SOUTHEASTERN REGIONAL MEDICAL CENTER AND RELATED ORGANIZATIONS

Financial Statements

For the Years Ended
September 30, 2016 and 2015

Southeastern Regional Medical Center and Related Organizations
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September 30, 2016 and 2015

S. Preston Douglas & Associates, LLP

CERTIFIED PUBLIC ACCOUNTANTS

MEMBERS
American Institute of CPAs
N. C. Association of CPAs

Independent Auditor's Report

To the Board of Trustees
Southeastern Regional Medical Center
and Related Organizations
Lumberton, North Carolina

We have audited the accompanying combined financial statements of Southeastern Regional Medical Center and Related Organizations (a North Carolina nonprofit health care corporation) which comprise the combined balance sheets as of September 30, 2016 and 2015, and the related combined statements of operations, combined statements of changes in net assets, combined statements of cash flows for the years then ended, and the related notes to the combined 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 audits to obtain reasonable assurance about whether the financial statements are free of 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

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

S. Preston Douglas + Associates, LLP

Lumberton, North Carolina
December 28,2016

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Southeastern Regional Medical Center and Related Organizations
Combined Balance Sheets
September 30, 2016 and 2015

	2016	2015
Assets		
Current assets		
Cash and cash equivalents	$ 11,826,284	$ 18,034,482
Current portion of assets limited as to use	8,892,120	8,455,095
Patient accounts receivable, net of allowance for doubtful accounts of $106,854,972 in 2016 and $108,060,005 in 2015	50,247,799	42,266,400
Other receivables	8,470,160	3,568,786
Inventories	7,820,191	7,260,605
Prepaid expenses	1,975,425	1,481,094
Total current assets	89,231,979	81,066,462
Property and equipment, net	177,292,785	172,554,003
Other assets		
Investments, assets limited as to use, net of current portion	117,520,988	128,293,514
Long-term investments	1,712,872	3,436,593
Other assets	1,699,371	1,801,764
Total other assets	120,933,231	133,531,871
Total assets	$ 387,457,995	$ 387,152,336
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term debt and capital leases	$ 3,941,116	$ 4,396,763
Accounts payable	5,723,364	5,118,539
Accrued expenses	24,974,762	25,005,211
Estimated third-party payer settlements	6,564,065	11,886,537
Total current liabilities	41,203,307	46,407,050
Long-term liabilities, net of current portion:		
Long-term debt and capital leases	53,605,463	59,121,304
Accrued pension expense	22,150,977	21,574,807
Total long-term liabilities, net of current portion	75,756,440	80,696,111
Total liabilities	116,959,747	127,103,161
Net assets		
Unrestricted	267,032,811	256,820,081
Temporarily restricted	954,440	868,048
Permanently restricted	2,510,997	2,361,046
Total net assets	270,498,248	260,049,175
Total liabilities and net assets	$ 387,457,995	$ 387,152,336

See accompanying notes.

Southeastern Regional Medical Center and Related Organizations
Combined Statements of Operations
For the Years Ended September 30, 2016 and 2015

	2016	2015
Unrestricted revenue and other support		
Net patient service revenue	$ 378,851,839	$ 377,395,132
Provision for bad debts	(74,484,760)	(79,028,399)
Net patient service revenue less provision for bad debts	304,367,079	298,366,733
Other revenue	12,533,202	11,012,354
Total unrestricted revenue and other support	316,900,281	309,379,087
Operating expenses		
Salaries and benefits	168,700,548	164,189,938
Medical supplies and drugs	57,462,252	53,788,228
Insurance	1,234,403	1,534,393
Depreciation and amortization	19,040,204	17,760,367
Interest expense	1,791,493	2,016,162
Other expenses	65,440,265	64,562,000
Total operating expenses	313,669,165	303,851,088
Operating income	3,231,116	5,527,999
Nonoperating gains (losses)		
Interest and dividends	4,811,839	4,595,375
Realized gains (losses)	1,752,821	1,720,855
Unrealized gains (losses)	2,481,080	(6,291,453)
Investment fees	(546,959)	(686,024)
Total nonoperating gains	8,498,781	(661,247)
Excess of unrestricted revenue and other support over expenses	$ 11,729,897	$ 4,866,752

See accompanying notes.

Southeastern Regional Medical Center and Related Organizations
Combined Statements of Changes in Net Assets
For the Years Ended September 30, 2016 and 2015

	2016	2015
Unrestricted net assets		
Excess of unrestricted revenue and other support over expenses	$ 11,729,897	$ 4,866,752
Pension adjustment	(1,486,440)	(11,142,472)
Net assets released from restrictions	3,404	1,416,774
Increase (decrease) in unrestricted net assets	10,246,861	(4,858,946)
Temporarily restricted net assets		
Contributions	764,900	279,639
Net assets released from restrictions - operations	(709,235)	(57,688)
Net assets released from restrictions - property and equipment	(3,404)	(1,416,774)
Increase (decrease) in temporarily restricted net assets	52,261	(1,194,823)
Permanently restricted net assets		
Restricted contributions, net of expenses	6,676	38,378
Investment income	143,275	(25,351)
Increase (decrease) in permanently restricted net assets	149,951	13,027
Increase (decrease) in net assets	10,449,073	(6,040,742)
Net assets, beginning of year	260,049,175	266,089,917
Net assets, end of year	$ 270,498,248	$ 260,049,175

See accompanying notes.

