519
Total financial assets available	$ 51,297,189

None of the financial assets available are subject to donor or other contractual restrictions that make them unavailable for general expenditure within one year of the balance sheet date. PMCI estimates that approximately 100% of the internally designated funds for capital improvements could be available for general expenditure within one year in the normal course of operations if approved by the Board of Directors. Accordingly, these assets have been included in the quantitative information above. PMCI has other assets whose use is limited for debt service. These assets whose use is limited are not available for general expenditure within the next year and are not reflected in the amounts above. However, certain board designated funds could be made available, if necessary. PMCI has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due.

Continued

18. Rural Hospital Tax Credit Contributions

The State of Georgia (State) passed legislation which will allow individuals or corporations to receive a State tax credit for making a contribution to certain qualified rural hospital organizations during calendar years 2017 through 2021. PMCI submitted the necessary documentation and was approved by the State to participate in the rural hospital tax credit program for 2019 and 2018. Contributions received under the program approximated $805,000 and $228,000 during 2019 and 2018, respectively. PMCI will have to be approved by the State to participate in the program in each subsequent year. Amounts received under the program are recorded as nonoperating income in the statements of operations and changes in net assets.