Baxter Regional Health System

Independent Auditor's Report, Consolidated Financial Statements
and Supplementary Information

December 31, 2016 and 2015

BKD LLP
CPAs & Advisors

Baxter Regional Health System

December 31, 2016 and 2015

Contents

BKD LLP
CPAs & Advisors
400 W. Capitol Avenue, Suite 2500 // P.O. Box 3667 // Little Rock, AR 72203-3667
501.372.1040 // fax 501.372.1250 // bkd.com

Independent Auditor's Report

Board of Directors
Baxter Regional Health System
Mountain Home, Arkansas

We have audited the accompanying consolidated financial statements of Baxter Regional Health System (the System) and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Baxter Regional Health System and its subsidiaries as of December 31, 2016 and 2015, and the results of their operations, the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Our audits were performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary consolidating information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the consolidating financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

BKD, LLP

Little Rock, Arkansas
April 19, 2017

Baxter Regional Health System

Consolidated Balance Sheets

December 31, 2016 and 2015

Assets

	2016	2015
Current Assets		
Cash and cash equivalents	$ 10,182,303	$ 8,921,741
Short-term investments	12,059,066	9,680,236
Assets limited as to use – current	1,733,866	2,005,093
Patient accounts receivable, net of allowance; 2016 – $5,769,727; 2015 – $6,060,587	21,049,622	21,162,863
Supplies	5,903,515	5,982,224
Prepaid expenses and other	1,892,282	2,285,805
Estimated amounts due from third-party payers	824,626	891,035
Total current assets	53,645,280	50,928,997
Assets Limited as to Use		
Internally designated for capital improvements	39,952,003	36,081,516
Externally restricted by donors	13,168,249	12,362,649
Held by trustee under indenture agreement	6,689,346	7,880,255
Other	200,000	200,000
	60,009,598	56,524,420
Less amount required to meet current obligations	1,733,866	2,005,093
	58,275,732	54,519,327
Investments in and Advances to Equity Investees	60,009	170,327
Property and Equipment, at Cost		
Land and land improvements	7,873,754	7,355,002
Buildings and leasehold improvements	75,904,377	73,273,567
Equipment	126,305,043	123,865,098
Construction in progress	1,395,145	522,367
	211,478,319	205,016,034
Less accumulated depreciation	145,547,372	138,397,125
	65,930,947	66,618,909
Other Assets		
Long-term investments	60,000	60,000
Other	112,427	115,348
	172,427	175,348
Total assets	$ 178,084,395	$ 172,412,908

Liabilities and Net Assets

	2016	2015
Current Liabilities		
Current maturities of long-term debt	$ 4,197,718	$ 4,331,432
Accounts payable	7,607,605	6,038,112
Accrued expenses	9,420,920	8,487,268
Accrued interest	748,552	852,465
Estimated amounts due to third-party payers	4,874,604	4,314,635
Total current liabilities	26,849,399	24,023,912
Long-term Debt	55,718,363	58,236,599
Total liabilities	82,567,762	82,260,511
Net Assets		
Unrestricted		
Baxter Regional Health System	82,826,533	78,454,295
Noncontrolling interest	142,694	53,683
Total unrestricted net assets	82,969,227	78,507,978
Temporarily restricted	5,228,220	4,325,233
Permanently restricted	7,319,186	7,319,186
Total net assets	95,516,633	90,152,397
Total liabilities and net assets	$ 178,084,395	$ 172,412,908

Baxter Regional Health System

Consolidated Statements of Operations

Years Ended December 31, 2016 and 2015

	2016	2015
Unrestricted Revenues, Gains and Other Support		
Patient service revenue (net of contractual discounts and allowances)	$ 187,320,923	$ 174,875,385
Provision for uncollectible accounts	6,609,089	6,674,374
Net patient service revenue less provision for uncollectible accounts	180,711,834	168,201,011
Other	3,350,346	2,092,980
Contributions received	1,187,082	1,899,604
Net assets released from restrictions used for operations	377,728	508,808
Total unrestricted revenues, gains and other support	185,626,990	172,702,403
Expenses and Losses		
Salaries and wages	76,403,836	71,100,387
Employee benefits	20,941,929	19,930,284
Professional fees	13,184,656	11,548,949
Supplies and other	62,605,539	59,303,992
Depreciation	10,297,601	10,796,128
Interest	2,259,075	2,767,780
Total expenses and losses	185,692,636	175,447,520
Operating Loss	(65,646)	(2,745,117)
Other Income (Expenses)		
Investment return	1,824,785	1,464,548
Loss on investment in equity investees	(110,318)	(120,750)
Loss on refinancing	(665,164)	-
Other, net	(160,298)	(110,353)
Total other income	889,005	1,233,445
Excess (Deficiency) of Revenues Over Expenses	823,359	(1,511,672)
Investment return – change in unrealized gains and losses on other-than-trading securities	3,297,490	(3,310,328)
Contributions of or for acquisition of property and equipment	320,800	93,380
Sale of member units	19,600	-
Increase (Decrease) in Unrestricted Net Assets	$ 4,461,249	$ (4,728,620)

Baxter Regional Health System
Consolidated Statements of Changes in Net Assets
Years Ended December 31, 2016 and 2015

	2016	2015
Unrestricted Net Assets		
Excess (deficiency) of revenues over expenses	$ 823,359	$ (1,511,672)
Investment return – change in unrealized gains and losses on other-than-trading securities	3,297,490	(3,310,328)
Contributions of or for acquisition of property and equipment	320,800	93,380
Sale of member units	19,600	-
Increase (decrease) in unrestricted net assets	4,461,249	(4,728,620)
Temporarily Restricted Net Assets		
Contributions received	5,572	326,794
Investment return	1,275,143	(645,194)
Net assets released from restriction	(377,728)	(508,808)
Increase (decrease) in temporarily restricted net assets	902,987	(827,208)
Change in Net Assets	5,364,236	(5,555,828)
Net Assets, Beginning of Year	90,152,397	95,708,225
Net Assets, End of Year	$ 95,516,633	$ 90,152,397

Baxter Regional Health System

Consolidated Statements of Cash Flows

Years Ended December 31, 2016 and 2015

	2016	2015
Operating Activities		
Change in net assets	$ 5,364,236	$ (5,555,828)
Items not requiring (providing) cash		
Depreciation and amortization	10,085,519	10,992,393
Change in realized and unrealized gains and losses	(4,370,983)	4,777,382
Contributions of or for acquisition of property and equipment	(320,800)	(395,941)
Loss on investments in equity investees	110,318	120,750
Loss on disposal of property and equipment	41,584	34,802
Loss on refunding	665,164	-
Provision for uncollectible accounts	6,609,089	6,674,374
Changes in		
Patient accounts receivable, net	(6,495,848)	(5,363,839)
Estimated amounts due to/from third-party payers	626,378	119,986
Accounts payable and accrued expenses	2,233,551	(1,039,481)
Other current assets and liabilities	475,153	297,173
Net cash provided by operating activities	15,023,361	10,661,771
Investing Activities		
Purchase of investments	(8,403,850)	(10,734,774)
Proceeds from disposition of investments	6,910,825	13,263,506
Purchase of property and equipment	(9,662,972)	(10,071,021)
Proceeds from sale of property and equipment	54,308	41,908
Net cash used in investing activities	(11,101,689)	(7,500,381)
Financing Activities		
Proceeds from contributions for acquisition of property and equipment	320,800	93,380
Proceeds from issuance of long-term debt	7,337,112	117,485
Escrow deposit for advance refunding	(9,269,980)	-
Principal payments on long-term debt	(1,049,042)	(4,254,802)
Net cash used in financing activities	(2,661,110)	(4,043,937)
Increase (Decrease) in Cash and Cash Equivalents	1,260,562	(882,547)
Cash and Cash Equivalents, Beginning of Year	8,921,741	9,804,288
Cash and Cash Equivalents, End of Year	$ 10,182,303	$ 8,921,741
Supplemental Cash Flows Information		
Interest paid	$ 2,671,129	$ 2,830,186
Capital additions included in accounts payable and accrued expenses	$ 772,278	$ 606,597
Property acquired through noncash contributions	$ -	$ 604,000

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations and Principles of Consolidation

Baxter Regional Health System (the System) is an Arkansas not-for-profit charitable corporation as described in Section 501(c)(3) of the Internal Revenue Code. The System primarily earns revenue by providing health care services, including hospital, clinical, hospice and home health services to patients in Baxter and Marion Counties, located in Arkansas, as well as its secondary service area of Ozark County, Missouri, and Izard and Fulton Counties, located in Arkansas.