Southeastern Regional Medical Center and Related Organizations
Combined Statements of Cash Flows
For the Years Ended September 30, 2016 and 2015

	2016	2015
Cash flows from operating activities		
Increase (decrease) in net assets	$ 10,449,073	$ (6,040,742)
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities:		
Depreciation and amortization	19,040,204	17,760,367
Provision for bad debts	74,484,760	79,028,399
Net realized and unrealized gains on investments	(4,233,901)	4,570,598
Amortization of original issue discount, premium and bond issue costs	(100,105)	(100,104)
Cash flows from (increase) decrease in:		
Receivables	(87,367,533)	(76,722,886)
Inventories	(559,586)	(1,838,397)
Prepaid expenses	(494,331)	356,536
Cash flows from increase (decrease) in:		
Accounts payable	604,825	(1,934,260)
Accrued expenses	(30,449)	1,340,797
Accrued pension expense	576,170	9,343,048
Third-party payer settlement	(5,322,472)	(5,776,037)
Net cash provided (used) by operating activities	7,046,655	19,987,319
Cash flows from investing activities		
Purchase of property and equipment	(23,778,986)	(19,465,699)
(Increase) decrease in assets limited as to use	14,569,402	2,478,988
(Increase) decrease in other long-term investments	1,723,721	1,609,891
Net cash provided (used) by investing activities	(7,485,863)	(15,376,820)
Cash flows from financing activities		
Principal payments on capital lease obligations	(3,668,990)	(1,905,169)
Principal payments on long-term debt	(2,100,000)	(2,040,000)
Net cash provided (used) by financing activities	(5,768,990)	(3,945,169)
Net increase (decrease) in cash and cash equivalents	(6,208,198)	665,330
Cash and cash equivalents, beginning of year	18,034,482	17,369,152
Cash and cash equivalents, end of year	$ 11,826,284	$ 18,034,482

Cash paid for interest in 2016 and 2015 was $1,714,679 and $2,050,342, respectively.

Capital lease obligation incurred for moveable equipment in 2015 was $911,177.

See accompanying notes.

Note A - Organization and Summary of Significant Accounting Policies

Organization

Southeastern Regional Medical Center and Related Organizations (the Hospital) is a not-for-profit health care corporation, exempt from federal income tax under Section 501(a) of the Internal Revenue Code (the Code) as an organization described in Section 501(c)(3) whereby only unrelated business income as defined by Section 512(a)(1) of the Code, is subject to federal income tax. The Hospital, located in Lumberton, North Carolina, provides inpatient, outpatient, and emergency care services through acute care as well as primary and specialty care services for residents of southeastern North Carolina.

Combination Policy

The accompanying combined balance sheets, statements of operations, statements of changes in net assets, and statements of cash flows, referred to as "Southeastern Regional Medical Center and Related Organizations," include the accounts of Southeastern Regional Medical Center, Health Horizons, Inc., Southeastern Regional Medical Center Foundation, and Southeastern Regional Physician Services, all of which are under common management. Intercompany balances and transactions have been eliminated in combination.

Controlled Affiliates of the Hospital

The following entities are controlled affiliates of the Hospital:

Health Horizons, Inc. is a 501(c)(3) not-for-profit corporation. Health Horizons, Inc. includes Southeastern Home Care Services which offers a complete range of skilled nursing care along with physical, occupational, and speech therapy services, as well as case management for eligible people in their homes; Southeastern Home Health which provides services after hospitalization; Southeastern Home Medical Equipment which provides medical, respiratory, and rehabilitation equipment and supplies and Southeastern Hospice which offers medical care and comfort for patients. The Hospital is the sole member of Health Horizons, Inc.

Southeastern Regional Medical Center Foundation (the Foundation) is a 501(c)(3) not-for-profit corporation. The purpose of the Foundation is to: (a) receive grants, bequests, donations, and contributions on behalf of; (b) provide fund-raising and other support to; and (c) make contributions to the Hospital and its related tax-exempt corporations. The Hospital is the sole member of the Foundation.

Southeastern Regional Physician Services (Physician Services) is a 501(c)(3) not-for-profit corporation. The purpose of Physician Services is to operate primary care, specialty, and urgent care clinics throughout Robeson, Bladen, Cumberland, and Scotland counties. The Hospital is the sole member of Physician Services.

Other Affiliates of the Hospital

The following entity is an affiliate of the Hospital, but is not controlled and is, therefore, not included within these combined financial statements.

Southeastern Ambulatory Surgery Center, LLC (ASC) was formed to operate an ambulatory surgery center focused on providing same-day surgical care, including diagnostic and preventive procedures to patients and is owned jointly by the Hospital and physicians practicing in the Lumberton area.

