

Baystate Health, Inc. and Subsidiaries

Consolidated Financial Statements as of and
for the Years Ended September 30, 2016 and 2015,
Consolidating Supplementary Financial Information
as of and for the Year Ended September 30, 2016,
and Independent Auditors' Report

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Baystate Health, Inc.:

We have audited the accompanying consolidated financial statements of Baystate Health, Inc. and subsidiaries ("Baystate Health"), which comprise the consolidated statements of financial position as of September 30, 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 consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' 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 Baystate Health'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 Baystate Health'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 Baystate Health, Inc. and subsidiaries as of September 30, 2016 and 2015, and the results of their operations, their changes in net assets, and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Consolidating Supplementary Financial Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating supplementary financial information listed in the table of contents is presented for the purpose of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations, and cash flows of the individual companies and is not a required part of the consolidated financial statements. This consolidating supplementary financial information is the responsibility of Baystate Health's management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. Such consolidating supplementary financial information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such consolidating supplementary financial information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such consolidating supplementary financial information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Deloitte + Touche LLP

January 10, 2017

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION AS OF SEPTEMBER 30, 2016 AND 2015

(In thousands)

	2016	2015		2016	2015
ASSETS			LIABILITIES AND NET ASSETS		
CURRENT ASSETS:			CURRENT LIABILITIES:		
Cash and cash equivalents	\$ 192,890	\$ 182,971	Accounts payable	\$ 150,340	\$ 135,596
Investments	328,509	303,285	Medical claims payable	59,878	74,342
Accounts receivable, patients, less allowance for uncollectible accounts of \$36,715 in 2016 and \$33,683 in 2015	136,174	131,392	Accrued salaries and wages	95,665	110,593
Accounts receivable, other	56,885	45,652	Accrued interest payable	2,243	2,816
Estimated final settlements receivable	17,934	26,836	Estimated final settlements payable	39,556	50,812
Inventories	28,863	27,489	Deferred revenue	24,740	17,406
Prepaid expenses and other current assets	<u>24,505</u>	<u>29,312</u>	Current portion of long-term debt	13,016	30,960
Total current assets	<u>785,760</u>	<u>746,937</u>	Current portion of capital lease obligations	<u>5,063</u>	<u>3,690</u>
LONG-TERM ASSETS:			Total current liabilities	390,501	426,215
Investments	56,885	57,798	LONG-TERM DEBT	549,647	515,855
Equity investment in unconsolidated affiliates	2,673	2,287	CAPITAL LEASE OBLIGATIONS	17,673	8,212
Notes receivable	69,344	68,516	PENSION LIABILITY	133,908	117,724
Deferred expense and other long-term assets	36,617	18,091	INSURANCE LIABILITY LOSS RESERVES	126,616	123,535
Goodwill	5,684	5,684	OTHER LIABILITIES	<u>54,886</u>	<u>47,982</u>
Land, buildings, and equipment, net	<u>714,632</u>	<u>711,620</u>	Total liabilities	<u>1,273,231</u>	<u>1,239,523</u>
	<u>885,835</u>	<u>863,996</u>	NET ASSETS:		
ASSETS WHOSE USE IS LIMITED:			Unrestricted:		
Board-designated funds	269,526	246,977	Operating	1,144,311	1,074,094
Investments of captive insurance company	84,808	108,576	Pension adjustment	<u>(405,452)</u>	<u>(347,052)</u>
Investments held by trustee under debt agreements	15,272	34,390	Total unrestricted	738,859	727,042
Beneficial interest in perpetual trusts	35,569	34,162	Temporarily restricted	57,381	55,040
Deferred compensation investments	<u>46,200</u>	<u>38,461</u>	Permanently restricted	<u>53,499</u>	<u>51,894</u>
	451,375	462,566	Total net assets	<u>849,739</u>	<u>833,976</u>
TOTAL ASSETS	<u>\$2,122,970</u>	<u>\$2,073,499</u>	TOTAL LIABILITIES AND NET ASSETS	<u>\$2,122,970</u>	<u>\$2,073,499</u>

See notes to consolidated financial statements.

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED SEPTEMBER 30, 2016 AND 2015 (In thousands)