Organization	Primary Business Activity	Tax Status
Baxter Regional Health System (the System)	Parent holding company	Not-for-profit 501(c)(3)
Baxter County Regional Hospital, Inc. d/b/a Baxter Regional Medical Center (the Medical Center)	Acute-care hospital	Not-for-profit 501(c)(3); the System is sole member
Hospital Development Foundation, Inc. d/b/a Baxter Regional Hospital Foundation (the Foundation)	Solicit contributions for the benefit of the System and its nonprofit subsidiaries	Not-for-profit 501(c)(3); the System is sole member
Hospice of the Ozarks, Inc. (Hospice)	Hospice services	Not-for-profit 501(c)(3); the Medical Center is sole member
The BRMC Hometown Clinics, LLC (the Clinics)	Operation physician clinics	Taxable LLC; 100% owned by the System
BRMC Pain Center, LLC (the Pain Center)	Real estate holding company	Taxable LLC; 51% owned by the System
Scribner Family Practice, LLC (SFP Clinic)	Physician clinic in Salem, Arkansas (Interest sold on March 31, 2016)	Taxable LLC; 100% owned by the System

Organization	Primary Business Activity	Tax Status
Baxter Regional Center for Integrative Medicine, LLC (BRCIM)	Holistic clinic in Mountain Home, Arkansas (Closed 2016)	Taxable LLC; 100% owned by the System
Baxter Regional Health System Clinically Integrated Network, LLC (BRCIN) d/b/a Baxter Physician Partners	Integrated network of providers to Improve the quality of health for patients in the network's service area	Taxable LLC; 100% owned by the System
BRMC Cancer Diagnostic Center, LLC (the Cancer Diagnostic Center)	Real estate holding company	Taxable LLC; 51% owned by the System

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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Noncontrolling Interest

Noncontrolling interest represents the 49% interest in the Pain Center and the Cancer Diagnostic Center owned by outside investors. Noncontrolling interest is presented as a component of unrestricted net assets and the changes in net assets attributable to the noncontrolling interest are included in the consolidated changes in net assets. Losses attributable to the noncontrolling interest are allocated to the noncontrolling interest even if the carrying amount of the noncontrolling interest is reduced below zero. Any changes in ownership that do not result in a loss of control are prospectively accounted for as a net asset transaction.

Changes in consolidated unrestricted net assets attributable to the controlling financial interest of the System and the noncontrolling interest are:

	Total	Controlling Interest	Noncontrolling Interest
Balance, January 1, 2015	$ 95,708,225	$ 95,652,655	$ 55,570
Deficiency of revenues over expenses	(1,511,672)	(1,509,785)	(1,887)
Investment return – change in unrealized gains and losses on other-than-trading securities	(3,310,328)	(3,310,328)	-
Contributions of or for acquisition of property and equipment	93,380	93,380	-
Change in temporarily restricted net assets	(827,208)	(827,208)	-
Change in net assets	(5,555,828)	(5,553,941)	(1,887)
Balance, December 31, 2015	90,152,397	90,098,714	53,683
Excess of revenues over expenses	823,359	753,948	69,411
Investment return – change in unrealized gains and losses on other-than-trading securities	3,297,490	3,297,490	-
Contributions of or for acquisition of property and equipment	320,800	320,800	-
Sale of member units	19,600	-	19,600
Change in temporarily restricted net assets	902,987	902,987	-
Change in net assets	5,364,236	5,275,225	89,011
Balance, December 31, 2016	$ 95,516,633	$ 95,373,939	$ 142,694

Cash and Cash Equivalents

The System considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2016 and 2015, cash equivalents consisted primarily of money market accounts with brokers.

At December 31, 2016, the System's cash accounts exceeded federally insured limits by approximately $8,810,000.

Investments and Investment Return

Investments in equity securities having a readily determinable fair value and investments in all debt securities are carried at fair value. The investment in equity investees is reported on the equity method of accounting. Other investments including guaranteed investment contracts and real estate held by the Medical Center are valued at the lower of cost (or fair value at time of donation, if acquired by contribution) or fair value. Real estate held by the Foundation is carried at fair value. Mutual funds are carried at fair market value and primarily consist of fixed income-based funds. Investment return includes dividend, interest and other investment income; realized and unrealized gains and losses on investments carried at fair value; and realized gains and losses on other investments.

Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year is included in unrestricted net assets. Other investment return is reflected in the statements of operations and changes in net assets as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

Assets Limited as to Use

Assets limited as to use primarily include (1) 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; (2) assets restricted by donors; and (3) assets held by trustees. Amounts required to meet current liabilities of the System are included in current assets.

Patient Accounts Receivable

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the System 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 uncollectible accounts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the System analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for uncollectible accounts, if necessary (for example, for expected uncollectible 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 include both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the System records a significant provision for uncollectible accounts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

The difference between the standard rates (or the discounted rates if negotiated or provided by policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Supplies

The System states supply inventories at the lower of cost, determined using the first-in, first-out method, or market.

Property and Equipment

Property and equipment acquisitions are recorded at cost and are depreciated using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives.

The estimated useful lives for each major depreciable classification of property and equipment are as follows:

Land improvements	5–25 years
Buildings and leasehold improvements	15–40 years
Equipment	3–20 years

Donations of property and equipment are reported at fair value as an increase in unrestricted net assets unless use of the assets is restricted by the donor. Monetary gifts that must be used to acquire property and equipment are reported as restricted support. The expiration of such restrictions is reported as an increase in unrestricted net assets when the donated asset is placed in service.

The System capitalized interest costs as a component of construction in process, based on the weighted-average rates paid for long-term borrowing. Total interest capitalized during the years ended December 31, 2016 and 2015, was immaterial.

Long-Lived Asset Impairment

The System evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimate future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

No asset impairment was recognized during the years ended December 31, 2016 and 2015.

Deferred Financing Costs

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt into interest expense using the effective interest method. Amounts amortized in 2016 and 2015 were approximately $75,000 and $55,000, respectively.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the System has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the System in perpetuity.

Net Patient Service Revenue

The System has agreements with third-party payers that provide for payments to the System at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such estimated amounts are revised in future periods as adjustments become known.

Charity Care

The System provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy. Because the System does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue.

Contributions

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are initially reported at fair value determined using the discounted present value of estimated future cash flows technique. The resulting discount is amortized using the level-yield method and is reported as contribution revenue.

Gifts received with donor stipulations are reported as either temporarily or permanently restricted support. When a donor restriction expires, that is, when a time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified and reported as an increase in unrestricted net assets. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions. Conditional contributions are reported as liabilities until the condition is eliminated or the contributed assets are returned to the donor.