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 and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

Cash and Cash Equivalents

Cash and cash equivalents include certain investments in highly liquid debt instruments with a maturity of three months or less, excluding amounts whose use is limited by board designation or other arrangements under trust agreements or with third-party payers.

Note A - Organization and Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents (continued)

The Hospital maintains cash and cash equivalents on deposit at financial institutions, which at times exceed the limits insured by the Federal Deposit Insurance Corporation. This exposes the Hospital to potential risk of loss in the event the financial institution becomes insolvent.

Allowance for Doubtful Accounts, Provision for Bad Debts

The Hospital records an allowance for doubtful accounts and bad debt expense for estimated losses resulting from non-payment for accounts receivable for services from patients. The Hospital accounts for uncollectible accounts receivable balances from third-party commercial insurers as reductions to net patient service revenue rather than bad debt expense. Management routinely evaluates account collection history, economic conditions, and trends in health care coverage in determining the sufficiency of the allowance for doubtful accounts and provision for bad debts. Accounts receivable are written off against the allowance for doubtful accounts when management determines that recovery is unlikely and collection efforts cease.

Assets Limited as to Use and Investments

Assets limited as to use are limited principally to certain funds established to be held and invested by a trustee. These funds are related to the issuance of the Hospital's Revenue Bonds, investments for capital improvements set aside by the Board of Trustees (the Board) over which the Board retains control and may at its discretion subsequently use for other purposes, self-insurance arrangements, and certain permanently restricted endowment assets.

The fair values of individual investments are based on quoted market prices of individual securities or investments or estimated amounts using quoted market prices of similar investments. Realized and unrealized investment returns from all unrestricted investments and assets limited as to use are included in the combined statements of operations as part of nonoperating gains and losses. Investment income (loss) on investments of temporarily or permanently restricted assets is added to or deducted from the appropriate restricted fund balance if the income is restricted. The cost of securities sold is based on the specific-identification method. Investments are classified as either current or noncurrent based on maturity dates and availability for current operations.

Substantially all investments are classified as trading securities, with unrealized gains and losses included in excess of unrestricted revenue and other support in excess of expenses.

Investment Risk and Uncertainties

The Hospital invests in professionally managed portfolios that contain corporate bonds, United States Government obligations, municipal obligations, asset-backed securities, marketable equity securities, and money market funds. Such investments are exposed to various risks, such as interest rate, market, and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term would materially affect investment balances and the amounts reported in the financial statements.

Inventory

Inventories of materials and supplies are stated at the lower of cost (first-in, first-out method) or market.

Property and Equipment

Property and equipment acquisitions are recorded at cost. Items acquired by gift are recorded at fair value at the time of acquisition. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed on the straight-line method.

Asset Impairment

The Hospital considers whether indicators of impairment are present and performs the necessary tests to determine if the carrying value of an asset is appropriate. Impairment write-downs are recognized in operating income at the time the impairment is identified. There was no impairment of long-lived assets in 2016 or 2015.

Note A - Organization and Summary of Significant Accounting Policies (continued)

Other Assets

Administrative, legal, financing, underwriting discount and other miscellaneous expenses associated with the issuance of the Series 2005 and Series 2012 Hospital Revenue Bonds have been capitalized and are being amortized over the repayment period of the bond issue for the years ending September 30, 2016 and 2015. The amortization expense of deferred debt issue costs was $102,394 and $102,394 for the years ended September 30, 2016 and 2015, respectively.

Net Assets

Resources are classified for reporting purposes into three net asset categories as permanently restricted, temporarily restricted, and unrestricted according to the absence or existence of board designations or donor-imposed restrictions. Permanently restricted net assets have been restricted by donors to be maintained by the Hospital in perpetuity to provide a permanent source of income. Temporarily restricted net assets are those assets whose use by the Hospital has been limited by donors to a specific time period or purpose.

Net Patient Service Revenue

The Hospital has agreements with third-party payers that provide for payments to the Hospital for patient services 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 estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated adjustments under reimbursement agreements with third-party payers. Estimated adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

The Hospital's revenues may be subject to adjustment as a result of examination by government agencies or contractors and as a result of differing interpretation of government regulations, medical diagnosis, charge coding, medical necessity, or other contract terms. The resolution of these matters, if any, often is not finalized until subsequent to the period during which the services were rendered.

Financial Assistance and Community Benefits

In support of its mission, the Hospital provides charity care to patients who lack financial resources and are deemed to be medically indigent. Policies have been established that define financial assistance and provide guidelines for assessing a patient's ability to pay. Evaluation procedures for financial assistance qualification have been established for those situations when previously unknown financial circumstances are revealed or when incurred charges are significant when compared to the individual patient's income and/or net assets. Because the Hospital does not pursue collection of amounts determined to qualify as financial assistance, they are not reported as revenue in the accompanying combined statements of operations and changes in net assets.

In addition, the Hospital provides services to other medically indigent patients under various state Medicaid programs that pay providers amounts less than the costs incurred for the services provided to recipients.

