

BRISTOL HOSPITAL, INCORPORATED

FINANCIAL STATEMENTS

September 30, 2016 and 2015

BRISTOL HOSPITAL, INCORPORATED

FINANCIAL STATEMENTS
September 30, 2016 and 2015

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Bristol Hospital, Incorporated

We have audited the accompanying financial statements of Bristol Hospital, Incorporated (the Hospital), which comprise the balance sheets as of September 30, 2016 and 2015, 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 the Hospital's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Bristol Hospital, Incorporated as of September 30, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

CROWE HORWATH LLP
Crowe Horwath LLP

Simsbury, Connecticut
January 30, 2017

BRISTOL HOSPITAL, INCORPORATED
BALANCE SHEETS
September 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 11,217,004	\$ 15,285,938
Accounts receivable, less allowance for doubtful accounts of \$3,495,868 (2016) and \$4,285,214 (2015)	17,168,498	16,471,779
Other receivables	4,388,159	3,843,217
Inventories of supplies	1,437,747	1,388,084
Prepaid expenses	1,174,059	1,008,601
Due from affiliates	2,132,518	2,528,802
Debt service funds	<u>347,671</u>	<u>347,671</u>
Total current assets	37,865,656	40,874,092
Assets limited as to use:		
Funds held for malpractice self-insurance fund	4,821,905	4,418,234
Board designated investments	7,398,146	6,705,918
Beneficial interest in assets held in trust by others	3,096,891	2,990,416
Funds held under bond indenture agreements, Series B Bonds	2,505,145	2,505,243
Interest in net assets of Foundation	6,287,114	6,033,606
Donor restricted investments	<u>788,090</u>	<u>954,319</u>
Total assets limited as to use	24,897,291	23,607,736
Non-current assets:		
Long-term investments	7,693,291	6,496,418
Investments in joint ventures	390,990	614,503
Deferred expenses and other assets	287,821	287,821
Unamortized bond finance costs	<u>735,816</u>	<u>925,972</u>
Total non-current assets	9,107,918	8,324,714
Property, plant and equipment:		
Land and land improvements	6,316,095	5,042,128
Buildings	68,111,314	67,804,901
Fixtures and equipment	<u>93,312,762</u>	<u>91,594,927</u>
	167,740,171	164,441,956
Less: accumulated depreciation	<u>(131,378,783)</u>	<u>(124,849,240)</u>
	36,361,388	39,592,716
Construction in progress	<u>645,260</u>	<u>616,812</u>
Property, plant and equipment, net	<u>37,006,648</u>	<u>40,209,528</u>
 Total assets	 <u>\$ 108,877,513</u>	 <u>\$ 113,016,070</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
BALANCE SHEETS (continued)
September 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
LIABILITIES AND NET ASSETS		
Current liabilities:		
Trade accounts payable	\$ 11,178,710	\$ 11,966,693
Accrued payroll and other accrued expenses	4,541,897	6,634,907
Estimated settlements to third-party payers	1,976,385	1,130,211
Borrowings on line of credit and demand loan	1,200,000	1,800,000
Current portion of capital lease liabilities	658,414	690,414
Current portion of long-term debt	<u>835,455</u>	<u>811,425</u>
Total current liabilities	20,390,861	23,033,650
Other accrued liabilities	8,251,915	7,795,193
Long-term capital lease liabilities, less current portion	1,262,141	1,854,778
Long-term debt, less current portion	23,543,656	25,024,410
Asset retirement obligation	604,800	604,800
Accrued pension liability	<u>38,325,259</u>	<u>32,795,767</u>
Total liabilities	92,378,632	91,108,598
Net assets:		
Unrestricted	6,457,317	11,995,043
Temporarily restricted	3,144,717	3,122,057
Permanently restricted	<u>6,896,847</u>	<u>6,790,372</u>
Total net assets	<u>16,498,881</u>	<u>21,907,472</u>
Total liabilities and net assets	<u>\$ 108,877,513</u>	<u>\$ 113,016,070</u>

The accompanying notes are an integral part of these financial statements.

BRISTOL HOSPITAL, INCORPORATED
 STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
 For the Years Ended September 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Operating revenues:		
Net patient service revenues	\$ 135,754,485	\$ 135,540,204
Provision for bad debts	<u>(2,209,664)</u>	<u>(2,212,274)</u>
Net patient service revenues less provision for bad debts	133,544,821	133,327,930
Other operating revenues	<u>3,643,010</u>	<u>3,838,007</u>
Total operating revenues	137,187,831	137,165,937
Operating expenses:		
Salaries, wages and fees	60,943,753	63,048,493
Supplies and other expenses	71,394,989	65,140,654
Depreciation and amortization	6,760,410	7,176,664
Interest expense	<u>1,044,552</u>	<u>1,267,462</u>
Total operating expenses	<u>140,143,704</u>	<u>136,633,273</u>
(Loss) gain from operations	(2,955,873)	532,664
Other income:		
Investment and other income, net	<u>1,070,208</u>	<u>795,166</u>
Total other income	<u>1,070,208</u>	<u>795,166</u>
Excess of revenues (under) over expenses	<u>\$ (1,885,665)</u>	<u>\$ 1,327,830</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
For the Years Ended September 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Unrestricted net assets:		
Excess of revenues (under) over expenses	\$ (1,885,665)	\$ 1,327,830
Net change in unrealized gains (losses) on investments	1,559,313	(910,541)
Transfer to Bristol Hospital Multispecialty Group	(260,467)	(292,388)
Change in interest in net assets of Foundation	64,619	(340,308)
Pension changes other than net periodic benefit costs	(5,568,087)	(5,842,926)
Net assets released from restrictions for capital acquisitions	552,561	-
Changes in postretirement health and welfare benefits other than net periodic benefit costs	<u>-</u>	<u>420,000</u>
Change in unrestricted net assets	(5,537,726)	(5,638,333)
Temporarily restricted net assets:		
Change in interest in net assets of Foundation	398,954	(291,563)
Net change in unrealized gains (losses) on investments	342,496	(196,834)
Contributions	151,410	88,102
Net assets released from restrictions	<u>(870,200)</u>	<u>(185,739)</u>
Change in temporarily restricted net assets	22,660	(586,034)
Permanently restricted net assets:		
Change in assets held in trust by others	<u>106,475</u>	<u>(295,116)</u>
Change in permanently restricted net assets	<u>106,475</u>	<u>(295,116)</u>
Change in net assets	(5,408,591)	(6,519,483)
Net assets, beginning of year	<u>21,907,472</u>	<u>28,426,955</u>
Net assets, end of year	<u>\$ 16,498,881</u>	<u>\$ 21,907,472</u>

The accompanying notes are an integral part of these financial statements.