Professional Liability Claims

The System recognizes an accrual for claim liabilities based on estimated ultimate losses and costs associated with settling claims and a receivable to reflect the estimated insurance recoveries, if any. Professional liability claims are described more fully in *Note 6*.

Self-Insured Employee Health Claims

The System has elected to self-insure certain costs related to its employee health program. Costs resulting from noninsured losses are charged to income when incurred. An estimated accrual is made for claims incurred but not submitted for payment at year-end. Total expense for employee health insurance claims for the years ended December 31, 2016 and 2015, was $12,459,248 and $11,417,033, respectively. The System has purchased insurance that limits its exposure for individual claims up to $400,000.

Self-Insured Workers' Compensation Trust

The System has a self-insured workers' compensation trust for its employees. Claims against the trust are administered by an independent risk management firm. Claims are recorded as an expense as they are paid. An annual estimated provision is accrued for both reported claims and claims incurred but not reported. Funds maintained to pay future claims are included in the System's consolidated financial statements.

Income Taxes

The System, the Medical Center, the Foundation, and the Hospice have been recognized as exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. As such, they are required to file IRS Form 990 on an annual basis. These entities are subject to federal income tax on any unrelated business taxable income.

The Pain Center and Cancer Diagnostic Center are organized as Arkansas limited liability companies and treated as partnerships for income tax purposes. Taxable income or losses are reported to the individual members for inclusion in their respective tax returns. The Clinics, BRCIM, BRCIN and the SFP Clinic are treated as disregarded entities and included in the parent Form 990 return. The System files tax returns in the U.S. federal jurisdiction. No provision for federal or state income taxes is included in the System's financial statements. The System and its subsidiaries are no longer subject to U.S. federal income tax examinations by tax authorities for income tax returns filed for years before 2013.

Excess (Deficiency) of Revenues over Expenses

The consolidated statements of operations include excess (deficiency) of revenues over expenses. Changes in unrestricted net assets that are excluded from excess (deficiency) of revenues over expenses, consistent with industry practice, include unrealized gains and losses on investments in other-than-trading securities, permanent transfers to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions that, by donor restriction, were to be used for the purpose of acquiring such assets).

Transfers Between Fair Value Hierarchy Levels

Transfers in and out of Level 1 (quoted market prices), Level 2 (other significant observable inputs) and Level 3 (significant unobservable inputs) are recognized on the period beginning date.

Electronic Health Records Incentive Program

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible hospitals that demonstrate meaningful use of certified electronic health records technology (EHR). Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to four years based upon a statutory formula, which is determined by the state, and approved by the Centers for Medicare & Medicaid Services (CMS). Payment under both programs is contingent on the hospital continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. In addition, documentation or evidence of meeting each meaningful use criterion must be retained in the event of a post-payment audit. The final amount for any payment year is determined based upon an audit by the administrative contractors. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

The System recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

The System has recorded revenue of approximately $1,100,000 in 2016, which is included in other revenue within operating revenues in the consolidated statements of operations. In 2015, no revenue related to EHR was recorded as the System was not reasonably assured of meeting the meaningful use requirements by the fiscal year-end.

Subsequent Events

Subsequent events have been evaluated through the date of the Independent Auditor's Report, which is the date the consolidated financial statements were issued.

Reclassifications

Certain reclassifications have been made to the 2015 consolidated financial statements including those to conform to the 2016 consolidated financial statement presentation and for the adoption of ASU 2015-03, *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, that were deemed to be immaterial. These reclassifications had no effect on the change in net assets.

Note 2: Net Patient Service Revenue

The System recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, the System recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated and provided by policy). On the basis of historical experience, a significant portion of the System's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the System records a significant provision for uncollectible accounts related to uninsured patients in the period the services are provided. This provision for uncollectible accounts is presented on the statements of operations as a component of net patient service revenue.

The System has agreements with third-party payers that provide for payments to the System at amounts different from its established rates. These payment arrangements include:

Medicare—Inpatient acute care, hospice, psychiatric and rehabilitation services and substantially all 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. The System is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicare administrative contractor.

Medicaid—Inpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement methodology subject to certain cost limitations. Outpatient services rendered to Medicaid beneficiaries are paid based on a fee schedule. The System is reimbursed for inpatient services at tentative rates with final settlement determined after submission of annual cost reports by the System and audits thereof by the Medicaid administrative contractor.

Based on its status as a private hospital, the System participates in the Arkansas Medicaid provider assessment program. This program assesses a fee, accounted for as a deduction from revenue, of no more than 5.5% on the net patient service revenue of private hospitals and allocates the proceeds to supplement Medicaid payments. The federal government matches the assessment amount at a rate of approximately 3 to 1, and these amounts are allocated to private hospitals in Arkansas based on each hospital's share of total Medicaid patients. Deductions from revenue under this program for the years ended December 31, 2016 and 2015, were approximately $2.5 million and $2.3 million, respectively. Amounts recorded for the provider assessment revenues under this program for the years ended December 31, 2016 and 2015, were approximately $5.5 million and $5.4 million, respectively.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

Patient service revenue, net of contractual allowances and discounts (but before the provision for bad debts), recognized in the years ended December 31, 2016 and 2015, respectively, was:

	2016	2015
Medicare	$ 90,270,090	$ 83,309,720
Medicaid	8,569,745	8,002,418
Other third-party payers	83,380,919	77,845,504
Self-pay	5,100,169	5,717,743
Total	$ 187,320,923	$ 174,875,385

Note 3: Concentration of Credit Risk

The System grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payer agreements. The mix of receivables from patients and third-party payers at December 31, 2016 and 2015, is:

	2016	2015
Medicare	37 %	41 %
Medicaid	3	2
Other third-party payers	51	47
Patients	9	10
	100 %	100 %

Note 4: Investments and Investment Return

Investments are reported in the consolidated balance sheets in the following captions and consist of the following:

	2016	2015
Assets limited as to use:		
Internally designated for capital improvements		
Cash and cash equivalents	$ 5,293,154	$ 2,469,642
Equity securities	20,536,186	20,031,702
Equity exchange-traded funds	5,145,537	4,460,203
Corporate debt securities	4,483,923	4,348,559
Preferred stock	1,860,284	1,923,423
Fixed income mutual funds	1,884,140	1,847,489
Real estate	250,000	250,000
Interest receivable	22,505	25,083
Other	476,274	725,415
	39,952,003	36,081,516
Externally restricted by donors		
Cash and cash equivalents	879,917	1,012,375
Equity mutual funds	108,460	109,281
Equity exchange-traded funds	1,256,597	1,032,606
Fixed income exchange-traded funds	453,085	286,423
Real estate	2,750,982	2,117,517
Equity securities	7,190,171	7,230,262
Other	529,037	574,185
	13,168,249	12,362,649
Held by trustee under indenture agreement		
Cash and cash equivalents	-	8,238
Mortgage-backed securities	4,928,838	-
Guaranteed investment contract	-	5,594,063
U.S. Treasury obligations fund	1,733,866	2,157,722
Interest receivable	26,642	120,232
	6,689,346	7,880,255
Other		
Certificates of deposit	200,000	200,000

	2016	2015
Other investments:		
Equity securities	$ 8,616,210	$ 7,296,481
Corporate debt securities	1,999,690	2,069,799
Preferred stock	1,443,166	310,917
Real estate	60,000	60,000
Fixed income mutual funds	-	3,039
	12,119,066	9,740,236
Less long-term investments	60,000	60,000
Short-term investments	12,059,066	9,680,236
Total System investments	$ 72,128,664	$ 66,264,656

Total investment return is comprised of the following:

	2016	2015
Interest and dividend income	$ 2,026,435	$ 2,286,408
Realized and unrealized gains (losses) on other-than-trading securities	4,370,983	(4,777,382)
	$ 6,397,418	$ (2,490,974)

Total investment return is reflected in the consolidated statements of operations and changes in net assets as follows:

	2016	2015
Unrestricted net assets		
Other nonoperating income	$ 1,824,785	$ 1,464,548
Change in unrealized gains (losses) on other-than-trading securities	3,297,490	(3,310,328)
Temporarily restricted net assets	1,275,143	(645,194)
	$ 6,397,418	$ (2,490,974)

At December 31, 2016, and 2015, the System's real estate investments included real estate located in various locations in north central Arkansas and southern Missouri with a carrying value of $3,060,982 and $2,427,517, respectively. The System has a practice of periodically challenging the value of its holdings, and updating these values when conditions arise that indicate the valuation could be materially affected.