Under current accounting standards, the Hospital is required to report the cost of providing financial assistance. The cost of financial assistance provided by the Hospital is based on the Hospital's aggregate cost to charge ratio and totaled $9,086,253 and $7,977,366 in 2016 and 2015, respectively.

In addition to its Financial Assistance policy, the Hospital has a long-standing commitment of supporting the community through the provision of outreach services designed to address identified health and social issues. Specifically, the Hospital provides a variety of screening and early detection tests, wellness activities, social support services and educational seminars. A majority of these services are provided at either nominal or no cost to community members.

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 a stipulated

Note A - Organization and Summary of Significant Accounting Policies (continued)

Donor-Restricted Gifts (continued)

time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets if restricted for capital or reported in the statements of operations as net assets released from restrictions if restricted for operating purposes. Donations received with no restrictions and donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying combined statements of operations as other operating revenues.

Unconditional promises to give cash or other assets are reported as other receivables and contributions with the appropriate net asset category. An allowance for uncollectible pledges receivable is estimated based on historical experience and other collection indicators.

Excess of Unrestricted Revenue and other Support over Expenses

The accompanying combined statements of operations and changes in net assets include the excess of revenue over expenses. Changes in unrestricted net assets, which are excluded from the excess of revenue over expenses, consistent with industry practice, include contributions of long-lived assets (including assets acquired using contributions, which, by donor restriction, are to be used for the purposes of acquiring such assets) and changes in pension liabilities.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Contracts with Customers (Topic 606).* This ASU establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts and customers. Particularly, 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 goods or services. ASU 2014-09 is effective for fiscal year 2019, and early adoption is permitted beginning in fiscal year 2018. The Hospital expects to record a decrease in net patient service revenue related to self-pay patients and a corresponding decrease in bad debt expense upon the adoption of this standard.

In April 2015, the FASB issued ASU No. 2015-03, *Interest-Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.* The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This guidance is effective for fiscal year 2017. The guidance is not expected to materially impact the Hospital's combined results of operations, net assets, or cash flows.

In February 2016, the FASB issued SSU No. 2016-02, *Leases* (ASU 2016-02). This ASU amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets. The adoption of ASU 2016-02 is effective in fiscal year 2020, and will require application of the new guidance at the beginning of the earliest comparable period presented. Early adoption is permitted. The Hospital is currently assessing the impact of the adoption of ASU No, 2016-02, which is expected to increase the Hospital's assets and liabilities but not have a significant impact on the results of operations.

The FASB issued ASU No. 2016-14, *Not-for-Profit Entities (ASU 2016-14),* which amends the requirements for financial statements and notes in Topic 958, Not-for-Profit Entities (NFP), and requires a NFP to:

- Reduce the number of net asset classes presented from three to two, with donor restrictions and with donor restrictions;
- Require all NFP's to present expenses by their functional and their natural classifications in one location in the financial statements;
- Require NFP's to provide quantitative and qualitative information about management of liquid resources and availability of financial assets to meet cash needs within one year of the balance sheet date;

The adoption of ASU 2016-14 is effective in fiscal year 2019, and is applied retrospectively in the year of adoption. The Hospital does not anticipate that the adoption of this ASU will have a material impact on its financial position and results of operations.

Note B – Investments and Assets Limited as to Use

Assets measured at fair value are presented in the accompanying combined balance sheet under the following classifications:

	2016	2015
Assets limited as to use, current	$ 8,892,120	$ 8,455,095
Assets limited as to use, noncurrent	117,520,988	128,293,514
Long-term investments	1,712,872	3,436,593
	$ 128,125,980	$ 140,185,202

Current and long- term assets whose use is limited for 2016 and 2015 are classified as follows:

	2016	2015
Board designated assets, primarily construction and capital	$ 101,053,613	$ 125,958,765
Board designated assets, Epic escrow	14,132,476	-
Bond indenture agreement assets restricted by trustees	2,334,899	2,334,749
Self-insurance assets board designated	8,892,120	8,455,095
	$ 126,413,108	$ 136,748,609

Assets Limited as to Use
The composition of assets limited as to use at September 30 is set forth in the following table. Investments are stated at fair value.

	2016	2015
By board for capital improvements and EPIC:		
Cash and short-term investments	$ 1,231,618	$ 1,807,752
Corporate bonds and other fixed income	54,757,407	66,424,210
Equity securities	36,889,163	35,222,438
Mutual funds	22,307,901	22,504,365
	115,186,089	125,958,765
Held by trustee:		
Cash and short-term investments	2,334,899	2,334,749
Self-insurance program:		
Cash and short-term investments	111,917	167,675
Equity securities	4,234,794	4,137,691
Corporate bonds and other fixed income	4,545,409	4,149,729
	8,892,120	8,455,095
Total investments, assets limited as to use	$ 126,413,108	$ 136,748,609

Investment income and gains for assets limited as to use and other investments, including temporarily and permanently restricted assets, are comprised of the following for the years ending September 30:

	2016	2015
Interest, dividends, and gains (losses) permanently restricted	$ 143,275	$ (25,351)
Interest and dividend income	4,811,839	4,595,375
Realized gains (losses) on trading securities	1,752,821	1,720,855
Unrealized gains (losses) on trading securities	2,481,080	(6,291,453)
Totals	$ 9,189,015	$ (574)

Note C – Fair Value Measurements

The Hospital follows the requirements of ASC 820 in regards to measuring the fair value of certain assets and liabilities as well as disclosures about fair value measurements. ASC 820 defines fair value as the price that would be received for an asset or paid for a transfer of a liability in an orderly transaction on the measurement date.