	2016	2015
OPERATING REVENUES:		
Net patient service revenue	\$ 1,338,863	\$ 1,242,785
Bad debts	<u>(29,846)</u>	<u>(20,743)</u>
Net patient service revenue, net of bad debts	1,309,017	1,222,042
Premiums	944,172	821,995
Other revenue	94,112	89,364
Net assets released from restrictions for operations	<u>5,634</u>	<u>5,160</u>
Total operating revenues	<u>2,352,935</u>	<u>2,138,561</u>
OPERATING EXPENSES:		
Salaries and wages	868,551	811,397
Supplies and expense	725,368	687,235
Medical claims and capitation	625,463	569,696
Depreciation and amortization	75,542	69,207
Interest expense	<u>11,387</u>	<u>10,892</u>
Total operating expenses	<u>2,306,311</u>	<u>2,148,427</u>
INCOME (LOSS) FROM OPERATIONS BEFORE OTHER INCOME	46,624	(9,866)
OTHER (EXPENSE) INCOME, Net	<u>(17,643)</u>	<u>69,651</u>
INCOME FROM OPERATIONS	<u>28,981</u>	<u>59,785</u>
NONOPERATING INCOME (LOSS):		
Investment income	2,343	6,225
Net realized gain on investments	38,360	9,810
Net unrealized gain (loss) on investments	11,034	(40,548)
Equity gain (loss) in unconsolidated affiliates	74	(312)
Net interest cost on swap agreements	(1,633)	(1,964)
Change in fair value of swap agreements	702	(84)
Income taxes and other	<u>(19,454)</u>	<u>1,105</u>
Total nonoperating income (loss)	<u>31,426</u>	<u>(25,768)</u>
EXCESS OF REVENUES OVER EXPENSES	60,407	34,017
OTHER CHANGES IN UNRESTRICTED NET ASSETS:		
Net assets released from restrictions for capital	3,327	3,618
Funds utilized for property and equipment	400	2,095
Transfers from restricted net assets	-	136
Contributed capital asset	6,084	-
Pension adjustment	(58,400)	(115,780)
Other	<u>(1)</u>	<u>(138)</u>
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	<u>\$ 11,817</u>	<u>\$ (76,052)</u>

See notes to consolidated financial statements.

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS FOR THE YEARS ENDED SEPTEMBER 30, 2016 AND 2015 (In thousands)

	2016	2015
UNRESTRICTED NET ASSETS:		
Excess of revenues over expenses	\$ 60,407	\$ 34,017
Net assets released from restrictions for capital	3,327	3,618
Funds utilized for property and equipment	400	2,095
Transfers from restricted net assets	-	136
Contributed capital asset	6,084	-
Pension adjustment	(58,400)	(115,780)
Other	(1)	(138)
	<u>11,817</u>	<u>(76,052)</u>
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS		
	<u>11,817</u>	<u>(76,052)</u>
TEMPORARILY RESTRICTED NET ASSETS:		
Restricted investment income	223	243
Net realized and unrealized gain (loss) on investments	4,849	(2,506)
Contributions	6,488	7,263
Transfers to unrestricted net assets	-	(136)
Net assets released from restrictions:		
For operations	(5,634)	(5,160)
For capital	(3,327)	(3,618)
Net assets from acquired subsidiary	-	4,024
Other	(258)	319
	<u>2,341</u>	<u>429</u>
INCREASE IN TEMPORARILY RESTRICTED NET ASSETS		
	<u>2,341</u>	<u>429</u>
PERMANENTLY RESTRICTED NET ASSETS:		
Contributions	198	359
Change in fair value of perpetual trusts	1,407	(3,226)
Net assets from acquired subsidiary	-	881
	<u>1,605</u>	<u>(1,986)</u>
INCREASE (DECREASE) IN PERMANENTLY RESTRICTED NET ASSETS		
	<u>1,605</u>	<u>(1,986)</u>
INCREASE (DECREASE) IN NET ASSETS		
	15,763	(77,609)
NET ASSETS—Beginning of year		
	<u>833,976</u>	<u>911,585</u>
NET ASSETS—End of year		
	<u>\$ 849,739</u>	<u>\$ 833,976</u>

See notes to consolidated financial statements.

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2016 AND 2015 (In thousands)

	2016	2015
OPERATING ACTIVITIES:		
Increase (decrease) in net assets	\$ 15,763	\$ (77,609)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation and amortization	75,542	69,207
Accretion on notes receivable	(1,401)	(1,382)
Pension adjustment	58,400	115,780
Net realized and unrealized (gain) loss on investments	(56,096)	32,564
Provision for bad debts	29,846	20,743
Change in fair value of perpetual trusts	(1,407)	3,226
Restricted contributions	(6,686)	(7,622)
Changes in equity investment of affiliate	(194)	(2,345)
Contributed capital asset	(6,084)	-
Net assets from acquired subsidiary	-	(773)
Changes in operating assets and liabilities:		
Accounts receivable, patients	(34,628)	(5,622)
Net estimated final settlements	(2,354)	(19,632)
Accounts payable and accrued expenses	(1,243)	15,839
Pension liability	(42,216)	(98,211)
Medical claims payable	(14,464)	25,769
Insurance liability loss reserves	3,081	(2,822)
Other	(20,387)	(15,728)
Net cash (used in) provided by operating activities	<u>(4,528)</u>	<u>51,382</u>
INVESTING ACTIVITIES:		
Proceeds from sale and maturities of investments	904,674	777,263
Purchase of investments	(852,347)	(805,160)
Cash acquired in acquisitions	-	1,202
Purchase of land, buildings, and equipment	<u>(78,023)</u>	<u>(100,185)</u>
Net cash used in investing activities	<u>(25,696)</u>	<u>(126,880)</u>
FINANCING ACTIVITIES:		
Proceeds from restricted contributions	6,686	7,622
Repayment of notes receivable	573	713
Proceeds from debt issuance	71,304	82,797
Repayments of debt and capital lease obligations	<u>(38,420)</u>	<u>(11,738)</u>
Net cash provided by financing activities	<u>40,143</u>	<u>79,394</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	9,919	3,896
CASH AND CASH EQUIVALENTS—Beginning of year	<u>182,971</u>	<u>179,075</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 192,890</u>	<u>\$ 182,971</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest	<u>\$ 14,340</u>	<u>\$ 13,533</u>