Certain investments in debt and marketable equity securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2016 and 2015, was $19,041,546 and $21,478,567, respectively, which was approximately 26% and 32%, respectively, of the System's investment portfolio.

To the extent they are material, management believes the declines in fair value for these securities are temporary because the declines are due to changes in the market conditions and not credit deterioration for the individual companies. The System expects the temporarily impaired debt securities to recover value as they near maturity. The System's investments in marketable equity securities consist of mutual funds and common stock in companies from a diverse range of industries. Based on the System's ability and intent to hold those investments for a reasonable period of time sufficient for a forecasted recovery of fair value, the System does not consider those investments to be other-than-temporarily impaired at December 31, 2016.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in excess of revenues over expenses in the period the other-than-temporary impairment is identified. The System routinely conducts periodic reviews to identify and evaluate each investment security to determine whether an other-than-temporary impairment has occurred.

The following tables show the System's investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2016 and 2015:

	December 31, 2016					
	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Debt securities	$ 3,595,173	$ 138,570	$ 2,514,826	$ 178,951	$ 6,109,999	$ 317,521
Equity securities	9,054,278	1,137,837	3,877,269	808,242	12,931,547	1,946,079
Total temporarily impaired securities	$12,649,451	$ 1,276,407	$ 6,392,095	$ 987,193	$19,041,546	$ 2,263,600

	December 31, 2015					
	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Debt securities	$ 1,409,157	$ 208,232	$ 3,320,576	$ 291,868	$ 4,729,733	$ 500,100
Equity securities	11,116,629	2,856,537	5,632,205	1,627,165	16,748,834	4,483,702
Total temporarily impaired securities	$12,525,786	$ 3,064,769	$ 8,952,781	$ 1,919,033	$21,478,567	$ 4,983,802

Note 5: Investments in and Advances to Equity Investees

The investments in and advances to equity investees relate to a 37% ownership of Renal Center of Mountain Home, LLC, which provides dialysis services to area residents, and a 50% ownership of Baxter Regional PHO, LTD., which provides medical credentialing services to the System.

Note 6: Professional Liability Claims

Beginning May 1, 2014, the System is self-insured for the first $100,000 per occurrence and $300,000 in aggregate for medical malpractice risks. For open claim years prior to that date, the System is self-insured for the first $250,000 per occurrence and $750,000 in aggregate for medical malpractice risks. The System purchases commercial insurance coverage above the self-insurance limits for the next $1,000,000 per occurrence and $3,000,000 in aggregate of medical malpractice risks.

This commercial coverage is provided under a claims-made policy. Under such a policy, only claims made and reported to the insurer during the policy term, regardless of when the incidents giving rise to the claims occurred, are covered.

Based on the System's claims experience, an accrual had been made for the System's estimated medical malpractice costs, including costs associated with litigating or settling claims under its malpractice insurance policy, amounting to approximately $554,000 and $850,000 as of December 31, 2016 and 2015, respectively. It is reasonably possible that this estimate could change materially in the near term.

Note 7: Long-term Debt

	2016	2015
Revenue refunding bonds (A)	$ -	$ 36,755,000
Revenue refunding bonds (B)	-	15,340,000
Revenue improvement bonds (C)	-	5,095,000
Revenue refunding bonds (D)	49,675,000	-
Installment note payable (E)	1,879,958	2,832,361
Note payable (F)	2,296,680	2,397,588
Note payable (G)	104,732	159,271
Note payable (H)	95,342	117,485
Note payable (I)	367,255	-
Note payable (J)	1,091,705	-
	55,510,672	62,696,705
Less unamortized debt issuance costs	(661,730)	(344,872)
Less current maturities	(4,197,718)	(4,331,432)
Plus bond premium	5,067,139	216,198
	$ 55,718,363	$ 58,236,599

(A) The Revenue Refunding Bonds (the Supplemental Bonds) consisted of Tax-exempt Revenue Bonds in the original amount of $39,980,000 dated February 1, 2007, which bore interest at rates ranging from 4.125% to 5.000%. Interest was due semiannually on March 1 and September 1. All outstanding maturities of the Supplemental Bonds were refunded on September 1, 2016, with funds from securities deposited into an irrevocable escrow account established upon issuance and delivery of the 2016 Revenue Refunding Bonds (see (*D*) below). Unamortized debt issuance costs, which related to the Supplemental Bonds as well as the bonds described in sections (*B*) and (*C*) below, were $0 and $344,872 at December 31, 2016 and 2015, respectively. The effective interest rate was 0% and 0.10% for the years ended December 31, 2016 and 2015, respectively.

Baxter County, Arkansas, issued the Supplemental Bonds on behalf of the Medical Center. The Supplemental Bonds were secured by substantially all of the Medical Center's property and equipment. The Supplemental Bonds were not guaranteed by the County.

The indenture agreement requires that certain funds be established with the trustee. Accordingly, these funds are included as assets limited as to use held by trustee in the financial statements. The indenture agreement also requires the Medical Center to comply with certain restrictive covenants including minimum insurance coverage, maintaining a debt-service coverage ratio of at least 115% and restrictions on incurrence of additional debt and transfers of assets.

The Revenue Refunding Bonds (the Refunding Bonds) consist of Tax-exempt Revenue Revenue Bonds in the original amount of $25,865,000 dated August 1, 2010, which bore interest at rates ranging from 3.000% to 4.375%. Interest was due semiannually on March 1 and September 1. All outstanding maturities of the Supplemental Bonds were refunded, on September 1, 2016, with funds from securities deposited into an irrevocable escrow account established upon issuance and delivery of the 2016 Revenue Refunding Bonds (see (*D*) below).

The County issued the Refunding Bonds on behalf of the Medical Center. The Refunding Bonds were secured by substantially all of the Medical Center's property and equipment and were issued on parity with the Supplemental Bonds described in (*A*). The Refunding Bonds were not guaranteed by the County.

Certain indenture requirements for the Refunding Bonds were shared with the Supplemental Bonds. See discussion of those requirements in (*A*).

(C) The Revenue Improvement Bonds (the Improvement Bonds) consist of Tax-exempt Revenue Bonds Series 2012A in the original amount of $5,765,000 and Taxable Subordinate Series 2012B in the original amount of $45,000 dated October 1, 2012, which bear interest at rates ranging from 1.250% to 4.400%. Interest is due semiannually on March 1 and September 1.

On September 1, 2016, proceeds from the 2016 Bonds (see (*D*) below) together with funds on deposit in bond funds and debt service reserve funds were used to purchase securities that were deposited in trust under an irrevocable escrow agreement sufficient in amount to pay future principal, interest and redemption premiums on the Improvement Bonds. This advance refunding transaction resulted in an extinguishment of debt since the System was legally released from its obligation on the Improvement Bonds at the time of the defeasance. Accordingly, the Improvement Bonds, aggregating $4,855,000 at December 31, 2016, remain outstanding, but are excluded from the System's consolidated balance sheet.