BRISTOL HOSPITAL, INCORPORATED
STATEMENTS OF CASH FLOWS
For the Years Ended September 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities:		
Change in net assets	\$ (5,408,591)	\$ (6,519,483)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	6,761,383	7,176,664
Provision for bad debts	2,209,664	2,212,274
Change in investments in joint ventures	223,513	150,110
Transfer to Bristol Hospital Multispecialty Group	(260,467)	(292,388)
Beneficial interest in net assets of the Foundation	(253,508)	631,872
Change in assets held in trust by others	(106,475)	295,116
Net realized and unrealized losses on investments	(1,609,522)	611,854
Accrued pension and postretirement liabilities	5,568,087	5,422,926
Changes in assets and liabilities:		
Accounts receivable	(2,906,383)	(968,909)
Other receivables	(544,942)	(33,708)
Inventories of supplies	(49,663)	25,555
Estimated settlements from third-party payers	-	581,194
Prepaid expenses	(165,458)	(61,007)
Due from affiliates	396,284	457,287
Deferred expenses and other assets	-	(1,475)
Trade accounts payable	(787,983)	(326,428)
Accrued payroll and other accrued expenses	(2,093,010)	(1,106,135)
Estimated settlements to third-party payers	846,174	1,130,211
Other accrued liabilities	456,722	(1,893,376)
Accrued pension and postretirement liabilities	<u>(38,595)</u>	<u>184,431</u>
Net cash provided by operating activities	2,237,230	7,676,585
Cash flows from investing activities:		
Additions to property, plant and equipment	(3,368,347)	(5,972,080)
Purchases of investments	(543,404)	(1,867,677)
Sales of investments	430,152	1,741,601
Changes in debt service funds	-	47,154
Changes in funds held for malpractice self insurance fund, net	<u>(403,671)</u>	<u>1,155,874</u>
Net cash used in investing activities	(3,885,270)	(4,895,128)
Cash flows from financing activities:		
Repayments of long-term debt	(2,081,361)	(425,586)
Transfer to Bristol Hospital Multispecialty Group	260,467	292,388
Payments on line of credit and demand loan	<u>(600,000)</u>	<u>(1,100,000)</u>
Net cash used in financing activities	<u>(2,420,894)</u>	<u>(1,233,198)</u>
Net change in cash and cash equivalents	(4,068,934)	1,548,259
Cash and cash equivalents at beginning of year	<u>15,285,938</u>	<u>13,737,679</u>
Cash and cash equivalents at end of year	<u>\$ 11,217,004</u>	<u>\$ 15,285,938</u>
Supplemental disclosure of cash flow information:		
Cash paid for interest	<u>\$ 1,230,311</u>	<u>\$ 1,453,221</u>
Supplemental disclosure of non-cash transactions:		
Capital leases entered into	<u>\$ -</u>	<u>\$ 2,287,365</u>

The accompanying notes are an integral part of these financial statements.

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 1 - GENERAL

Organization: Bristol Hospital, Incorporated (the Hospital), a not-for-profit, non-stock corporation incorporated under the General Statutes of the State of Connecticut, is a wholly-owned subsidiary of Bristol Hospital and Health Care Group (BHHCG). BHHCG is the sole member of the Hospital, Bristol Hospital Development Foundation, Inc. (BHDF or the Foundation), Bristol Health Care, Inc. and Subsidiary (BHC), Bristol Hospital EMS, LLC (EMS) and Bristol Hospital Multispecialty Group (BHMSG). The Board of BHHCG elects the Hospital's Board of Directors, which manages the properties and affairs of the Hospital.

The Foundation was formed as a non-profit corporation for the purpose of raising funds for the Hospital and other members of BHHCG. The Foundation is a subsidiary of BHHCG and its Board of Directors is appointed by BHHCG. The Foundation also holds certain endowment funds on behalf of the Hospital. These endowment funds are reflected by the Hospital as an interest in the net assets of the Foundation, within the net asset categories of the Hospital and on the balance sheets. Assets held by the Foundation in which the Hospital has a net interest in are classified by the Hospital within the applicable net asset class. Increases or decreases in the Hospital's interest in the net assets of the Foundation are reflected in the statements of operations and changes in net assets within the applicable net asset categories.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as promulgated by the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC).

Use of Estimates: The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that impact the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also impact the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Hospital's significant estimates relate to the allowance for doubtful accounts and contractual allowances on patient accounts receivable, valuation of investments, estimated settlements due to third-party payers, reserves for self-insurance liabilities and the pension and other postretirement employee benefit plan liability assumptions.

Net Asset Categories: To ensure observance of limitations and restrictions placed on the use of resources available to the Hospital, the accounts of the Hospital are maintained in the following net asset categories:

Unrestricted - Unrestricted net assets represent available resources other than donor restricted contributions. Included in unrestricted net assets are assets set aside by the Board of Directors (the Board) for future capital improvements, over which the Board retains control and may, at its discretion, subsequently use for other purposes.

Temporarily Restricted - Temporarily restricted net assets represent contributions that are restricted by the donor either as to purpose or as to time of expenditure.

Permanently Restricted - Permanently restricted net assets represent contributions received with the donor restriction that the principal be invested in perpetuity and that the income earned thereon be available for operations, and beneficial interest in assets held in trust by others.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and Cash Equivalents: The Hospital considers certain highly liquid investments with maturities of ninety days or less at the date of purchase to be cash equivalents. Cash balances maintained at banks are insured by the Federal Deposit Insurance Corporation (FDIC). The FDIC insures cash balances up to \$250,000 per depositor, per bank. Amounts in excess of the FDIC limits are uninsured. Cash and cash equivalents are maintained primarily with one bank including one investment bank sponsored money market fund and from time to time cash balances exceed FDIC limits. It is the Hospital's policy to monitor the bank's financial strength on an ongoing basis.

Assets Limited as to Use: Assets limited as to use include funds held for malpractice self-insurance, assets set aside by the Board of Directors for future capital improvements over which the Board of Directors retains control, the beneficial interest in assets held in trust by others, investments held in escrow under borrowing arrangements, donor restricted investments and interest in net assets of BHDF, and may, at its discretion, subsequently use for other purposes.

Inventories: Inventories are stated at the lower of cost or market, determined by the first-in, first-out (FIFO) method.

Investments: The Hospital accounts for its investments in accordance with FASB ASC 320, "*Investments - Debt and Equity Securities*." Short-term investments and investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the accompanying balance sheets. Investment income (including realized gains and losses on investments, interest and dividends) is included in the excess of revenues over expenses, unless the income is restricted by donor or law. Unrealized gains and losses on investments are excluded from excess of revenues over expenses.

All of the Hospital's investments as of September 30, 2016 and 2015, were classified as available for sale. Available for sale securities may be sold prior to maturity and are carried at fair value. Realized gains and losses, relating to available for sale securities, determined on the specific identification basis, along with interest and dividend income, are reported as a component of non-operating income on the statements of operations and changes in net assets.

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

Other Than Temporary Impairment of Investments: The Hospital accounts for other than temporary impairments in accordance with FASB ASC 320. When a decline in fair market value is deemed to be other than temporary, a provision for impairment is charged to earnings, included in non-operating income, and the cost basis of that investment is reduced.

The Hospital's management reviews several factors to determine whether a loss is other than temporary, such as the length of time a security is in a unrealized loss position, extent to which the fair value is less than cost, the financial condition and near term prospects of the issuer and the Hospital's intent and ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value. No impairment losses were recognized in 2016 and 2015.

Deferred Financing Costs: Costs incurred with the long-term debt were capitalized and are being amortized over the life of the related bonds. Amortization expense totaled \$189,183 and \$54,594 during 2016 and 2015, respectively.

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BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, Plant and Equipment: Property, plant and equipment is recorded at cost or, if received as a donation, at the fair value on the date received. The Hospital provides for depreciation of property, plant and equipment using the straight-line method in amounts sufficient to amortize the cost of its assets over their useful lives. Leasehold improvements are amortized over the shorter of the lease term or the following useful lives range. Useful lives assigned to assets are as follows: Land improvements - 2 to 25 years; Leasehold improvements - 15 to 20 years; Buildings - 15 to 40 years; and Fixtures and equipment - 3 to 20 years. For the years ended September 30, 2016 and 2015, depreciation expense amounted to \$6,571,227 and \$7,122,070, respectively.