See notes to consolidated financial statements.

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED SEPTEMBER 30, 2016 AND 2015

1. ORGANIZATION

Baystate Health, Inc. (“Baystate Health” or BH), based in Springfield, Massachusetts, is the parent corporation of an integrated health care delivery system with the mission “to improve the health of the people in our community every day, with quality and compassion.”

Baystate Health currently includes the following:

- Baystate Medical Center, Inc. (BMC), located in Springfield, Massachusetts, is the largest of the five hospitals in the Baystate Health system. BMC, the leading health facility in western Massachusetts, is the only tertiary care referral medical center and Level 1 trauma center in the region. It is also home to western New England’s only neonatal and pediatric intensive care units. BMC is a 718-bed, tax-exempt, not-for-profit, academic teaching hospital.
- Baystate Total Home Care, Inc. (BTHC) is a tax-exempt, not-for-profit corporation, which is organized to benefit, support, and further the charitable activities of BMC by holding, leasing, improving, and managing real estate held by, or acquired on behalf of, BMC. BTHC serves as the operating entity in connection with the new markets tax credit (NMTC) financing for the BMC Expansion Project.
- Baystate Franklin Medical Center, Inc. (BFMC), located in Greenfield, Massachusetts, is an 89-bed, tax-exempt, not-for-profit, acute care community hospital. BFMC serves the northern tier of northwestern Massachusetts and southern Vermont.
- Baystate Wing Hospital Corporation (BWH), located in Palmer, Massachusetts, is a 74-bed, tax-exempt, not-for-profit, acute care community hospital acquired in 2014.
 - Baystate Mary Lane Hospital Corporation (BMLH), located in Ware, Massachusetts, was a 25-bed, tax-exempt, not-for-profit, acute care community hospital. BMLH was merged into BWH as of September 10, 2016, and BMLH no longer provides inpatient services.
- Baystate Noble Hospital, Inc. and subsidiaries (“BNH consolidated”) consists of three tax-exempt, not-for-profit corporations located in Westfield, Massachusetts, acquired in 2015:
 - Baystate Noble Hospital, Inc. (BNH) is a 97-bed, tax-exempt, not-for-profit acute care community hospital. BNH provides inpatient, outpatient, and emergency care services for residents in the greater Westfield community. BNH is the sole corporate member of the following organizations:
 - Baystate Westfield Medical Corporation (WMC) is a tax-exempt, not-for-profit physician practice that provides medical services to residents of the greater Westfield community.
 - Baystate Noble Visiting Nurse and Hospice Services, Inc. (BNVNAH) is a tax-exempt, not-for-profit community-based home health care and hospice agency, whose primary purpose is to provide home health services and promote and maintain community health to the city of Westfield and surrounding communities.