The County issued the Improvement Bonds on behalf of the Medical Center and are secured by substantially all of the Medical Center's property and equipment. The Improvement Bonds were not guaranteed by the County.

Certain indenture requirements for the Improvement Bonds are shared with the Supplemental Bonds. See discussion of those requirements in (*A*).

(D) The 2016 Revenue Refunding Bonds (the 2016 Bonds) consist of Tax-exempt Hospital Revenue Bonds Series 2016A in the original amount of $44,925,000 and Series 2016B in the original amount of $4,785,000; issued for the purpose, together with funds in bond fund and debt service reserve funds, of refunding $52,095,000 of existing revenue bonds discussed in (*A*) and (*B*) and advance refunding $5,095,000 of existing revenue bonds discussed in (*C*) above; and bearing interest at rates ranging from 2% to 5%. The 2016 Bonds are payable in annual installments including mandatory sinking fund redemption through September 1, 2032. Interest is due semiannually on March 1 and September 1. The System is required to make monthly deposits into the debt service funds of approximately $365,000.

All of the 2016 Bonds still outstanding may be redeemed at the System's option on or after September 1, 2026, at a redemption price of 100% of the principal amount thereof, plus accrued interest to the date of redemption. The 2016 Bonds are obligations of the Medical Center, but are guaranteed by the System. Unamortized debt issuance costs were $661,730 at December 31, 2016. The effective interest rate was 0.09% for the year ended December 31, 2016.

The County issued the 2016 Bonds on behalf of the Medical Center. The 2016 Bonds are secured by a mortgage on the hospital facility, the gross receipts of the Hospital and the assets restricted under the trust agreement. The 2016 Bonds were not guaranteed by the County.

The trust agreement requires that certain funds be established with the trustee. Accordingly, these funds are included as assets limited as to use held by trustee in the financial statements. The trust agreement also requires the Medical Center to comply with certain restrictive covenants including minimum insurance coverage, maintaining a debt-service coverage ratio of at least 115% and restrictions on incurrence of additional debt and transfers of assets.

(E) Due November 29, 2018; to Banc of America Public Capital Corp; monthly payments are approximately $84,000 including interest of 2.24%. The proceeds were used for the purchase of certain specified capital equipment that is required to serve as collateral.

(F) Due October 1, 2018; 59 monthly payments of $14,532 including interest of 2.99% and one balloon payment of $2,108,361, secured by BRMC Pain Center, LLC, building and land and guaranteed by the System.

(G) Due October 1, 2018; monthly payments are $4,900 including interest of 2.99%, secured by BRMC Pain Center, LLC, equipment.

(H) Due December 21, 2020; monthly payments are $2,113 including interest of 2.99% secured by certain BRMC Pain Center, LLC, equipment.

(I) Due on demand, but if no demand, monthly payments of $7,500 including interest of 2.75% are due through April 1, 2021; secured by BRMC Cancer Diagnostic Center, LLC, equipment.

(J) Due on demand, but if no demand, monthly payments of $6,073 including interest of 2.75% are due through April 1, 2021; with a balloon payment of $900,868 then due; secured by BRMC Cancer Diagnostic Center, LLC, building and land.

Aggregate annual maturities and sinking fund requirements of long-term debt at December 31, 2016, are:

2017	$ 4,197,718
2018	6,349,123
2019	3,365,567
2020	3,524,807
2021	3,608,234
Thereafter	34,465,223
	$ 55,510,672

Note 8: Temporarily and Permanently Restricted Net Assets

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

	2016	2015
Scholarships	$ 2,329,354	$ 1,810,564
Purchase of equipment	187,879	187,410
Indigent care	122,721	94,384
For periods after December 31, 2016 and 2015	2,588,266	2,232,875
	$ 5,228,220	$ 4,325,233

During 2016 and 2015, net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes in the amounts of $377,728 and $508,808, respectively.

Permanently restricted net assets are restricted to investments to be held in perpetuity, the income of which is restricted to the following purposes:

	2016	2015
Scholarships	$ 5,372,162	$ 5,372,162
Community health needs	1,848,319	1,848,319
Indigent care	98,705	98,705
	$ 7,319,186	$ 7,319,186

Note 9: Endowment

The System's endowment consists of approximately eight individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the governing body to function as endowments (board-designated endowment funds). As required by accounting principles generally accepted in the United States of America (GAAP), net assets associated with endowment funds, including board-designated endowment funds, are classified and reported based on the existence or absence of donor-imposed restrictions.

The System's governing body has interpreted the State of Arkansas Prudent Management of Institutional Funds Act (SPMIFA) as requiring 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. As a result of this interpretation, the System classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts donated to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the System in a manner consistent with the standard of prudence prescribed by SPMIFA.

In accordance with SPMIFA, the System considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of the System and the fund
3. General economic conditions
4. Possible effect of inflation and deflation
5. Expected total return from investment income and appreciation or depreciation of investments
6. Other resources of the System
7. Investment policies of the System

The composition of net assets by type of endowment fund at December 31, 2016 and 2015, was:

	2016			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ -	$ 2,399,901	$ 7,319,186	$ 9,719,087
Board-designated endowment funds	215,119	-	-	215,119
Total endowment funds	$ 215,119	$ 2,399,901	$ 7,319,186	$ 9,934,206

	2015			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ -	$ 1,797,408	$ 7,319,186	$ 9,116,594
Board-designated endowment funds	186,413	-	-	186,413
Total endowment funds	$ 186,413	$ 1,797,408	$ 7,319,186	$ 9,303,007

Changes in endowment net assets for the years ended December 31, 2016 and 2015, were:

	2016			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 186,413	$ 1,797,408	$ 7,319,186	$ 9,303,007
Investment return				
Investment income	19,294	315,725	-	335,019
Net appreciation	9,412	633,077	-	642,489
Total investment return	28,706	948,802	0	977,508
Contributions	-	-	-	-
Appropriation of endowment assets for expenditure	-	(346,309)	-	(346,309)
Endowment net assets, end of year	$ 215,119	$ 2,399,901	$ 7,319,186	$ 9,934,206

	2015			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 213,291	$ 2,697,151	$ 7,319,186	$ 10,229,628
Investment return				
Investment income	(9,524)	277,450	-	267,926
Net appreciation	(8,543)	(682,620)	-	(691,163)
Total investment return	(18,067)	(405,170)	0	(423,237)
Contributions	-	-	-	-
Appropriation of endowment assets for expenditure	(8,811)	(494,573)	-	(503,384)
Endowment net assets, end of year	$ 186,413	$ 1,797,408	$ 7,319,186	$ 9,303,007

Amounts of donor-restricted endowment funds classified as permanently and temporarily restricted net assets at December 31, 2016 and 2015, consisted of:

	2016	2015
Permanently restricted net assets – portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation or SPMIFA	$ 7,319,186	$ 7,319,186
Temporarily restricted net assets – with purpose restrictions	$ 2,399,901	$ 1,797,408

From time to time, fair value of assets associated with individual donor-restricted endowment funds may fall below the level the System is required to retain as a fund of perpetual duration pursuant to donor stipulation or SPMIFA. There were no such deficiencies at December 31, 2016 and 2015.

The System has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs and other items supported by its endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds the System must hold in perpetuity or for donor-specified periods, as well as those of board-designated endowment funds.