The methodologies used to determine fair value of assets and liabilities reflect market participant objectives and are based on the applications of a three-level valuation hierarchy that prioritizes observable market inputs over unobservable inputs. The three levels are defined as follows:

Note C – Fair Value Measurements (continued)

- Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, 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 for substantially the same term of the assets or liabilities.
- Level 3 – Inputs are unobservable inputs for the assets or liabilities, which are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value instrument.

The following tables present the financial instruments measured at fair value on a recurring basis as of September 30, 2016 and 2015:

	Fair Value as of September 30, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**
Assets:				
Cash and cash equivalents	$ 11,826,284	$ -	$ -	$ 11,826,284
Trading securities and other assets whose use is limited:				
Cash and cash equivalents	3,678,434	-	-	3,678,434
Corporate bonds and other fixed income	-	59,302,816	-	59,302,816
Equity securities	41,123,957	-	-	41,123,957
Mutual funds	22,307,901	-	-	22,307,901
Other	-	-	1,712,872	1,712,872
Total	$ 78,936,576	$ 59,302,816	$ 1,712,872	$ 139,952,264

	Fair Value as of September 30, 2015			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	$ 18,034,482	$ -	$ -	$ 18,034,482
Trading securities and other assets whose use is limited:				
Cash and cash equivalents	4,310,176	-	-	4,310,176
Corporate bonds and other fixed income	-	70,573,939	-	70,573,939
Equity securities	39,360,129	-	-	39,360,129
Mutual funds	22,504,365	-	-	22,504,365
Other	-	-	3,436,593	3,436,593
Total	$ 84,209,152	$ 70,573,939	$ 3,436,593	$ 158,219,684

Valuation Techniques and Inputs

Investments - The fair value of Level 1 investments, which primarily includes equity securities, corporate bonds, mutual funds, and cash, is based on quoted market prices that are valued on a daily basis. Level 2 investments consist of U.S. government securities, corporate bonds and other fixed income investments. The fair value of the U.S. government securities and corporate bonds is established based on values obtained from nationally recognized pricing services that value the investments based on similar securities and matrix pricing of similar quality and maturity securities. Level 3 investments are valued at cost.

The carrying values of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other liabilities, and short-term borrowings are reasonable estimates of their fair values due to the short-term nature.

Note C – Fair Value Measurements (continued)

The estimated fair value of the long-term debt, including the current portion, was $57,546,579 and $63,518,067 at September 30, 2016 and 2015, respectively. The fair value of this Level 2 liability is based on quoted market prices for the same or similar issues and the relationship of those bond yields with various market indices.

The fair value of pledges receivable, a Level 2 asset, is based on discounted cash flow analysis and approximated the carrying value of $303,984 and $141,126 at September 30, 2016 and 2015, respectively.

Note D - Property and Equipment

A summary of property and equipment at September 30 follows:

	2016	2015
Land	$ 5,306,117	$ 5,296,117
Land improvements	4,119,781	4,109,816
Buildings and improvements	171,900,088	166,252,687
Furniture and fixtures	23,827,119	23,804,122
Fixed equipment	17,251,719	19,826,574
Moveable equipment	148,269,724	138,106,038
Automobiles	1,874,538	1,831,696
Rental equipment	2,365,502	2,159,759
	374,914,588	361,386,809
Less - Accumulated depreciation and amortization	210,696,314	193,177,682
	164,218,274	168,209,127
Construction in progress	13,074,511	4,344,876
Property and equipment, net	$ 177,292,785	$ 172,554,003

Construction in progress consists of building construction and renovations and costs associated with a new system for integrated electronic health records. As these projects are completed, the related assets are transferred out of construction in progress and into the appropriate asset category and are depreciated over the applicable useful lives.

Depreciation expense for the years ended September 30, 2016 and 2015 amounted to $19,040,204 and $17,760,367, respectively.

Note E – Self-Insurance Liabilities and Related Insurance Recoverables

The Hospital retains certain levels of professional and general liability risks. For those risks, the Hospital has established trust funds to pay claims and related costs. The Hospital is required to maintain cash and investments sufficient to fund actuarially determined tail liabilities. There are known claims and incidents that may result in the assertion of additional claims, as well as claims from unknown incidents that may be asserted arising from services provided to patients. The Hospital has employed independent actuaries to estimate the ultimate costs, if any, of the settlement of such claims. Accrued malpractice losses in the amount of $6,165,285 and $6,992,124 for 2016 and 2015, respectively, are included in current liabilities to cover the Hospital's malpractice exposure.