- Baystate Medical Practices, Inc. (BMP) is a tax-exempt, not-for-profit organization formed in 2010. BMP includes a multispecialty academic group practice established to support the educational and research programs of Baystate Health, as well as numerous primary care and outreach services. BMP also includes community-based primary care (internists and pediatricians), medical and surgical practices, obstetrical and gynecological, and hospitalist physicians dedicated to the care and management of patients hospitalized at BH-affiliated hospitals. BMP also provides preventative, diagnostic, and therapeutic health services enhancing the cardiovascular clinical, educational, community, and research activities for BH and its service area.
- Baystate Visiting Nurse Association & Hospice (BVNAH) is a tax-exempt, not-for-profit organization that provides comprehensive home health care committed to providing the highest quality care to patients and families, primarily in the home setting. BVNAH meets individual needs by bringing experienced nurses, rehabilitation therapists, social workers, and home care aides to patients' homes.
- Health New England, Inc. (HNE) is a tax-exempt, not-for-profit health maintenance organization located in Springfield, Massachusetts. HNE's service area in Massachusetts includes Franklin, Berkshire, Hampden, and Hampshire counties and parts of Worcester County. HNE also serves Hartford, Litchfield, and Tolland counties in Connecticut. HNE includes the following subsidiaries:
 - HNE Holding Company, which is the parent company of HNE Advisory Services, Inc. (HAS); Health New England Insurance Services, Inc. (HIS); and HNE Insurance Company, Inc. (HIC); three for-profit subsidiaries. Through HAS, HNE provides administrative services for self-insured employee health benefit plans sponsored by employer groups. HIS provides insurance brokerage services. Through HIC, an insurance subsidiary, HNE provides the Medicare Supplement line of business that began coverage on January 1, 2013.
 - HNE of Connecticut, Inc. is a not-for-profit insurance subsidiary that services the health insurance needs of the Connecticut population.
- Ingraham Corporation (IC) is a for-profit, taxable corporation that served as a holding company for Baystate Health Ambulance, Inc. (BHA).
 - BHA was a for-profit, taxable corporation that delivered mobile critical care providing 24-hour service throughout western New England. On May 24, 2014, BH exited this business line through a sale of all BHA's fixed assets to a third party and was dissolved during 2015.
- Baystate Administrative Services, Inc. is a tax-exempt, not-for-profit corporation that provides management support for the BH subsidiaries, including human resources, marketing, strategic planning, information services, and financial services.
- Baystate Health Foundation, Inc. (BHF) is a tax-exempt, charitable organization established for the purpose of fund-raising for healthcare-related activities, in support, and for the benefit, of BH and those subsidiaries of BH that are tax-exempt, not-for-profit corporations and to hold endowment, charitable donations, and other funds for their benefit.
- Baystate Health Insurance Company, Ltd. (BHIC) is a captive insurance company organized and licensed in the Cayman Islands, British West Indies. BHIC provides professional liability and other insurance coverage to the corporate members of BH and their employees. In 2004, BHIC began offering malpractice insurance to members of BH's medical staff who meet criteria for participation.

2. SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation—The accompanying consolidated financial statements include the accounts of BH and its subsidiaries noted above. All intercompany and subsidiary accounts and transactions have been eliminated in consolidation.

Use of Estimates—The preparation of consolidated 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates are made in the areas of the allowance for uncollectible accounts receivable, reserve for contractual allowances, investment valuation, estimated final settlements receivable and payable, medical claims payable, insurance liability loss reserves, income taxes, pension liability, and the fair value of assets acquired and liabilities assumed (see Note 3).

Net Assets—Baystate Health and its subsidiaries report net assets and revenues, expenses, gains, and losses based upon the existence or absence of donor-imposed restrictions. In the accompanying consolidated financial statements, net assets that have similar characteristics have been combined into the following categories:

Unrestricted—Net assets that are not subject to donor-imposed stipulations. Net assets may be designated for specific purposes by action of the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.

Temporarily Restricted—Net assets whose use by Baystate Health and its subsidiaries are subject to donor-imposed stipulations that can be fulfilled by actions of Baystate Health and its subsidiaries or that expire by the passage of time. At September 30, 2016 and 2015, temporarily restricted net assets consist of amounts restricted as to spending for various purposes, such as education, research, clinical, and health care programs, as well as cumulative net appreciation of permanently restricted funds which is available for governing board appropriation.

Permanently Restricted—Net assets subject to donor-imposed stipulations that they be maintained permanently by Baystate Health and its subsidiaries. At September 30, 2016 and 2015, permanently restricted net assets consist of the original cost of permanent endowment gifts and beneficial interests in perpetual trusts.

Revenues from sources other than donor-restricted contributions are reported as increases in unrestricted net assets. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets, unless their use is restricted by explicit donor stipulations or by law. Expirations of temporary restrictions recognized on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as releases from temporarily restricted net assets to unrestricted net assets. Temporary restrictions on gifts to acquire long-lived assets are considered met in the period in which the assets are acquired or placed in service.

Contributions, including unconditional promises to give and grant awards, are recognized as revenues in the period received. Contributions received with donor-imposed restrictions are reported as permanently or temporarily restricted, depending upon the specific restriction. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair values at the date of the gift. Contributions to be received

after one year are discounted at a risk-free rate commensurate with the expected payment term. Amortization of the discount is recorded as contribution revenue in the appropriate net asset category. Allowance is made for uncollectible contributions based upon management's judgment and analysis of the creditworthiness of the donors, past collection experience, and other relevant information.

Cash and Cash Equivalents—Cash and cash equivalents include all highly liquid investments with a maturity of three months or less when purchased.

Investments—Investments include cash equivalents, mutual funds, fixed-income securities, as well as interests in limited partnerships, hedge funds, and common collective trusts. Investments in equity securities with readily determinable fair values and all investments in debt securities are recorded at estimated fair value in the consolidated statements of financial position. The accounting for the investments held by the pension plan is discussed in Note 17.