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

The System has various spending policies that govern expenditures of investment returns on endowment funds. Spending policies for donor-restricted endowments are based on the purpose restrictions placed on any proceeds from endowment funds and generally specify a fixed amount of spending each year. Spending policies related to board-designated endowment funds vary based on the goals set for each endowment fund, but are generally designed to support the endowment's short-term goals while allowing sufficient reinvestment to appreciate each fund.

Note 10: Charity Care

In support of its mission, the System voluntarily provides free care to patients who lack financial resources and are deemed to be medically indigent. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported in net patient service revenue. In addition, the System provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts that are less than established charges for the services provided to the recipients, and many times the payments are less than the cost of rendering the services provided. Uncompensated charges relating to these services were $4,169,074 and $4,678,755 for the years ended December 31, 2016 and 2015, respectively. Management estimates that cost relating to these services was approximately $1,309,923 and $1,444,332 for the years ended December 31, 2016 and 2015, respectively, using a Medicare-based reasonable costs methodology.

In addition to uncompensated charges, the System also commits significant time and resources to endeavors and critical services that meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screening and assessments, prenatal education and care, community educational services and various support groups.

Note 11: Functional Expenses

The System provides health care services primarily to residents within its geographic area. Expenses related to providing these services are as follows:

	2016	2015
Health care services	$ 167,704,129	$ 156,900,359
General and administrative	17,988,507	18,547,161
	$ 185,692,636	$ 175,447,520

Note 12: Operating Leases

The System leases equipment under various lease agreements. Total rent and lease expense was $2,001,751 and $1,912,413 for the years ended December 31, 2016 and 2015, respectively.

Note 13: Pension Plan

The System has a defined contribution pension plan covering substantially all employees. An employee who chooses to participate in the plan must make a minimum contribution of 2% of their salary during their first through third year of service, 2.5% during their fourth through fifth year of service and 3% after five years of service in order to receive a matching contribution from the System. The System's matching contribution is 3%, 3.5% and 4% of the participant's salary during each of these time periods, respectively. Employees are 100% vested in the portion of their account accumulated from their contributions to the plan. Employees become fully vested in matching contributions after three years of service. Total pension expense, net of forfeitures utilized, for the years ended December 31, 2016 and 2015, was $1,940,151 and $1,773,743, respectively.

Note 14: Disclosures About Fair Value of Assets and Liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable 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 for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities.

Recurring Measurements

The following tables present the fair value measurements of assets recognized in the accompanying balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2016 and 2015:

		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2016				
Fixed income mutual funds	$ 1,884,140	$ 1,884,140	$ -	$ -
Equity mutual funds	108,460	108,460	-	-
Equity securities	36,342,567	36,342,567	-	-
Equity exchange-traded funds	6,402,134	6,402,134	-	-
Preferred stocks	3,303,450	3,303,450	-	-
Fixed income exchange-traded funds	453,085	453,085	-	-
U.S. Treasury obligations	1,733,866	1,733,866	-	-
Mortgage-backed securities	4,928,838	-	4,928,838	-
Corporate debt securities	6,483,613	-	6,483,613	-
Other	1,005,311	476,274	-	529,037
Real estate held by the Foundation	2,810,982	-	-	2,810,982
Total	$ 65,456,446	$ 50,703,976	$ 11,412,451	$ 3,340,019
December 31, 2015				
Fixed income mutual funds	$ 1,850,528	$ 1,850,528	$ -	$ -
Equity mutual funds	109,281	109,281	-	-
Equity securities	34,558,445	34,558,445	-	-
Equity exchange-traded funds	5,492,809	5,492,809	-	-
Preferred stocks	2,234,341	2,234,341	-	-
Fixed income exchange-traded funds	286,423	286,423	-	-
U.S. Treasury obligations	2,157,722	2,157,722	-	-
Corporate debt securities	6,418,358	-	6,418,358	-
Other	1,299,600	800,945	-	498,655
Real estate held by the Foundation	2,177,517	-	-	2,177,517
Total	$ 56,585,024	$ 47,490,494	$ 6,418,358	$ 2,676,172

The following is a reconciliation of investments carried at fair value and the System's total investments:

	2016	2015
Financial instruments carried at fair value	$ 65,456,446	$ 56,585,024
Financial instruments not carried at fair value:		
Cash and cash equivalents	6,173,071	3,490,254
Guaranteed investment contract	-	5,594,063
Real estate held by the Medical Center	250,000	250,000
Certificates of deposit	200,000	200,000
Interest receivable	49,147	145,315
Money market funds classified as cash	-	-
Total System investments	$ 72,128,664	$ 66,264,656

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2016. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Investments

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3. See the table below for inputs and valuation techniques used for Level 3 securities.

Level 3 Valuation Process

Fair value determinations for Level 3 measurements of securities are the responsibility of the Controller's office. The Controller's office contracts with a pricing specialist to generate fair value estimates on a monthly or quarterly basis. The Controller's office challenges the reasonableness of the assumptions used and reviews the methodology to ensure the estimated fair value complies with accounting standards generally accepted in the United States.

Fair value determinations for Level 3 measurements of real estate held by the Foundation and beneficial interests in charitable remainder trusts are the responsibility of the Controller's office. The Controller's office contracts with a certified appraiser to generate fair value estimates for real estate upon purchases or when conditions indicate that previous measurements may no longer be reasonable. Management evaluates these conditions no less frequently than annually. The Controller's office challenges the reasonableness of the assumptions used and reviews the methodology to ensure the estimated fair value complies with accounting standards generally accepted in the United States. The Controller's office determines the fair value estimates of beneficial interests in charitable remainder trusts based on a discounted cash flow model.

Level 3 Reconciliation

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying consolidated balance sheets using significant unobservable (Level 3) inputs:

	2016	2015
Balance, beginning of year	$ 2,676,172	$ 1,995,670
Purchases	633,464	694,298
Total realized and unrealized gains and losses included in change in net assets	30,383	(13,796)
Balance, end of year	$ 3,340,019	$ 2,676,172

Unobservable (Level 3) Inputs

The following tables present quantitative information about unobservable inputs used in recurring (Level 3) fair value measurements:

	Fair Value at 12/31/2016	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Beneficial interest in charitable remainder trusts	$ 529,037	Discounted cash flow	Life expectancy of the beneficiary Expected rate of return	1.8–6.9 years (4.4 years) 1.9–2.0% (1.95%)
Real estate	$ 2,810,982	Estimated based on comparable real estate transactions	Comparable real estate transactions	Various

	Fair Value at 12/31/2015	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
Beneficial interest in charitable remainder trusts	$ 498,655	Discounted cash flow	Life expectancy of the beneficiary Expected rate of return	2.8–7.9 years (5.4 years) 1.7–1.8% (1.75%)
Real estate	$ 2,177,517	Estimated based on comparable real estate transactions	Comparable real estate transactions	Various

Sensitivity of Significant Unobservable Inputs

The following is a discussion of the sensitivity of significant unobservable inputs, the interrelationships between those inputs and other unobservable inputs used in recurring fair value measurement and of how those inputs might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement.

Beneficial Interest in Charitable Remainder Trusts

The significant unobservable inputs used in the fair value measurement of the System's beneficial interest in charitable remainder trusts are life expectancy of the beneficiaries and expected rates of return. Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value measurement. Those inputs are not interrelated.

Real Estate

The significant unobservable input used in the fair value measurement of the System's real estate investment is comparable real estate transactions. Significant increases (decreases) in this input would result in a significantly higher (lower) fair value measurement.

Note 15: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Allowance for Net Patient Service Revenue Adjustments

Estimates of allowances for adjustments included in net patient service revenue are described in *Notes 1* and *2*.