Investments in Joint Ventures: The Hospital has invested in the following joint ventures and limited liability companies, which are accounted for under the equity method of accounting.

	<u>Ownership Percentage</u>
Bristol MSO, LLC	50.00%
MedWorks, LLC	49.00%
Connecticut Occupational Medical Partners	33.00%
Central Connecticut Endoscopy Center	6.50%
Connecticut Hospital Laboratory Network	4.54%

Investments in limited liability companies are accounted for using the equity method in accordance with FASB ASC 323, "*Investments - Equity Method and Joint Ventures*" in instances where the limited partner's interest is more than minor (3-5%), or the Board has the ability to exercise significant influence over the operations of the company.

During 2016 and 2015, the Hospital recorded income of \$269,593 and \$186,842, respectively, related to its equity method investments, which is included in net investment and other income on the statements.

During 2015, the Hospital withdrew its investment in Total Laundry Collaborative, LLC. At the time of withdrawal, the Hospital recorded a \$245,906 loss related to its full investment balance in the limited liability company.

Donor Restricted Gifts: Unconditional promises to give cash and other assets to the Hospital 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 either temporarily or permanently 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 the stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of operations and changes in net assets, as net assets released from restrictions. Donor restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying statements of operations and changes in net assets.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Assets Held in Trust by Others: The Hospital has been named sole or participating beneficiary in several perpetual trusts. Under the terms of these trusts, the Hospital has the irrevocable right to receive the income earned on the trust assets in perpetuity. Fluctuations in the value of such assets are recognized as changes in permanently restricted net assets.

Board Restricted: As of September 30, 2016 and 2015, the Hospital has \$7,398,146 and \$6,705,918, respectively, of unrestricted investments which have been restricted by the Board of Directors of BHHCG and are not available for use without the approval of the Board of Directors.

Temporarily and Permanently Restricted Net Assets: Temporarily restricted net assets are those whose use by the Hospital have been limited by donors to a specific time period or purpose. Temporarily restricted net assets consist primarily of contributions for capital improvements and healthcare services. Permanently restricted net assets, which are primarily endowment gifts and assets held in trust by others, have been restricted by donors to be maintained in perpetuity (see Note 6). Both temporarily and permanently restricted net assets also consist of contributions held by the Foundation for healthcare services for the benefit of the Hospital.

Excess of Revenues (Under) Over Expenses: The statements of operations and changes in net assets include excess of revenues (under) over expenses. This measurement is the performance indicator. Changes in unrestricted net assets which are excluded from excess of revenues (under) over expenses, consistent with industry practice, include unrealized gains and losses on investments other than trading securities, certain changes in the pension and postretirement benefit liabilities, 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 purposes of acquiring such assets).

For purposes of presentation, transactions deemed by management to be ongoing, major or central to the provision of healthcare services are reported as operating revenues and expenses. Investment interest income and income (loss) generated on equity investments are considered non-operating activities.

Income Taxes: The Hospital is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal and state income taxes on related income pursuant to Section 501(a) of the Code.

The Hospital accounts for uncertain tax positions with provisions of FASB ASC 740, "Income Taxes," which provides a framework for how companies should recognize, measure, present and disclose uncertain tax positions in their financial statements. The Hospital may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position.

The Hospital does not have any uncertain tax positions as September 30, 2016 and 2015. It is the Hospital's policy to record penalties and interest associated with uncertain tax provisions as a component of operating expenses. As of September 30, 2016 and 2015, the Hospital did not record any penalties or interest associated with uncertain tax positions. The Hospital's prior three tax years are open and subject to examination by the Internal Revenue Service.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair Value Measurements: The Hospital measures fair value in accordance with FASB ASC 820, "*Fair Value Measurements and Disclosures*," which defines fair value, establishes a framework for measuring fair value and requires certain disclosures about fair value measurements (see Note 5). The definition of fair value under FASB ASC 820 focuses on the price that would be received to sell the asset, which is referred to as the exit price.

Malpractice, General and Workers' Compensation Self-Insurance: The Hospital maintains self-insurance coverage for medical malpractice, general liability and workers' compensation insurance (see Notes 12 and 13). The Hospital has continually maintained a liability for reserves relating to these coverages. These liabilities are recorded within other accrued liabilities on the balance sheets. The liability for malpractice insurance includes an estimated incurred but not reported claim reserve. The Hospital has recorded an additional liability and related recoverable from their commercial insurers relating to estimated reserves in excess of the self-insured layer. These amounts are recorded as increases under the captions "other receivables" and "other accrued liabilities" in the accompanying balance sheets by \$3,544,353 and \$3,304,416 as of September 30, 2016 and 2015, respectively. The increases represent the Hospital's estimate of liabilities and recoveries for certain professional and general liability claims in excess of the self-insured retentions. There were no increases relating to additional reserves on self-insured workers' compensation as there were no reserve estimates in excess of the self-insured retention.

Reclassifications: Certain items in the prior year financial statements were reclassified to conform to the current presentation. These reclassifications had no effect on net assets or the change in net assets.

Subsequent Events: Subsequent events have been evaluated through January 30, 2017, which is the date through which procedures were performed and the financial statements were issued. Management believes there are no subsequent events having a material impact on the financial statements.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 3 - REVENUES FROM SERVICES TO PATIENTS AND CHARITY CARE

The following reconciles gross patient service revenues to net patient service revenues:

	2016				
	Medicare and Medicare HMOs	Medicaid and Medicaid HMOs	Blue Cross	Commercial and Other	Total
Gross revenues from services to patients	\$ 217,459,852	\$ 99,946,173	\$ 43,355,043	\$ 108,628,912	\$ 469,389,980
Deductions and allowances	<u>(163,467,144)</u>	<u>(79,584,709)</u>	<u>(25,519,506)</u>	<u>(65,064,136)</u>	<u>(333,635,495)</u>
Net revenues from services to patients	<u>\$ 53,992,708</u>	<u>\$ 20,361,464</u>	<u>\$ 17,835,537</u>	<u>\$ 43,564,776</u>	<u>\$ 135,754,485</u>
	2015				
	Medicare and Medicare HMOs	Medicaid and Medicaid HMOs	Blue Cross	Commercial and Other	Total
Gross revenues from services to patients	\$ 205,561,817	\$ 97,960,036	\$ 42,171,690	\$ 98,415,135	\$ 444,108,678
Deductions and allowances	<u>(151,197,545)</u>	<u>(79,343,874)</u>	<u>(25,165,184)</u>	<u>(52,861,871)</u>	<u>(308,568,474)</u>
Net revenues from services to patients	<u>\$ 54,364,272</u>	<u>\$ 18,616,162</u>	<u>\$ 17,006,506</u>	<u>\$ 45,553,264</u>	<u>\$ 135,540,204</u>

Net patient service revenue is reported at the established net realizable amounts from patients, third-party payers and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Net patient service revenue and accounts receivable are recorded when patient services are performed. Amounts received from most payers are different from established billing rates of the Hospital based on agreements with these payers, and these differences are accounted for as contractual allowances. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, per diem payments, and discounted charges, including estimated retroactive settlements under payment agreements with third-party payors. Adjustments and settlements under reimbursement agreements with third-party payers. Adjustments and settlements under reimbursement agreements with third-party payers are accrued on an estimated basis in the period the related services are provided, and adjusted in future periods as final settlements are determined.