Baystate Health has also entered into partnership agreements with limited partnerships ("alternative investments"), the majority of which are in private markets, whereby they have agreed to certain capital commitments. Baystate Health's policy is to record its ownership interest in these alternative investments of less than 5% at the lower of cost or market. For those alternative investments where the ownership interest is more than 5%, the ownership interests are reported using the equity method of accounting. As of September 30, 2016, approximately \$35,691,000 of total capital commitments, including those held within the pension plan assets discussed in Note 17, remain outstanding. Certain of the partnerships may hold some securities without readily determinable fair values and, consequently, the general partner may estimate fair value for such securities. These estimates may differ significantly from the values that would have been used had a ready market existed and may also differ significantly from the values at which such investments may be sold and the differences could be material.

Interest and dividends on investments are included in other revenue or nonoperating income (loss) in the consolidated statements of operations, unless the income or loss is restricted by donor or law. Realized gains and losses and unrealized gains and losses on investments are included in nonoperating income (loss) or temporarily restricted net assets, as applicable. Investment-related expenses, such as custodial fees and investment fees, are netted against investment revenues and are immaterial for the years ended September 30, 2016 and 2015.

Baystate Health and its subsidiaries have elected the fair value option for certain of their investments. Baystate Health made this election to reflect changes in fair value of its investments, including both increases and decreases and whether realized or unrealized, in its excess of revenue over expenses. Within excess revenues over expenses, Baystate Health recognized net unrealized gains on investments totaling \$11,034,000 in 2016 as compared to net unrealized losses on investments totaling \$40,548,000 in 2015.

Certain investments are included in pooled investment funds. Current market value is used to determine the percent of each fund in the pool. Income from investments of a pool, including gains or losses, is allocated to participating funds based on the respective fund's percentage of the pool.

Inventories—Inventories are stated at the lower of cost (principally first-in, first-out method) or market.

Notes Receivable—In December 2009 and May 2009, BMC loaned \$31,186,783 and \$32,617,500, respectively, to a third party relating to project costs of approximately \$252,000,000 for the construction of a new hospital facility at 759 Chestnut Street, Springfield, Massachusetts. The loans are part of a financing arrangement that utilizes NMTCs to reduce cash required by BMC to construct this new facility. Each loan bears interest at 2.139% annually, with annual cash payments during the first seven years of the 33-year term based on an interest rate of 1.00%. The notes are recorded as notes receivable in the consolidated statements of financial position as of September 30, 2016 and 2015.

Equity Investment in Unconsolidated Affiliates—Baystate Health participates in joint ventures with 50% or less ownership and accounts for the investment in those unconsolidated affiliates as equity investments.

Deferred Expenses and Other Long-Term Assets—Deferred expenses include unamortized bond issuance expenses of approximately \$3,743,000 and \$4,025,000 as of September 30, 2016 and 2015, respectively, which are amortized over the weighted-average terms of the bonds.

Goodwill—Goodwill is assessed annually for indicators of impairment on July 1 of each year. There were no such indicators in the years ended September 30, 2016 and 2015.

Assets Whose Use is Limited—Assets whose use is limited include assets held by the trustee under indenture agreements and designated assets set aside by the Board of Trustees for future capital improvements and other strategic initiatives, which are in furtherance of Baystate Health and its subsidiaries' exempt and charitable purposes. Also included are investments of the captive insurance company, deferred compensation investments, and beneficial interests in perpetual trusts.

Land, Buildings, and Equipment—Land, buildings, and equipment are stated at cost, less depreciation and amortization determined on the straight-line basis.

Maintenance and repairs are charged to expense as incurred. Betterments and major renewals are capitalized. Cost of assets sold or retired and the related amounts of accumulated depreciation are eliminated from the accounts in the year of disposal and the resulting gain or loss is included in other revenue. Buildings and equipment under capital lease obligations are amortized using the straight-line method over the shorter period of the lease term or the estimated useful life. Useful life is assigned in accordance with the American Hospital Association's guide, *Estimated Useful Lives of Depreciable Hospital Assets*. Such amortization is included in depreciation and amortization in the consolidated statements of operations. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Consolidated Statements of Operations—All activities of Baystate Health deemed by management to be ongoing and central to the provision of health care services are reported as operating revenues and expenses. Other (expense) income, net in the consolidated statements of operations for the year ended September 30, 2016, consists of severance and benefit costs related to a reduction in force. Included in other income, net in the consolidated statements of operations for the year ended September 30, 2015, is a pension curtailment credit of approximately \$71,400,000 (see Note 17), net of severance charges of approximately \$1,700,000. Other activities are considered nonoperating and include board-designated investment income and realized gains and losses, unrealized gains and losses on investments, investment return on deferred compensation plan investments and related compensation expense, changes in BHIC loss reserves, equity gains and losses in unconsolidated affiliates, contributions of net assets from acquired subsidiaries, interest on swap agreements, changes in fair value of swap agreements, income taxes, and acquisition-related costs associated with the purchase of BNH consolidated.