Professional Liability Claims

Estimates related to the accrual for medical malpractice claims are described in *Notes 1* and *6*.

Admitting Physicians

The System is served by an admitting physician group whose patients comprise approximately 13% of the System's inpatient admissions.

Litigation

In the normal course of business, the System is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by the System's commercial insurance; for example, allegations regarding employment practices or performance of contracts. The System evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of ultimate expected loss, if any, for each of these matters.

As of December 31, 2016 and 2015, the System did not record an estimated loss. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

Investments

The System invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying consolidated balance sheets.

Note 16: Letter of Credit

In order to provide a reserve for malpractice and workers' compensation deductibles, the System has obtained a letter of credit (Letter), which expires May 11, 2017. The amount available for withdrawal is approximately $150,000. As of December 31, 2016 and 2015, no amounts were drawn on the Letter.

Note 17: Patient Protection and Affordable Care Act

The *Patient Protection and Affordable Care Act* (PPACA) has and will continue to substantially reform the United States health care system. The legislation impacts multiple aspects of the health care system including many provisions that change payments from Medicare, Medicaid and insurance companies. A significant component of PPACA is the expansion of the Medicaid program to a wide range of newly eligible individuals. In anticipation of this expansion, payments under certain existing programs, such as Medicare disproportionate share, will be substantially decreased. Each state's participation in an expanded Medicaid program is optional. The state of Arkansas has enacted a form of Medicaid expansion which uses the expansion funding to purchase private insurance policies on the health care exchanges for qualifying beneficiaries beginning January 1, 2014, originally called the Arkansas Private Option and now termed Arkansas Works.

Arkansas Works has been subject to annual reauthorization. In April 2016, Arkansas legislature reauthorized the Medicaid expansion with certain modifications through December 31, 2021, subject to annual budgetary reappropriation.

Supplementary Information

Baxter Regional Health System

Consolidating Schedule – Balance Sheet Information

December 31, 2016

Assets	Baxter County Regional Hospital, Inc.	Hospice of the Ozarks, Inc.	Hospital Development Foundation, Inc.	Baxter Regional Health System	BRHS Hometown Clinics, Inc
Current Assets					
Cash and cash equivalents	$ 7,713,998	$ 1,285,193	$ 834,565	$ 36,030	$ 80,502
Short-term investments	-	10,584,641	1,474,425	-	-
Assets limited as to use – current	1,733,866	-	-	-	-
Patient accounts receivable, net	20,522,187	449,869	-	-	77,566
Supplies	5,903,515	-	-	-	-
Prepaid expenses and other	1,085,915	-	608,415	-	-
Estimated amounts due from third-party payers	824,626	-	-	-	-
Due from affiliates	1,815,671	-	-	-	-
Total current assets	39,599,778	12,319,703	2,917,405	36,030	158,068
Assets Limited as to Use					
Internally designated for capital improvements	39,851,683	100,320	-	-	-
Externally restricted by donors	195,308	-	12,972,941	-	-
Held by trustee under indenture agreement	6,689,346	-	-	-	-
Other	200,000	-	-	-	-
	46,936,337	100,320	12,972,941	0	0
Less amount required to meet current obligations	1,733,866	-	-	-	-
	45,202,471	100,320	12,972,941	0	0
Investments in and Advances to Equity Investees	60,009	-	-	(467,310)	-
Property and Equipment, at Cost					
Land and land improvements	6,482,389	94,261	20,000	267,104	-
Buildings and leasehold improvements	70,449,167	2,094,777	-	601,325	-
Equipment	123,749,816	1,537,236	29,359	158,455	20,491
Construction in progress	344,843	-	-	1,050,302	-
	201,026,215	3,726,274	49,359	2,077,186	20,491
Less accumulated depreciation	142,682,425	2,200,800	29,359	109,690	3,050
	58,343,790	1,525,474	20,000	1,967,496	17,441
Other Assets					
Long-term investments	-	-	60,000	-	-
Other	23,535	48,083	40,809	-	-
	23,535	48,083	100,809	0	0
Total assets	$ 143,229,583	$ 13,993,580	$ 16,011,155	$ 1,536,216	$ 175,509

BRMC Pain Center, LLC	SFP Clinic, LLC	BRCIM, LLC	BRCIN, LLC	Cancer Diagnostic Center	Eliminations	Consolidated
$ 119,041	$ -	$ -	$ 43,999	$ 68,975	$ -	$ 10,182,303
-	-	-	-	-	-	12,059,066
-	-	-	-	-	-	1,733,866
-	-	-	-	-	-	21,049,622
-	-	-	-	-	-	5,903,515
136	-	-	197,816	-	-	1,892,282
-	-	-	-	-	-	824,626
-	-	-	-	-	(1,815,671)	0
119,177	0	0	241,815	68,975	(1,815,671)	53,645,280
-	-	-	-	-	-	39,952,003
-	-	-	-	-	-	13,168,249
-	-	-	-	-	-	6,689,346
-	-	-	-	-	-	200,000
0	0	0	0	0	0	60,009,598
-	-	-	-	-	-	1,733,866
0	0	0	0	0	0	58,275,732
-	-	-	-	-	467,310	60,009
630,000	-	-	-	380,000	-	7,873,754
2,019,108	-	-	-	740,000	-	75,904,377
389,686	-	-	-	420,000	-	126,305,043
-	-	-	-	-	-	1,395,145
3,038,794	0	0	0	1,540,000	0	211,478,319
448,608	-	-	-	73,440	-	145,547,372
2,590,186	0	0	0	1,466,560	0	65,930,947
-	-	-	-	-	-	60,000
-	-	-	-	-	-	112,427
0	0	0	0	0	0	172,427
$ 2,709,363	$ 0	$ 0	$ 241,815	$ 1,535,535	$ (1,348,361)	$ 178,084,395

Baxter Regional Health System

Consolidating Schedule – Balance Sheet Information (Continued)

December 31, 2016

Liabilities and Net Assets	Baxter County Regional Hospital, Inc.	Hospice of the Ozarks, Inc.	Hospital Development Foundation, Inc.	Baxter Regional Health System	BRHS Hometown Clinics, Inc
Current Liabilities					
Current maturities of long-term debt	$ 3,886,848	$ -	$ -	$ -	$ -
Accounts payable	6,837,281	-	744,570	-	25,754
Accrued expenses	9,420,920	-	-	-	-
Accrued interest	748,552	-	-	-	-
Estimated amounts due to third-party payers	4,874,604	-	-	-	-
Due to affiliate	-	301,743	159,562	1,100,603	-
Total current liabilities	25,768,205	301,743	904,132	1,100,603	25,754
Long-term Debt	52,075,548	-	-	-	-
Total liabilities	77,843,753	301,743	904,132	1,100,603	25,754
Net Assets					
Unrestricted					
Baxter Regional Health System	65,190,518	13,691,837	2,754,929	435,613	149,755
Noncontrolling interest	-	-	-	-	-
Total unrestricted net assets	65,190,518	13,691,837	2,754,929	435,613	149,755
Temporarily restricted	190,312	-	5,037,908	-	-
Permanently restricted	5,000	-	7,314,186	-	-
Total net assets	65,385,830	13,691,837	15,107,023	435,613	149,755
Total liabilities and net assets	$ 143,229,583	$ 13,993,580	$ 16,011,155	$ 1,536,216	$ 175,509