For uninsured patients that do not qualify for charity care, the Hospital recognizes revenue based on its discounted rates. On the basis of historical experiences, a significant portion of the Hospital's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the Hospital records a significant provision for bad debts related to uninsured patients in the period the services are provided.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 3 - REVENUES FROM SERVICES TO PATIENTS AND CHARITY CARE (continued)

Patient accounts receivable are based on gross charges and stated at net realizable value. Accounts receivable are reduced by an allowance for contractual adjustments, based on expected payment rates from payers under current reimbursement methodologies, and also by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the Hospital analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts, based upon management's assessment of historical and expected net collections considering business and economic conditions, trends in health care coverage, and other collection indicators. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for contractual adjustments and allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Hospital analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts (for example, for expected uncollectable deductibles and copayments on accounts for which the third-party payer has not yet paid, or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and co-payment balances due for which third-party coverage exists for part of the bill), the Hospital records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

For uninsured patients that do not qualify for financial assistance, the Hospital offers a discount off its standard rates for services provided. The difference between the discounted rates and the amounts actually collected after all reasonable collection efforts have been exhausted is written off against the allowance for doubtful accounts in the period they are determined uncollectable. The Hospital's allowance for doubtful accounts covers approximately 98% and 100% of self-pay accounts receivable as of September 30, 2016 and 2015, respectively.

As of September 30, 2016 and 2015, approximately 62% and 59% of net patients accounts receivable were from governmental payers (Medicare and Medicaid). Nongovernmental payers are primarily insurance companies and self-pay payers. Management has recorded an allowance for doubtful accounts, as noted above, which, in its opinion, is sufficient to provide for risk of nonpayment.

Charity Care: It is an inherent part of the Hospital's mission to provide necessary medical care free of charge, or at a discount, to individuals without insurance or other means of paying for such care. As the amounts determined to qualify for charity care are not pursued for collection, they are not reported as net patient service revenue. Patients who would otherwise qualify for charity care but who do not provide adequate information would be characterized as bad debt and included in the provision for bad debts. The cost of charity care provided, determined using a cost-to-charge ratio, was \$1,229,318 and \$1,261,286 for the years ended September 30, 2016 and 2015. The Hospital did not change its charity care or financial assistance policy during 2016 or 2015.

Federal Regulatory Environment: The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
 NOTES TO THE STATEMENTS
 For the Years Ended September 30, 2016 and 2015

NOTE 3 - REVENUES FROM SERVICES TO PATIENTS AND CHARITY CARE (continued)

Government activity continues to increase with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs, together with the impulsion of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Hospital is in compliance with fraud and abuse regulations as well as other applicable government laws and regulations. While no known regulatory inquiries are pending, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions known or un-asserted at this time.

NOTE 4 - INVESTMENTS

The Hospital has investments carried on the balance sheets within assets held in trust under bond indenture agreements related to financing activities with the State of Connecticut Health and Educational Facilities Authority (CHEFA or the Authority), funds held within a malpractice self insurance fund, assets held in trust by others, board designated investments, long-term investments and temporary and permanently donor restricted investments. The fair values of investments, as of September 30, 2016 and 2015, are summarized as follows:

	<u>2016</u>	<u>2015</u>
Debt Service Funds:		
U.S. treasury obligations	\$ <u>347,671</u>	\$ <u>347,671</u>
Assets Limited as to Use:		
Board designated investments:		
Cash and interest bearing accounts	\$ 80,755	\$ 84,119
Equity mutual funds	7,237,626	6,537,776
Fixed income mutual funds	<u>79,765</u>	<u>84,023</u>
Total	<u>\$ 7,398,146</u>	<u>\$ 6,705,918</u>
Held for malpractice self insurance fund:		
Corporate and foreign bonds	\$ 565,658	\$ 857,141
Cash and interest bearing accounts	100,895	-
Equity securities	134,933	80,775
Equity mutual funds	2,620,300	1,142,592
Fixed income mutual funds	<u>1,400,119</u>	<u>2,337,726</u>
Total	<u>\$ 4,821,905</u>	<u>\$ 4,418,234</u>
Held by trustee under bond indenture agreement:		
U.S. treasury obligations	<u>\$ 2,505,145</u>	<u>\$ 2,505,243</u>
Long-term Investments:		
Cash and interest bearing accounts	\$ 82,856	\$ 96,571
Equity mutual funds	<u>7,610,435</u>	<u>6,399,847</u>
Total	<u>\$ 7,693,291</u>	<u>\$ 6,496,418</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 4 - INVESTMENTS (continued)

Beneficial interest assets held in trust by others of \$3,096,891 and \$2,990,416, as of September 30, 2016 and 2015, respectively, are held by bank trustees and are not under the Hospital's investment control. These assets are invested within diversified portfolios.

As of September 30, 2016 and 2015, investment amounts not included in the aforementioned table include donor restricted investments in the amounts of \$636,680 and \$954,319, respectively, which are investments in mutual funds and are classified as temporarily and permanently restricted net assets. Also not included in the above table are cash and investments held within the Hospital's interest in the net assets of the Foundation.

The Hospital has cash and investments totaling \$6,287,114 and \$6,033,606 held within the Foundation, of which \$3,405,814 and \$3,405,814 are permanently restricted as of September 30, 2016 and 2015, respectively. Other temporarily restricted cash and investments of \$2,776,161 and \$2,561,880, and the Foundation's unrestricted net assets, are included within the Hospital's interest in the Foundation on the balance sheets as of September 30, 2016 and 2015, respectively.

NOTE 5 - FAIR VALUE MEASUREMENTS

GAAP defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the Hospital's principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the Hospital has the ability to access as of the measurement date. The fair values of money market funds and mutual funds that are readily marketable are determined by obtaining quoted prices from nationally recognized securities exchanges.

Level 2: Significant other unobservable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data. The fair values of the Hospital's Level 2 U.S. Treasury obligations, various fixed income bond funds, and preferred equity securities were determined by matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities. The fair values of the Hospital's Level 2 investments are determined by management after considering prices received from third-party pricing services.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability. Funds held in trust by others represents beneficial interest in certain assets held by third parties. These interest are classified as Level 3 investments as the reported fair values are based on a combination of Level 1 and Level 2 inputs and significant unobservable inputs as determined by the trustees who exercise control over the investments.