The consolidated statements of operations include excess of revenues over expenses as the performance indicator. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses, include net assets released from restrictions for capital, contributed capital asset, funds utilized for property and equipment, transfers to restricted net assets, and the pension adjustment.

Net Patient Service Revenue—Net patient service revenue is reported at estimated net realizable amounts from patients, third-party payers, and others for services rendered and includes estimated retroactive revenue adjustments due to future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related

services are rendered and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. Contracts, laws, and regulations governing Medicare, Medicaid, Blue Cross, and the Health Safety Net (HSN) programs are 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. Blue Cross and other managed care plans have negotiated with Baystate Health and its subsidiaries various forms of contractual payment rates. The most common payment rates include discounted charges, per case, per diems, and fee schedules.

Medicaid payment rates are negotiated between the Division of Medical Assistance and individual hospitals. Medicare Prospective Payment System (PPS) regulations determine payment due acute care hospitals for inpatient services provided to Medicare beneficiaries. Medicare payments for outpatient services are a blend of PPS and fee schedules.

During 2016 and 2015, Baystate Health recorded adjustments to amounts accrued for settlements related to prior fiscal years. The net effect of such adjustments was an increase to net patient service revenue of approximately \$29,215,000 and \$24,065,000 in 2016 and 2015, respectively.

Medicare and Medicaid Electronic Health Record (EHR) Program—Certain health care providers can earn up to four incentive payments between federal fiscal years 2011 and 2016 if certain specific program criteria are met. In the initial year, the providers are required to establish an EHR system and maintain its meaningful use status for a continuous 90-day period. In subsequent years, such meaningful use must be maintained for the entire 365-day federal fiscal year. Baystate Health records the revenue related to this program when management is reasonably assured that Baystate Health has complied with the terms of the program.

Baystate Health has included approximately \$3,587,000 and \$6,078,000 in other revenue related to the program in fiscal years 2016 and 2015, respectively. The estimate is based on cost report data, which is subject to audit, and the amounts recognized are subject to change. Baystate Health's attestation of compliance with the meaningful use criteria is subject to audit by the federal or state government or its designee.

Premium Revenue—Premium revenue represents insurance membership contract revenue at HNE. The contracts generally cover a 12-month period and are subject to cancellation by the employer group or HNE upon 30 days' written notice. Premiums are due monthly and are recognized as revenue during the period in which HNE is obligated to provide services to members.

HNE enters into risk-sharing arrangements with certain providers and payors, whereby a settlement amount is calculated based on actual medical claims experience as compared to budgeted amounts or a pre-determined risk corridor, based upon contractual arrangements. These settlements are estimated and accrued during the period the related services were rendered and adjusted in future periods as final settlements are determined. During 2016, HNE recorded adjustments to amounts accrued for risk sharing settlements related to the prior fiscal year as a change in estimate. The net effect of the adjustments was an increase in premium revenue of approximately \$9,600,000 and \$0, in 2016 and 2015, respectively.

Medical Claims and Capitation—Net—The cost of medical claims and capitation is accrued for in the period in which services are provided and include certain estimated amounts. The estimates for claims expense may be more or less than the amounts ultimately paid when the claims are settled. Such changes in estimates are reflected in the consolidated statements of operations.

HSN—In April 2006, the Commonwealth of Massachusetts passed Chapter 58 of the Acts of 2006, “An Act Providing Access to Affordable, Quality, Accountable Health Care;” the goal of which is to provide near-universal health insurance coverage to Massachusetts residents through a combination of Medicaid expansions, subsidized private insurance programs, insurance market reforms, and the HSN.

The HSN reimburses hospitals for uncompensated care based on actual services provided at rates approximating the PPS, subject to available funds. Like its predecessor, the Uncompensated Care Pool, the HSN is partially funded by acute hospitals through an assessment on gross charges billed to nongovernmental payers.

Charity Care and Community Support—It is the policy of Baystate Health to provide care to any patient in need of medical care, regardless of the patient’s ability to pay for such care. Based upon the patient’s financial capability to pay, such care is provided free of charge or at amounts below normal charges. Because amounts determined to qualify as charity care are not pursued, they are not reported as revenue. The net cost of charity care includes the direct and indirect cost of providing charity care services, offset by revenues received from indigent care pools (primarily the HSN). The cost is estimated by utilizing a ratio of cost to gross charges applied to the gross uncompensated care charges associated with providing charity care.