Note F - Long-Term Debt

Series 2005

On September 15, 2005, North Carolina Medical Care Commission issued Bonds on behalf of Southeastern Regional Medical Center with a face amount of $20,000,000. The proceeds were used for the acquisition and construction of the heart center and the 7th floor of the bed tower.

Series 2012

In October 2012, the North Carolina Medical Care Commission issued Series 2012 Revenue Refunding Bonds on behalf of Southeastern Regional Medical Center with a face amount of $40,210,000. The proceeds of the 2012 Bonds were used to refund the Series 1999 Revenue Bonds and the Series 2002 Revenue Bonds and to pay certain expenses incurred in connection with the issuance and sale of the 2012 Bonds. The 2012 Bonds were issued with a premium of $4,049,963, which is being amortized over the life of the bonds. The accumulated amortization was $809,992 and $607,494 at September 30, 2016 and September 30, 2015, respectively.

Note F – Long-Term Debt (continued)

Capital Leases

On December 3, 2013, the Hospital entered into a lease agreement with General Electric Capital Corporation for the acquisition of linear accelerator equipment in the amount of $2,877,878. The agreement was collateralized by the equipment. The lease was payable in 72 monthly payments of 44,730, including interest imputed at 3.775%. On October 20, 2015, the lease was bought out and a final payment made.

The Hospital has entered into various lease agreements with Winthrop Resource Corporation to secure information technology equipment dating from 2012 through 2015. The leases are payable over periods of 44 to 60 monthly payments. The total annual payment is approximately $1,628,714, including interest imputed at 7.1%. The equipment is included in property and equipment on the combined balance sheets and the depreciation of the assets is included in depreciation expense in the amount of $1,641,772 for the year ended September 30, 2016 and $1,550,655 for the year ended September 30, 2015.

Long-term debt as shown on the balance sheets consisted of the following at September 30:

	2016	2015
Series 2005 Hospital Revenue Bonds; principal maturing in varying annual amounts ranging from $600,000 to $1,085,000; interest rate variable, controlled by 91-day Treasury Bill rate	$ 17,635,000	$ 18,250,000
Series 2012 Hospital Revenue Refunding Bonds; principal maturing in varying annual amounts ranging from $1,440,000 to $2,860,000; interest rates ranging from 2% to 5%	33,495,000	34,980,000
Unamortized premium, net	3,239,971	3,442,469
	36,734,971	38,422,469
Capital leases	3,176,608	6,845,598
Totals	57,546,579	63,518,067
Less current portion bond principle and capital leases	(3,738,618)	(4,194,265)
Less current portion bond premium amortization	(202,498)	(202,498)
Long-term portion	$ 53,605,463	$ 59,121,304

Scheduled principal and interest repayments on long-term debt, excluding premium, for the next five years are as follows:

	Capital Lease Obligation		Long-term debt	
	Principal	Interest	Principal	Interest
2017	$ 1,573,618	$ 55,096	$ 2,165,000	$ 1,750,004
2018	1,192,372	36,595	2,245,000	1,679,463
2019	302,812	17,383	2,320,000	1,605,588
2020	107,806	1,398	2,400,000	1,529,649
2021	-	-	2,495,000	1,449,437

Under the terms of the Bond Indenture, the Hospital is required to maintain certain deposits with a trustee. Such deposits are included with assets whose use is limited in the financial statements. The provisions under the Bond Indenture require the Hospital to maintain reporting, financial, and other covenants. The Hospital was in compliance with these provisions at September 30, 2016.

The Hospital was in compliance with these provisions at September 30, 2015, except for certain reporting requirements under the terms of the bond indenture, which have since been cured.

Note G - Pension Benefits

The Hospital has a defined benefit plan that covers substantially all of its employees. The plan benefits are based on years of service and the employees' compensation during the last five years of covered employment. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future. The plan was amended, effective January 1, 2005, so that no eligible employee hired or rehired on or after

January 1, 2005 can become a participant in the plan or accrue any benefits under the plan. Effective December 31, 2009, the plan was amended to cease benefit accruals.

The following table sets forth the changes in benefit obligations, changes in plan assets, and components of net periodic benefit cost for the years ended September 30:

	2016	2015
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 103,654,015	$ 100,175,093
Service cost	-	-
Interest cost	4,596,670	4,396,428
Actuarial (gain) loss	7,911,087	5,665,883
Benefits paid	(7,227,384)	(6,583,389)
Projected benefit obligation at end of year	$ 108,934,388	$ 103,654,015
Change in plan assets:		
Fair value of plan assets at beginning of year	$ 82,079,208	$ 87,943,334
Actual return on plan assets	8,931,587	(2,280,737)
Employer contributions	3,000,000	3,000,000
Benefits paid	(7,227,384)	(6,583,389)
Fair value of plan assets at end of year	86,783,411	82,079,208
Funded status	$ (22,150,977)	$ (21,574,807)
Amounts recognized in the balance sheet:		
Non-current liabilities	(22,150,977)	(21,574,807)
Total Asset/ (Liability)	$ (22,150,977)	$ (21,574,807)
Amounts recognized in Accumulated Other Comprehensive Income:		
Net transition (obligation)/ asset	$ -	$ -
Prior service (cost)/ credit	-	-
Net actuarial gain/ (loss)	(35,631,182)	(34,144,742)
Total	$ (35,631,182)	$ (34,144,742)

The accumulated benefit obligation for the plan was $103,654,015 and $100,175,093 at September 30, 2016 and 2015, respectively.