In many cases, a valuation technique used to measure fair value includes inputs from multiple levels of the fair value hierarchy. The lowest level of significant input determines the placement of the entire fair value measurement in the hierarchy.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 5 - FAIR VALUE MEASUREMENTS (continued)

The following table presents the financial instruments, carried at fair value as of September 30, 2016, by the valuation hierarchy. This table includes assets limited as to use, including the assets held within the Hospital's interest in the net assets of BHDF, and long-term investments:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash equivalents	\$ 1,035,415	\$ -	\$ -	\$ 1,035,415
Equities:				
Mutual Funds:				
U.S. large cap	5,481,141	-	-	5,481,141
U.S. mid cap	2,836,630	-	-	2,836,630
U.S. small cap	1,892,249	-	-	1,892,249
Internationally developed	3,154,128	-	-	3,154,128
Commodities	693,529	-	-	693,529
Public REIT	1,103,571	-	-	1,103,571
Closed end	274,573	-	-	274,573
Emerging markets	148,428	-	-	148,428
Preferred equity securities	-	91,563	-	91,563
Fixed Income:				
U.S. treasury obligations	-	2,852,816	-	2,852,816
Corporate and foreign bonds	-	565,658	-	565,658
Taxable fixed income mutual funds	-	6,067,433	-	6,067,433
Internationally developed	-	2,712,460	-	2,712,460
Closed-end fixed income mutual funds	-	353,586	-	353,586
Other	-	540,503	-	540,503
Global high yield taxable	-	37,679	-	37,679
	<u>16,619,664</u>	<u>13,221,698</u>	<u>-</u>	<u>29,841,362</u>
Beneficial interest in assets held in trust by others	<u>-</u>	<u>-</u>	<u>3,096,891</u>	<u>3,096,891</u>
Total	<u>\$ 16,619,664</u>	<u>\$ 13,221,698</u>	<u>\$ 3,096,891</u>	<u>\$ 32,938,253</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 5 - FAIR VALUE MEASUREMENTS (continued)

The following table presents the financial instruments, carried at fair value, as of September 30, 2015, by the valuation hierarchy. This table includes assets limited as to use, including the assets held within the Hospital's interest in the net assets of BHDF, and long-term investments:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash equivalents	\$ 1,292,584	\$ -	\$ -	\$ 1,292,584
Equities:				
Mutual Funds:				
U.S. large cap	5,722,241	-	-	5,722,241
U.S. mid cap	2,752,398	-	-	2,752,398
U.S. small cap	1,820,817	-	-	1,820,817
Internationally developed	4,021,187	-	-	4,021,187
Commodities	832,642	-	-	832,642
Public REIT	871,770	-	-	871,770
Emerging markets	148,563	-	-	148,563
Preferred equity securities	-	80,775	-	80,775
Fixed Income:				
U.S. treasury obligations	-	3,106,363	-	3,106,363
Corporate and foreign bonds	-	857,141	-	857,141
Taxable fixed income mutual funds	-	4,291,686	-	4,291,686
Internationally developed	-	926,702	-	926,702
Global high yield taxable	-	736,540	-	736,540
	<u>17,462,202</u>	<u>9,999,207</u>	-	<u>27,461,409</u>
Beneficial interest in assets held in trust by others	<u>-</u>	<u>-</u>	<u>2,990,416</u>	<u>2,990,416</u>
 Total	 <u>\$ 17,462,202</u>	 <u>\$ 9,999,207</u>	 <u>\$ 2,990,416</u>	 <u>\$ 30,451,825</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
 NOTES TO THE STATEMENTS
 For the Years Ended September 30, 2016 and 2015

NOTE 5 - FAIR VALUE MEASUREMENTS (continued)

A rollforward of the investments classified as Level 3, within the fair value hierarchy, are as follows:

	<u>2016</u>	<u>2015</u>
Balance at beginning of year	\$ 2,990,416	\$ 3,285,532
Interest and dividends	60,376	59,890
Contributions	46,034	46,653
Withdrawals	(130,010)	(176,401)
Net realized (losses) gains	(14,430)	48,860
Fees	(37,968)	(39,694)
Net unrealized gains	<u>182,474</u>	<u>(234,425)</u>
Balance at end of year	<u>\$ 3,096,891</u>	<u>\$ 2,990,416</u>

There were no transfers between fair value hierarchy Level 1, Level 2, and Level 3 for any invested assets recorded at fair value during 2016 and 2015. The valuation techniques used by the Hospital maximize the use of observable inputs and minimize the use of unobservable inputs. The fair value of the Hospital's Level 2 and Level 3 investments are determined by management after considering prices received from third-party pricing services.

As of September 30, 2016 and 2015, the Hospital's other financial instruments include cash and cash equivalents, accounts payable, accrued expenses, estimated settlements due to third-party payers and long-term debt. The carrying amounts reported in the balance sheets for these financial instruments approximate their fair value.

NOTE 6 - NET ASSETS AND ENDOWMENTS

Temporarily restricted net assets, as of September 30, 2016 and 2015 are available for the following purposes:

	<u>2016</u>	<u>2015</u>
Library operations and improvements	\$ 393,948	\$ 560,177
Healthcare services - Foundation	<u>2,750,769</u>	<u>2,561,880</u>
Total	<u>\$ 3,144,717</u>	<u>\$ 3,122,057</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 6 - NET ASSETS AND ENDOWMENTS (continued)

Permanently restricted net assets, as of September 30, 2016 and 2015, are available for the following purposes:

	<u>2016</u>	<u>2015</u>
Held in perpetuity, income restricted for healthcare services - Foundation	\$ 3,405,814	\$ 3,405,814
Other donor restricted investments	394,142	394,142
Beneficial interest in assets held in trust by others	<u>3,096,891</u>	<u>2,990,416</u>
Total	<u>\$ 6,896,847</u>	<u>\$ 6,790,372</u>

The Hospital's endowment and restricted net assets consists of multiple funds established for a variety of purposes. These funds include donor restricted endowment funds, the Hospital's beneficial interest in the BHDF and funds held in trust by others. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor restrictions.

The Hospital has interpreted the relevant laws as requiring the preservation of the fair value of the original gift as of the gift date of the donor restricted endowment funds absent explicit donor stipulations to the contrary. The remaining portion of the donor restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Hospital during its annual budgeting process.

The Board of Directors of the Hospital considers the following factors in making a determination to appropriate or accumulate donor restricted endowment funds: (1) the duration and preservation of the fund; (2) the purposes of the Hospital and the donor restricted endowment fund; (3) general economic conditions; (4) the possible effect of inflation and deflation; (5) the expected total return from income and the appreciation of investments; (6) other resources of the Hospital; and (7) the investment policies of the Hospital.

The Hospital has adopted investment and spending policies for endowment assets that attempt to provide a reasonably stable and predictable stream of earnings to support the operations of the endowments and to preserve and enhance over time the real value of the endowment assets. The Board of Directors is responsible for defining and reviewing the investment policies to determine an appropriate long-term asset allocation policy. The asset allocation policy reflects the objective with allocations structured for capital growth and inflation protection over the long-term.

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

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 6 - NET ASSETS AND ENDOWMENTS (continued)

Changes in net assets for endowments for the years ended September 30, 2016 and 2015, are as follows:

	2016		
	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at October 1, 2015	\$ -	\$ 6,790,372	\$ 6,790,372
Investment return:			
Investment income	208,122	-	208,122
Net change in market value	-	106,475	106,475
Appropriations	<u>(208,122)</u>	<u>-</u>	<u>(208,122)</u>
Balance at September 30, 2016	<u>\$ -</u>	<u>\$ 6,896,847</u>	<u>\$ 6,896,847</u>
	2015		
	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at October 1, 2014	\$ -	\$ 7,085,488	\$ 7,085,488
Investment return:			
Investment income	248,861	-	248,861
Net change in market value	-	(295,116)	(295,116)
Appropriations	<u>(248,861)</u>	<u>-</u>	<u>(248,861)</u>
Balance at September 30, 2015	<u>\$ -</u>	<u>\$ 6,790,372</u>	<u>\$ 6,790,372</u>

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or relevant law requires the Hospital to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. As of September 30, 2016 and 2015, the Hospital's interest in the permanently restricted investment in donor restricted endowment funds did not drop below the amount required to be retained in perpetuity. Therefore, there were no reductions to unrestricted net assets.