The costs of charity care provided during the years ended September 30, 2016 and 2015, are as follows (in thousands):

	2016	2015
HSN assessment	\$ 6,742	\$ 6,379
HSN receipts	(6,488)	(6,731)
Free care (at cost)	<u>14,054</u>	<u>12,245</u>
 Total	 <u>\$ 14,308</u>	 <u>\$ 11,893</u>

In addition to the charity care provided to patients, Baystate Health and its subsidiaries have ongoing community outreach initiatives in the areas of health services access, education, safety, and community reinvestment. The initiatives include freestanding health centers, improving school-based health services, implementing an immunization tracking system to link preschool-aged children to primary care providers, youth development programs, increasing minority employment, improving the community’s health status, wellness, health and safety programs for senior citizens, and health screenings and forums.

Allowance for Uncollectible Accounts—Accounts receivable are reduced by an allowance for uncollectible accounts. In evaluating the collectibility of accounts receivable, Baystate Health analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for uncollectible accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for uncollectible accounts. For receivables associated with services provided to patients who have third-party coverage, Baystate Health analyzes contractually due amounts and provides an allowance for uncollectible accounts and a provision for bad debts, if necessary. For receivables associated with self-pay patients, Baystate Health records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for uncollectible accounts.

Baystate Health's allowance for uncollectible accounts for self-pay patients decreased from 95% of self-pay accounts receivable at September 30, 2015, to approximately 91% of self-pay accounts receivable at September 30, 2016. In addition, Baystate Health's self-pay write-offs, net of recoveries increased approximately \$8,081,000 from \$45,023,000 for fiscal year 2015 to \$53,104,000 for fiscal year 2016. Baystate Health has not changed its charity care or uninsured discount policies during fiscal year 2015 or 2016. Baystate Health does not maintain a material allowance for uncollectible accounts from third-party payers nor did it have significant write-offs from third-party payers. Baystate Health 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 who do not qualify for charity care, Baystate Health recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy).

Net patient service revenue (after contractual allowances and discounts) recognized during the years ended September 30, 2016 and 2015, from Baystate Health's major payer sources is as follows (in thousands):

	2016	2015
Medicare	\$ 591,018	\$ 521,153
Medicaid	213,397	206,683
Commercial and other	519,993	501,872
Self-pay	<u>14,455</u>	<u>13,077</u>
Total	<u>\$1,338,863</u>	<u>\$1,242,785</u>

Impairment of Long-Lived Assets—Long-lived assets to be held and used are reviewed for impairment whenever circumstances indicate that the carrying amount of an asset may not be recoverable. Long-lived assets to be disposed of are reported at the lower of the carrying amount or fair value, less cost to sell.

Research Grants and Contracts—Revenue related to research grants and contracts is recognized as the related costs are incurred. Indirect costs relating to certain government grants and contracts are reimbursed at fixed rates negotiated with the government agencies. Research grants and contracts have been accounted for as exchange transactions. Amounts received in advance of incurring the related expenditures are recorded as unexpended research grants and are included with deferred revenue in the accompanying consolidated statements of financial position.

Accounting for Defined Benefit Pension and Other Postretirement Plans—Baystate Health recognizes the overfunded or underfunded status of its defined benefit and postretirement plans as an asset or liability in its consolidated statements of financial position. Changes in the funded status of the plans are reported as a change in unrestricted net assets presented below the excess of revenues over expenses in the consolidated statements of operations and changes in net assets in the year in which the changes occur.

Income Taxes—All of Baystate Health's consolidated entities are recognized by the Internal Revenue Service as tax-exempt, not-for-profit organizations under Section 501(c)(3) of the Internal Revenue Code (IRC), except for BHIC and IC. HNE is exempt under IRC 501(c)(4).

New Accounting Pronouncements—In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-15, *Classification of Certain Cash Receipts and Cash Payments*. This guidance adds or clarifies guidance on the classification of certain

cash receipts and payments in the consolidated statements of cash flows. This guidance is effective for Baystate Health beginning October 1, 2019. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In August 2016, the FASB issued ASU No 2016-14, *Presentation of Financial Statements of Not-For-Profit Entities*. This guidance simplifies and improves how not-for-profit entities classify net assets as well as the information presented in financial statements and notes about liquidity, financial performance, and cash flows. This guidance is effective for Baystate Health beginning October 1, 2018. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In May 2016, the FASB issued ASU No. 2016-12, *Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients*, which amends certain aspects of the FASB's revenue standard ASU No. 2014-09, *Revenue from Contracts with Customers*. In March 2016, the FASB issued ASU No. 2016-08, *Revenue from Contracts with Customers: Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)*. This guidance amends the principal versus agent implementation guidance and illustrations in the FASB's revenue standard, ASU No. 2014-09. In July 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which defers the effective date of the FASB's revenue standard, ASU No. 2014-09, by one year for all entities and permits early adoption on a limited basis. In May 2014, the FASB issued ASU No. 2014-09. This guidance outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. After the deferral of the effective date, this guidance is effective for Baystate Health beginning October 1, 2018. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-07, *Investments—Equity Method and Joint Ventures: Simplifying the Transition to the Equity Method of Accounting*. This guidance eliminates the requirement to retrospectively apply the equity method to an investment that subsequently qualifies for such accounting as a result of an increase in the level of ownership interest or degree of influence. This guidance is effective for Baystate Health beginning October 1, 2017. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. This guidance introduces a lessee model that brings substantially all leases on the consolidated balance sheet. This guidance is effective for Baystate Health beginning October 1, 2019. Retrospective application is required. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. This guidance revises accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments. This guidance is effective for Baystate Health beginning October 1, 2019. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In September 2015, the FASB issued ASU No. 2015-16, *Simplifying the Accounting for Measurement-Period Adjustments*. This guidance requires an acquirer in a business combination to recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The effect on earnings of changes in depreciation or amortization, or other income effects (if any) as a result of the change to the provisional amounts, calculated as if the accounting had been completed as of the acquisition date, must be recorded