Components of Net Periodic Benefit Cost and Other Amounts Recognized in Other Comprehensive Income:

Net Periodic Benefit Cost:	2016	2015
Service costs	$ -	$ -
Interest cost in projected benefit obligation	4,596,670	4,396,428
Expected return on assets	(5,107,689)	(5,082,491)
Amortization of transition obligation (asset)	-	-
Amortization of prior service cost	-	-
Amortization of net (gain) loss	2,600,749	1,858,965
Curtailment expense	-	-
Net periodic benefit cost	$ 2,089,730	$ 1,172,902

The net transition obligation (asset), prior service cost (credit), and estimated net loss (gain) for the plan that are expected to be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are $0, $0, and $2,783,047, respectively.

Note G - Pension Benefits (continued)

Assumptions:	2016	2015
Weighted-average assumptions used to determine benefit obligation at September 30		
Discount rate	3.80%	4.53%
Expected long-term rate of return	6.00%	6.00%
Rate of compensation increase	N/A	N/A
Weighted-average assumptions used to determine net periodic benefit cost for years ended September 30		
Discount rate	4.53%	4.49%
Expected long-term return on plan assets	6.00%	6.00%
Rate of compensation increase	N/A	N/A

Plan assets have been invested in equities, fixed income, real estate, and money markets. The composition of plan assets for the past two years is shown below. The expected long-term rate of return of 6% has been determined by use of Aon Hewitt Investment Consulting's expectations of returns for various asset classes applied to the asset allocation listed below. Six percent is at the high end of the acceptable range. The intent of the investment policy is to add more liability-hedging assets over time, which will lead to a lower expected return over time. This will be monitored each year and the expectation is that the expected long-term rate of return will decline in future years.

Plan Assets
The composition of plan assets is as follows:

	Target Allocation	Percentage of Plan Assets September 30 2016	2015
Return-seeking securities	32-42%	41.5%	32.1%
Liability-hedging securities	68-58%	58.5%	67.9%

Investment policy guidelines for the Plan include a portfolio that will provide liquidity to meet the Plan's benefit payments and expenses payable from the Plan under ERISA, offer a reasonable probability of achieving a growth of assets that will assist in closing the Plan funding gap, and manage the Plan's assets in a liability framework. The mix of growth and liability matching assets is determined by the acceptable level of risk to the funded status.

The following table presents the Plan's financial instruments as of September 30, 2016 and 2015 measured at fair value on a recurring basis by the valuation hierarchy described in Note C:

	Plan Assets at Fair Value as of September 30, 2016			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	$ 925,497	$ -	$ -	$ 925,497
Mutual funds	-	85,823,491	-	85,823,491
	$ 925,497	$ 85,823,491	$ -	$ 86,748,988

	Plan Assets at Fair Value as of September 30, 2015			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	$ 485,147	$ -	$ -	$ 485,147
U.S. government and agency issues	-	2,698,541	-	2,698,541
Corporate bonds and other fixed income	-	55,314,490	-	55,314,490
Equity securities	21,513,121	-	-	21,513,121
Real estate	-	-	2,094,909	2,094,909
	$ 21,971,268	$ 58,013,031	$ 2,094,909	$ 82,079,208

Note G - Pension Benefits (continued)

Plan Assets (continued)

The fair value of Level 1 investments, which consists of equity securities and certain mutual funds, is based on quoted market prices and are value on a daily basis. Level 2 investments consist of U.S. government securities, corporate bonds and fixed income instruments. The fair value of the U.S. government securities and corporate bonds is established based on values obtained from nationally recognized pricing services that value the investments based on similar securities and matrix pricing of similar quality and maturity services. Level 3 investments consist of limited partnership interests in real estate and are based on net asset value.

Cash Flows

Contributions - The Hospital is not required to make a contribution to its pension plan in 2017.

Estimated Future Benefit Payments – The following benefit payments, which reflect future service, as appropriate, are expected to be paid:

2017	$	4,710,000
2018		5,174,000
2019		5,400,000
2020		5,524,000
2021		5,682,000
Years 2022 - 2026		30,498,000

Defined Contribution Plan

The Hospital has a defined contribution plan qualified under Internal Revenue Code Section 403(b) covering all employees. For employees hired before January 1, 2005, the Hospital matches 25% of the first 4% of compensation deferred by the employee, subject to Internal Revenue Service limitations.