NOTE 7 - LEASES

The Hospital leases property and equipment under non-cancelable operating leases that expire in various years through fiscal year 2020. Certain leases may be renewed at the end of their term. Additionally, the Hospital has entered into various capital leases for medical equipment. Amounts due are included in capital lease liabilities on the balance sheets.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 7 - LEASES (continued)

Future minimum payments under non-cancelable capital and operating leases with initial terms of one year or more consisted of the following as of September 30, 2016:

	<u>Operating Leases</u>	<u>Capital Leases</u>	
2017	\$ 173,991	\$ 669,660	
2018	173,991	585,157	
2019	173,991	516,433	
2020	173,991	223,854	
2021	<u>173,991</u>	<u>-</u>	
Total	<u>\$ 869,955</u>	1,995,104	
Less: amount representing interest		<u>(74,549)</u>	
Present value of net minimum lease payments		1,920,555	
Less: current maturities of capital lease obligations		<u>(658,414)</u>	
Long-term capital lease obligations		<u>\$ 1,262,141</u>	

As of September 30, 2016 and 2015, fixtures and equipment on the balance sheets includes assets under capital leases of \$2,282,120 and \$2,617,651, respectively. Accumulated depreciation on these assets amounted to \$961,887 and \$626,356 as of September 30, 2016 and 2015, respectively. Rental expense on operating leases was approximately \$1,419,860 and \$1,664,030 for the years ended September 30, 2016 and 2015, respectively. The Hospital has numerous operating leases which are deemed month to month.

NOTE 8 - LONG-TERM DEBT

On January 1, 2002, CHEFA issued \$38,000,000 of Series B Bonds (the Series B Bonds or Bonds) on behalf of BHHCG, which includes, the Hospital, BHC, EMS and the BHDF (collectively referred to as the "Obligated Group" under the Series B Bonds). The Series B Bonds mature serially from 2002 through 2032 with annual interest rates ranging from 3.0 to 5.5 percent. The Loan Agreement with the Authority and the Trust Indenture for the Series B Bonds contain certain covenants that require the Obligated Group to maintain a debt service coverage ratio of at least 1.25 at each fiscal year end and to maintain days cash on hand of at least 70 days at each June 30th and December 31st.

In 2006 and 2007, the Obligated Group did not meet certain covenants. As a result, in 2007, the Obligated Group entered into a forbearance agreement with the bond insurer. The forbearance agreement changed the days cash on hand measurement period from each December 31 and June 30 to each March 31 and September 30, beginning September 30, 2007. In addition, the forbearance agreement reduced the required number of days cash on hand to 40 days at September 30, 2007, reverting gradually back to 70 days on March 31, 2011 and thereafter. The forbearance agreement also limits additional long-term indebtedness based on certain debt service coverage ratios, as defined. In connection with the forbearance agreement, in fiscal 2008, the Obligated Group was required to deposit \$2,678,000 into a separate debt service reserve fund as well as amend the Series B Loan Agreement to conform to the terms and conditions of the forbearance agreement. In 2009, the required separate debt service reserve fund was returned and no longer required based on conditions of the forbearance agreement being met.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 8 - LONG-TERM DEBT (continued)

In January 2008, the CHEFA Loan Agreement and related Trust Indenture were amended. The amended agreement requires the debt service coverage ratio to be not less than 1.35 to 1 and the days cash on hand to be not less than 70 days. The Obligated Group, for the years ended September 30, 2016 and 2015, is in compliance with the terms of the forbearance agreement, the amended Series B Loan Agreement and the Trust Indenture.

Members of the Obligated Group are jointly and severally obligated to provide amounts sufficient to enable the Authority to pay principal and interest on the Series B Bonds. The Bonds have been allocated to the Hospital and BHC and as such, the Hospital and BHC will make future debt service payments as required under the terms of the Bonds. As collateral for payment of the Series B Bonds, the Authority has assigned and pledged to the Trustee the payments to be made by the Hospital and BHC under their respective agreements. The Hospital and BHC have recorded their respective portions of the Bonds with BHC receiving 56.3% of all bonds maturing through fiscal year 2020 and the Hospital receiving 43.7% of all bonds maturing through fiscal year 2020 along with the remaining 100% of the Bonds maturing through fiscal year 2032.

Below is a summary of the Hospital's and BHC's annual principal payments relating to CHEFA, due as of September 30, 2016:

	Bristol Hospital Incorporated	Bristol Health Care, Inc. and Subsidiary	Total Obligated Group
Year ending September 30:			
2017	\$ 478,515	\$ 616,485	\$ 1,095,000
2018	506,920	653,080	1,160,000
2019	535,325	689,675	1,225,000
2020	563,730	726,270	1,290,000
2021	1,225,000	-	1,225,000
Thereafter	<u>18,860,000</u>	<u>-</u>	<u>18,860,000</u>
	22,169,490	2,685,510	24,855,000
Less: portion classified as current	<u>(478,515)</u>	<u>(616,485)</u>	<u>(1,095,000)</u>
	21,690,975	2,069,025	23,760,000
Less: discount	<u>(312,850)</u>	<u>(18,369)</u>	<u>(331,219)</u>
Total	<u>\$ 21,378,125</u>	<u>\$ 2,050,656</u>	<u>\$ 23,428,781</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 8 - LONG-TERM DEBT (continued)

Effective January 31, 2014, a line of credit was terminated and the remaining outstanding balance of \$3,000,000 was converted into a term loan. Pursuant to the term loan conversion, the Hospital was required to immediately reduce the outstanding balance on the line of credit by \$200,000 to \$2,800,000. The term loan is due September 2018, with principal payments of \$50,000 due monthly. The interest on the term loan is equal to Bank of America's prime rate plus 2%, which was 5.5% and 5.25% as of September 30, 2016 and 2015, respectively. At September 30, 2016 and 2015, the balance outstanding on the term loan was \$1,200,000 and \$1,800,000, respectively.

The term loan requires the Hospital to maintain, at each quarter end, a debt service coverage ratio of 1.25 and days cash on hand at least 60 days at September 30.

On May 28, 2004, the Hospital purchased a building in Bristol, which was subsequently leased to EMS. As part of the purchase, the Hospital obtained a mortgage in the amount of \$350,000. The term of the mortgage is for 30 years. The initial interest rate is 5.00%, fixed for five years, then changing on each fifth year anniversary to the prevailing commercial interest rate less 1.00%. The balance outstanding at September 30, 2016 and 2015 is \$264,172 and \$273,261, respectively.

On July 24, 2007, the Hospital financed an existing building for \$1,400,000. The term of the mortgage note is for twenty years. The initial interest rate is 6.38%, fixed for five years, and then changing on each fifth year anniversary to the then current interest rate paid on the FHLB Five Year Classic Advance Rate plus 1.25%. The balance outstanding as of September 30, 2016 and 2015 is \$916,571 and \$984,656, respectively.

On July 16, 2010, the Hospital entered into a commercial mortgage loan with United Bank in the amount of \$850,000 as part of a purchase and refinance of a medical office building. The term of the mortgage is for fifteen years. Initial monthly payments on the loan for the first five years are \$7,173 and are subject to change based on the following adjustment to the interest rate. The initial interest rate is 6%, fixed for five years, and then changing on each fifth year anniversary to the then current FHLB Classic Advance Rate plus 2.50%. The balance outstanding as of September 30, 2016 and 2015 was \$594,109 and \$643,218 respectively.