BRMC Pain Center, LLC	SFP Clinic, LLC	BRCIM, LLC	BRCIN, LLC	Cancer Diagnostic Center	Eliminations	Consolidated
$ 186,540	$ -	$ -	$ -	$ 124,330	$ -	$ 4,197,718
-	-	-	-	-	-	7,607,605
-	-	-	-	-	-	9,420,920
-	-	-	-	-	-	748,552
-	-	-	-	-	-	4,874,604
-	-	-	253,763	-	(1,815,671)	0
186,540	0	0	253,763	124,330	(1,815,671)	26,849,399
2,308,151	-	-	-	1,334,664	-	55,718,363
2,494,691	0	0	253,763	1,458,994	(1,815,671)	82,567,762
109,483	-	-	(11,948)	39,036	467,310	82,826,533
105,189	-	-	-	37,505	-	142,694
214,672	0	0	(11,948)	76,541	467,310	82,969,227
-	-	-	-	-	-	5,228,220
-	-	-	-	-	-	7,319,186
214,672	0	0	(11,948)	76,541	467,310	95,516,633
$ 2,709,363	$ 0	$ 0	$ 241,815	$ 1,535,535	$ (1,348,361)	$ 178,084,395

Baxter Regional Health System

Consolidating Schedule – Statement of Operations Information

Year Ended December 31, 2016

	Baxter County Regional Hospital, Inc.	Hospice of the Ozarks, Inc.	Hospital Development Foundation, Inc.	Baxter Regional Health System	BRHS Hometown Clinics, Inc.
Unrestricted Revenues, Gains and Other Support					
Patient service revenue (net of contractual discounts and allowances)	$ 183,625,327	$ 3,235,603	$ -	$ -	$ 333,315
Provision for uncollectible accounts	6,609,089	-	-	-	-
Net patient service revenue less provision for uncollectible accounts	177,016,238	3,235,603	-	-	333,315
Other	2,845,046	-	-	46,022	-
Contributions received	534,048	471,958	1,088,151	-	-
Net assets released from restrictions used for operations	-	-	377,728	-	-
Total unrestricted revenues, gains and other support	180,395,332	3,707,561	1,465,879	46,022	333,315
Expenses and Losses					
Salaries and wages	73,468,735	1,844,082	291,939	-	466,413
Employee benefits	20,321,347	507,263	-	-	31,618
Professional fees	12,877,695	104,707	-	3,365	40,076
Supplies and other	60,777,887	1,168,287	1,572,100	21,333	337,371
Depreciation and amortization	9,936,222	124,835	2,090	51,853	3,050
Interest	2,152,617	-	-	-	-
Total expenses and losses	179,534,503	3,749,174	1,866,129	76,551	878,528
Operating Income (Loss)	860,829	(41,613)	(400,250)	(30,529)	(545,213)
Other Income (Expense)					
Investment return	954,587	749,442	120,756	-	-
Loss on investment in equity investees	(110,318)	-	-	(529,482)	-
Loss on refinancing	(665,164)	-	-	-	-
Other, net	(160,298)	-	-	-	-
Total other income	18,807	749,442	120,756	(529,482)	0
Excess (Deficiency) of Revenues Over Expenses	879,636	707,829	(279,494)	(560,011)	(545,213)
Investment return – change in unrealized gains and losses on other-than-trading securities	2,761,001	467,988	68,501	-	-
Contributions of or for acquisition of property and equipment	373,362	-	320,800	-	-
Sale of member units	-	-	-	-	-
Transfers from (to) affiliates	(2,297,833)	-	-	1,175,961	754,499
Increase in Unrestricted Net Assets	$ 1,716,166	$ 1,175,817	$ 109,807	$ 615,950	$ 209,286

BRMC Pain Center, LLC	SFP Clinic, LLC	BRCIM, LLC	BRCIN, LLC	Cancer Diagnostic Center	Eliminations	Consolidated
$ -	$ 113,318	$ 13,360	$ -	$ -	$ -	$ 187,320,923
-	-	-	-	-	-	6,609,089
-	113,318	13,360	-	-	-	180,711,834
439,104	-	-	923,179	160,562	(1,063,567)	3,350,346
-	-	-	-	-	(907,075)	1,187,082
-	-	-	-	-	-	377,728
439,104	113,318	13,360	923,179	160,562	(1,970,642)	185,626,990
-	85,801	13,838	233,028	-	-	76,403,836
-	7,499	1,497	72,705	-	-	20,941,929
3,595	1,619	1,800	150,924	875	-	13,184,656
145,405	50,738	20,400	466,522	22,126	(1,976,630)	62,605,539
106,111	-	-	-	73,440	-	10,297,601
78,879	-	-	-	27,579	-	2,259,075
333,990	145,657	37,535	923,179	124,020	(1,976,630)	185,692,636
105,114	(32,339)	(24,175)	0	36,542	5,988	(65,646)
-	-	-	-	-	-	1,824,785
-	-	-	-	-	529,482	(110,318)
-	-	-	-	-	-	(665,164)
-	-	-	-	-	-	(160,298)
0	0	0	0	0	529,482	889,005
105,114	(32,339)	(24,175)	0	36,542	535,470	823,359
-	-	-	-	-	-	3,297,490
-	-	-	-	-	(373,362)	320,800
-	-	-	-	39,999	(20,399)	19,600
-	130,005	169,254	-	-	68,114	0
$ 105,114	$ 97,666	$ 145,079	$ 0	$ 76,541	$ 209,823	$ 4,461,249

Baxter Regional Health System

Consolidating Schedule – Statement of Changes in Net Assets Information

Year Ended December 31, 2016

	Baxter County Regional Hospital, Inc.	Hospice of the Ozarks, Inc.	Hospital Development Foundation, Inc.	Baxter Regional Health System	BRHS Hometown Clinics, Inc.
Unrestricted Net Assets					
Excess (deficiency) of revenues over expenses	$ 879,636	$ 707,829	$ (279,494)	$ (560,011)	$ (545,213)
Investment return – change in unrealized gains and losses on other-than-trading securities	2,761,001	467,988	68,501	-	-
Contributions of or for acquisition of property and equipment	373,362	-	320,800	-	-
Sale of member units	-	-	-	-	-
Transfers from (to) affiliates	(2,297,833)	-	-	1,175,961	754,499
Increase in unrestricted net assets	1,716,166	1,175,817	109,807	615,950	209,286
Temporarily Restricted Net Assets					
Contributions received	-	-	5,572	-	-
Investment return	484	-	1,274,659	-	-
Net assets released from restriction	-	-	(377,728)	-	-
Increase in temporarily restricted net assets	484	0	902,503	0	0
Change in Net Assets	1,716,650	1,175,817	1,012,310	615,950	209,286
Net Assets, Beginning of Year	63,669,180	12,516,020	14,094,713	(180,337)	(59,531)
Net Assets, End of Year	$ 65,385,830	$ 13,691,837	$ 15,107,023	$ 435,613	$ 149,755

BRMC Pain Center, LLC	SFP Clinic, LLC	BRCIM, LLC	BRCIN, LLC	Cancer Diagnostic Center	Eliminations	Consolidated
$ 105,114	$ (32,339)	$ (24,175)	$ -	$ 36,542	$ 535,470	$ 823,359
-	-	-	-	-	-	3,297,490
-	-	-	-	-	(373,362)	320,800
-	-	-	-	39,999	(20,399)	19,600
-	130,005	169,254	-	-	68,114	0
105,114	97,666	145,079	0	76,541	209,823	4,461,249
-	-	-	-	-	-	5,572
-	-	-	-	-	-	1,275,143
-	-	-	-	-	-	(377,728)
0	0	0	0	0	0	902,987
105,114	97,666	145,079	0	76,541	209,823	5,364,236
109,558	(97,666)	(145,079)	(11,948)	-	257,487	90,152,397
$ 214,672	$ 0	$ 0	$ (11,948)	$ 76,541	$ 467,310	$ 95,516,633