For employees hired or rehired on or after January 1, 2005, there is a new enhanced 403 (b) plan. After a one year waiting period, the Hospital contributes 2% of each eligible employee's annual compensation to the plan, subject to a 3 year vesting period. In addition, the Hospital will match a percentage of the first 4% of compensation deferred by the employee based on years of service as of the immediately preceding December 31st, subject to Internal Revenue Service limitations. The percentages are 25% for the first 5 years of service, 50% for the next 5 years of service and 100% for each year of service thereafter. The amount of the contribution made by the Hospital is within its discretion and may vary. The Hospital's contributions to the 403(b) plans were $1,941,293 and $2,073,103 for 2016 and 2015, respectively.

Note H – Temporarily and Permanently Restricted Net Assets

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

		2016		2015
Healthcare services:				
Purchase of property and equipment	$	130,415	$	130,330
Operating expenses and charity care		824,025		737,718
	$	954,440	$	868,048

Permanently restricted net assets, the income from which is expendable to support research, education and other expenses, was $2,510,997 and $2,361,046 for September 30, 2016 and 2015, respectively.

Note I - Net Patient Service Revenue

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

Medicare - Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient non-acute services and defined capital and medical education costs related to

Medicare beneficiaries are paid based on a cost reimbursement methodology. The Hospital is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Medicare fiscal intermediary has audited the Hospital's Medicare cost reports through September 30, 2013.

Medicaid - Inpatient and outpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement methodology. The Hospital is reimbursed at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicaid fiscal intermediary. The Medicaid fiscal intermediary has audited the Hospital's Medicaid cost reports through September 30, 2013.

Revenue from the Medicare and Medicaid programs accounted for approximately 48.2% and 21.5%, respectively, of the hospital's net patient revenue for the year ended 2016, and 48.9% and 21.0%, respectively, of the hospital's net patient revenue for the year ended 2015. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

The Hospital also has entered into payment agreements with certain commercial insurance carriers, HMO's, and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established covered charges, and prospectively determined daily rates.

The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third party payer agreements. The mix of receivables from patients and third party payers consisted of the following at September 30:

	2016	2015
Medicare	28.4%	27.7%
Medicaid	23.6%	23.0%
Other third party payers	32.8%	34.8%
Self pay patients	15.2%	14.5%
	100.0%	100.0%

Note J – Functional Expenses

The Hospital provides general healthcare services primarily to residents within its geographic location. For the years ended September 30, 2016 and 2015, expenses related to providing these services were as follows:

	2016	2015
Healthcare services	$ 289,244,929	$ 277,131,604
Research and education	1,077,839	995,168
Fund-raising	339,609	329,200
General, administrative, and other	23,616,927	25,461,115
	$ 313,309,304	$ 303,917,087

Note K - Reclassifications

Certain amounts in the prior-year financial statements have been reclassified for comparative purposes to conform to the presentation in the current-year financial statements.

Note L - Commitments and Contingencies

Construction commitments. The Hospital has approved contracts for uncompleted construction and renovation with outstanding balances of $1,739,707 and $2,454,199 for the years ending September 30, 2016 and 2015, respectively.

Contract commitment. The Hospital has selected Epic for a single, integrated electronic health record (EHR) and revenue cycle management (RCM) system. The new system will replace the Hospital's two EHRs and various legacy systems currently in use, and will be a foundation for the system's clinical and financial operations over the next decade. Implementation began in May, 2016 with a targeted go-live date in November, 2017. Management plans to fund this project with excess cash flow, unrestricted reserves and potential new debt issuance in 2017.

Operating leases. The Hospital leases various equipment and facilities under operating leases expiring at various dates. Total rental expense in 2016 and 2015 for all operating leases was approximately $732,020 and $1,097,259, respectively.

The following is a schedule by year of future minimum lease payments under operating leases as of September 30, 2016, that have initial or remaining lease terms in excess of one year.

Year Ending September 30	Amount
2017	$ 736,937
2018	387,560
2019	120,776
2020	14,832
2021	-

Litigation. The Hospital is involved in litigation and regulatory investigations arising in the ordinary course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Hospital's future financial position or results from operations.

Transactions with affiliates The Hospital has entered into a loan commitment with First Citizens Bank, Lumberton, North Carolina, on behalf of Southeastern Ambulatory Surgery Center, LLC. It is a guarantor on a line of credit in the amount of $1,690,880 at September 30, 2016.

Note M – Related Party Transactions

The Hospital leases office space to Southeastern Ambulatory Center, LLC (ASC). The terms of the lease are for twenty years at an annual base rent of $384,880, plus actual common area maintenance charges. At September 30, 2016 the ASC owed the Hospital $552,283.

Note N– Subsequent Events

Management evaluation. Management has evaluated subsequent events through December 28, 2016, the date that the financial statements were available for issue.

Hurricane Matthew. On October 8, 2016, Hurricane Matthew devastated the City of Lumberton, Robeson County, and many surrounding counties. The Hospital estimates incremental costs associated with the hurricane in excess of $6 million dollars. Although the Hospital believes that much of these additional costs will be reimbursed by either insurance coverage for property damage and business interruption or by FEMA, the amount can not be reasonably estimated at this time.