In 2013, the Hospital entered into a \$1,000,000 promissory loan agreement with the Connecticut Hospital Association Trust for the purchase of equipment, which enables the Hospital to conserve electrical energy and to manage electrical energy needs. The Hospital shall repay the principal balance of the note in 84 equal monthly installments of \$11,905. The balance outstanding as of September 30, 2016 and 2015 was \$547,619 and \$690,476, respectively.

In 2016 and 2015, the Hospital has a \$500,000 line of credit available with United Bank. Interest is payable at 4.25%. As of September 30, 2016 and 2015, there were no advances outstanding on this line of credit.

As of September 30, 2016 and 2015, the Hospital is in compliance with all financial covenants related to previously noted debt.

(Continued)

BRISTOL HOSPITAL, INCORPORATED
 NOTES TO THE STATEMENTS
 For the Years Ended September 30, 2016 and 2015

NOTE 8 - LONG-TERM DEBT (continued)

Below is a summary of the Hospital's annual principal long-term debt payments due subsequent to September 30, 2016, as described above:

2017	\$ 835,455
2018	889,861
2019	824,296
2020	834,970
2021	1,384,080
Thereafter	<u>19,903,045</u>
Total	<u>\$ 24,671,707</u>

NOTE 9 - PENSION PLAN AND POSTRETIREMENT HEALTH BENEFITS

Pension Plan: The Hospital and BHC have a defined benefit pension plan (the Plan) covering substantially all of its and its subsidiaries' employees. The benefit formula is based on years of service and the employee's compensation during the highest paid years of employment and credited service. The funding policy is to contribute annually an actuarially determined amount intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

Effective December 31, 2006, the Plan was frozen with regard to future pension benefit accruals.

Significant disclosures relating to the Plan as of September 30, 2016 and 2015, are as follows:

	<u>2016</u>	<u>2015</u>
Change in benefit obligation:		
Projected benefit obligation at beginning of year	\$ 82,962,000	\$ 79,822,000
Interest cost	3,851,000	3,711,000
Actuarial loss	10,134,000	2,952,000
Benefits paid	<u>(3,668,000)</u>	<u>(3,523,000)</u>
Benefit obligation at end of year	<u>\$ 93,279,000</u>	<u>\$ 82,962,000</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ 50,166,000	\$ 52,805,000
Employer contributions	4,036,000	2,748,000
Actual return on plan assets, net of expenses	4,420,000	(1,864,000)
Benefits paid	<u>(3,668,000)</u>	<u>(3,523,000)</u>
Fair value of plan assets at end of year	<u>\$ 54,954,000</u>	<u>\$ 50,166,000</u>
Accrued pension liability:		
Unfunded status and accrued pension liability	<u>\$ (38,325,000)</u>	<u>\$ (32,796,000)</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 9 - PENSION PLAN AND POSTRETIREMENT HEALTH BENEFITS (continued)

	<u>2016</u>	<u>2015</u>
Assumptions:		
Weighted-average assumptions used to determine benefit obligations:		
Discount rate	3.75%	4.75%
Expected return on plan assets	8.50%	8.50%
Rate of compensation increase	N/A	N/A
Weighted-average assumptions used to determine net periodic benefit cost:		
Discount rate	4.75%	4.75%
Expected return on plan assets	8.50%	8.50%
Rate of compensation increase	N/A	N/A

For the years ended September 30, 2016 and 2015, there are no differences between the Plan's accumulated benefit obligation and projected benefit obligation as the Plan is frozen.

Pension Plan Amendments: Effective October 1, 2003, the formula for calculating benefits under the Plan was changed, on a prospective basis, to calculate accumulated benefits based on each eligible participant's annual compensation in each Plan year versus each eligible participant's five-year average compensation for each plan year. Benefits earned by plan participants prior to September 30, 2003, under the old benefit formulation, remain unchanged.

The following table sets forth the components of net periodic benefit cost for the years ended September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Components of net periodic benefit cost		
Interest cost	\$ 3,851,000	\$ 3,711,000
Expected return on plan assets	(4,261,000)	(4,493,000)
Recognized net loss	<u>4,407,000</u>	<u>3,466,000</u>
 Net periodic benefit cost	 <u>\$ 3,997,000</u>	 <u>\$ 2,684,000</u>

As of September 30, 2016 and 2015, amounts included in unrestricted net assets not yet amortized as a component of net periodic benefit cost are \$50,618,509 and \$45,050,422, respectively, which consists of unrecognized actuarial losses only. The amortization of the above expected to be recognized in net periodic benefit costs for the year ended September 30, 2017 is \$4,968,788.

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BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 9 - PENSION PLAN AND POSTRETIREMENT HEALTH BENEFITS (continued)

Changes in benefit obligations recognized in unrestricted net assets include the following as of September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Loss arising during year	\$ (9,975,060)	\$ (9,308,549)
Amortization of loss in performance indicator	<u>4,406,973</u>	<u>3,465,623</u>
Change recognized outside of performance indicator	<u>\$ (5,568,087)</u>	<u>\$ (5,842,926)</u>

The investment objective for the Plan seeks a long-term return to meet the Plan obligations. The expected return on plan assets assumption is derived based on the target asset allocation and expected long-term rates of return for those asset classes.

The Hospital's target and actual pension plan weighted-average asset allocations as of September 30, 2016, by asset category, are as follows:

	<u>Target Allocation</u>	<u>Actual Allocation</u>
Asset category:		
Equity securities	40% - 95%	58%
Debt securities	0% - 45%	24%
Other	0% - 40%	16%
Money market funds		<u>2%</u>
Total		<u><u>100%</u></u>

Fair value methodologies used to assign plan assets to levels in accordance with ASC 820 are consistent with the inputs described in Note 5. In addition, the alternative investment funds, which consist of the Omega Overseas Credit Opportunities Fund, Ltd. (the Omega Fund) and the Beach Point Total return Offshore Fund II Ltd. (the Beach Point Fund), are not traded in an active market. The fair values have been estimated using the net asset value per share of the investments, as reported by the fund managers in fund investment statements provided to, and reviewed by, the pension plan's Investment Committee. The audited financial statements of the alternative investment funds are as of December 31, and the Investment Committee evaluates the gap period, with consideration of specific fund transactions and investment returns of established benchmarks for that gap period. The Investment Committee analyzes the investment valuation methods used by the fund managers, as reported in the audited financial statements.

The Omega Fund and the Beach Point Fund are not redeemable until the pension plan has held these funds for twelve consecutive months. After the initial 12-month period, the Omega Fund is redeemable with 60 days' notice at the end of each calendar year-end, and the Beach Point Fund is redeemable with 60 days' notice at the end of each calendar quarter.

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BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 9 - PENSION PLAN AND POSTRETIREMENT HEALTH BENEFITS (continued)

The objective of the Omega Fund is to generate current income and attract risk-adjusted returns by investing in a variety of structured products and credit instruments with expected volatility generally below that of the equity markets. The majority of the Omega Fund's investments are in common stocks, corporate bonds and collateralized loan obligations. The Beach Point Fund's investment objective is to protect principal and achieve superior total return through a portfolio of high yield securities, including bonds and bank debt, stressed and distressed securities, undervalued equities, short-selling of debt and equity securities and, to a lesser extent, "special situation" investing. While both alternative investment funds are reported at net asset value, as a practical expedient for estimating fair value, funds which have redemption restrictions that exceed a 90-day time period are classified as Level 3 measurements. There are no outstanding funding commitments to either of the funds as of September 30, 2016 and 2015.

The fair values of the Hospital's pension plan assets, by asset category, are as follows for the years ended September 30, 2016 and 2015:

	2016			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Money market funds	\$ 832,068	\$ -	\$ -	\$ 832,068
Equities:				
Mutual funds	48,507,935	-	-	48,507,935
Alternative investment funds	<u>-</u>	<u>-</u>	<u>5,613,509</u>	<u>5,613,509</u>
 Total	 <u>\$ 49,340,003</u>	 <u>\$ -</u>	 <u>\$ 5,613,509</u>	 <u>\$ 54,953,512</u>
	2015			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Money market funds	\$ 129,603	\$ -	\$ -	\$ 129,603
Equities:				
Mutual funds	44,716,736	-	-	44,716,736
Alternative investment funds	<u>-</u>	<u>-</u>	<u>5,320,602</u>	<u>5,320,602</u>
 Total	 <u>\$ 44,846,339</u>	 <u>\$ -</u>	 <u>\$ 5,320,602</u>	 <u>\$ 50,166,941</u>

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BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 10 - OTHER EMPLOYEE BENEFIT PLANS

The Hospital's employees are eligible to participate in a 403(b) plan, which requires that employees work a minimum 1,000 hours per year beginning on January 1 to remain eligible. Employees are eligible to participate at their hire date and must be employed on December 31 to receive employer contributions. As of September 30, 2016 and 2015, the Hospital recorded a liability for their anticipated discretionary participant contribution match to the participants of the 403(b) plan, which is included within accrued payroll and other related expenses on the balance sheets. The Hospital incurred \$473,750 and \$246,836 of expense related to its 403(b) plan for the years ended September 30, 2016 and 2015, respectively.

NOTE 11 - AMOUNTS DUE FROM AFFILIATES AND RELATED PARTIES

The following are the balances due from affiliates as of September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Bristol Health Care, Inc. and Subsidiary	\$ 1,719,873	\$ 2,204,009
Bristol Hospital Development Foundation	174,953	-
Bristol Hospital EMS, LLC	<u>237,692</u>	<u>324,793</u>
Total	<u>\$ 2,132,518</u>	<u>\$ 2,528,802</u>

The Hospital allocates employee and management expenses to related entities based on direct costs incurred, in addition to allocated general overhead. The Hospital provided rental space to related entities, with revenues of approximately \$515,000 and \$408,000 in 2016 and 2015, respectively, which is included in other operating revenues.

NOTE 12 - MALPRACTICE AND GENERAL INSURANCE

In 2009, the Hospital established a self-insurance malpractice trust to provide malpractice insurance coverage for the Hospital. The Hospital has established a trust for the purpose of setting aside assets for self-insurance purposes. The self-insurance malpractice trust provides for a claims-made policy covering \$2 million per claim and \$6 million in the aggregate.

In addition, the Hospital has a \$15 million excess policy with an independent insurance company. Under the trust agreement, the trust assets can only be used for payment of professional and general liability losses, related expenses and the cost of administering the trust.

The assets of, and contributions to the trust are reported in the accompanying financial statements as assets limited as to use. Income from trust assets and administrative costs are reported in the accompanying statements of operations and changes in net assets, as other income. The \$4,821,905 and \$4,418,234 of assets which reside in the trust, as of September 30, 2016 and 2015, respectively are included within the Hospital's days cash on hand debt covenant test, as the Hospital's Board of Directors can terminate this trust at anytime and utilize these funds for operating purposes.

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BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 12 - MALPRACTICE AND GENERAL INSURANCE (continued)

The Hospital's malpractice liabilities, determined with the assistance of an independent actuary, as of September 30, 2016 and 2015 were estimated at \$2,872,000 and \$3,003,865, respectively, which are included within other accrued liabilities on the balance sheet. Included in this liability is an estimated incurred but not reported claim reserve, as the Hospital currently has a claims-made policy. In addition, the Hospital has recorded a liability and related recoverable based on estimates of any malpractice or general liability claims in excess of the self-insured retention.

NOTE 13 - SELF-INSURANCE OF WORKERS' COMPENSATION

The Hospital self-insures workers' compensation claims with a retention of the first \$350,000 per claim. The Hospital has also purchased excess liability insurance, which provides coverage for workers' compensation claims in excess of \$350,000 per claim. The self-insurance plan is unfunded. During the year, potential losses from asserted and unasserted claims identified by the Hospital's third-party administrator and accrued based upon estimates that incorporate the Hospital's past experience, as well as the nature of each claim or incident and relevant trend factors. The Hospital's year-end workers' compensation reserve, as estimated by third-party administrator and the Hospital's management in conjunction with its independent actuaries, is included in other accrued liabilities on the balance sheets and is discounted at 3.0% in 2016 and 2015, respectively. The balances as of September 30, 2016 and 2015 are \$1,812,738 and \$1,436,665, respectively.

NOTE 14 - CONTINGENCIES

Malpractice claims that fall within the Hospital's malpractice insurance have been asserted against the Hospital by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. There are also known incidents that have occurred through September 30, 2016 and 2015 that may result in the assertion of additional claims. Hospital management has accrued its best estimate of these contingent losses.

The Hospital is a party to various lawsuits and inquiries by various regulatory agencies in the normal course of its business. Management believes that the lawsuits and inquiries will not have a material adverse effect on its balance sheets, statements of operations and changes in net assets or cash flows.

NOTE 15 - FUNCTIONAL EXPENSES AND NON-OPERATING INCOME

The Hospital provides general health care services to residents primarily within their geographic location. Functional expenses related to their operating activities for the fiscal years ended September 30, 2016 and 2015, are as follows:

	<u>2016</u>	<u>2015</u>
Healthcare services	\$ 115,819,173	\$ 112,918,043
General and administrative	<u>24,324,531</u>	<u>23,715,230</u>
Total	<u>\$ 140,143,704</u>	<u>\$ 136,633,273</u>

(Continued)

BRISTOL HOSPITAL, INCORPORATED
NOTES TO THE STATEMENTS
For the Years Ended September 30, 2016 and 2015

NOTE 15 - FUNCTIONAL EXPENSES AND NON-OPERATING INCOME (continued)

Non-operating income for the years ended September 30, 2016 and 2015, consists of:

	<u>2016</u>	<u>2015</u>
Income, gains and (expenses):		
Interest and dividend income	\$ 970,096	\$ 826,403
Net realized gains on securities	50,209	25,677
Gain on equity in joint ventures	269,593	186,842
Expenses	<u>(219,690)</u>	<u>(243,756)</u>
Total	<u>\$ 1,070,208</u>	<u>\$ 795,166</u>

NOTE 16 - ASSET RETIREMENT OBLIGATIONS

FASB ASC 410, "*Asset Retirement and Environmental Obligations*," addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets, such as asbestos containing facilities, when the amount of the liability can be reasonably estimated. Management currently believes that certain facilities under their control could require a fair market value assessment of their Asset Retirement Obligation (ARO). As of September 30, 2016 and 2015, the Hospital has recorded an ARO related to asbestos contamination in buildings of \$604,800. Management will continue to monitor its exposure for asbestos removal, and adjust its ARO as necessary.