in the reporting period in which the adjustment amounts are determined rather than retrospectively. Also, the acquirer must present separately on the face of the income statement, or disclose in the notes, the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. This guidance is effective for Baystate Health beginning October 1, 2017. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In July 2015, the FASB issued ASU No. 2015-11, *Simplifying the Measurement of Inventory*. This guidance requires entities to measure most inventories at the lower of cost or net realizable value. This guidance is effective for Baystate Health beginning October 1, 2017. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

In May 2015, the FASB issued ASU No. 2015-09, *Disclosures about Short-Duration Contracts*. This guidance expands the disclosures that an insurance entity must provide about its short-duration insurance contracts. This guidance is effective for Baystate Health beginning October 1, 2017. Baystate Health is still evaluating the impact this guidance may have on its consolidated financial statements.

3. ACQUISITION

Baystate Noble—Effective July 1, 2015, Baystate Health acquired The Trustees of Noble Hospital, Inc and subsidiaries (“Noble”). Noble was renamed Baystate Noble Hospital, Inc. following the acquisition. The acquisition is expected to have a positive impact on quality, access, and affordability of health care in western Massachusetts. No cash consideration was paid in connection with the transaction.

The consolidated statement of operations for 2015 includes the operations of BNH consolidated since the date of acquisition. In 2015, the consolidated statement of operations includes total operating revenues of approximately \$20,145,000 related to BNH consolidated and deficiency of revenues over expenses of approximately \$311,000.

This transaction was accounted for as an acquisition in accordance with ASU No. 2010-07, *Not-for-profit Entities (Topic 958): Mergers and Acquisitions*, which required the assets and liabilities of BNH consolidated to be accounted for at fair value, as of the date of acquisition.

The amounts assigned to BNH consolidated major assets and liabilities at the acquisition date are as follows (in thousands):

Fair value of assets acquired:	
Current assets	\$ 9,842
Property, plant, and equipment	19,463
Other noncurrent assets	<u>4,426</u>
Total	<u>33,731</u>
Fair value of liabilities assumed:	
Current liabilities	21,662
Long-term liabilities	<u>11,296</u>
Total	<u>32,958</u>
Fair value of net assets acquired	<u>\$ 773</u>
Contribution of net assets from acquired subsidiary	<u>\$ 773</u>

Components of the \$773,000 include an unrestricted net deficit of \$4,132,000, temporarily restricted net assets of \$4,024,000, and permanently restricted net assets of \$881,000. The \$4,132,000 unrestricted net deficit is recorded as goodwill in the accompanying consolidated statements of financial position.

Costs related to the acquisition totaled approximately \$706,000 and are included in nonoperating income (loss) as income taxes and other in the 2015 consolidated statement of operations.

The fair value adjustments required to account for the Noble acquisition have been recorded in the consolidated financial statements of BNH consolidated.

4. CASH, INVESTMENTS, AND ASSETS WHOSE USE IS LIMITED

The composition of cash, investments, and assets whose use is limited at September 30, 2016 and 2015, is as follows (in thousands):

	2016	2015
Cash and cash equivalents	\$ 207,041	\$ 166,457
Mutual funds	218,335	305,415
Fixed-income securities	163,932	161,333
Alternative investments—limited partnerships	33,126	36,467
Domestic equity securities	49,595	2,874
Beneficial interests in perpetual trusts	35,569	34,162
Commingled equity mutual funds	59,146	104,817
Commingled emerging markets funds	53,239	16,579
Commingled commodity funds	10,474	24,528
Commingled other funds	68,281	83,800
Hedge fund of funds	67,303	70,188
Commingled master limited partnership	37,216	-
Commingled hedge fund	<u>26,402</u>	<u>-</u>
	<u>\$ 1,029,659</u>	<u>\$ 1,006,620</u>

Cash, investments, and assets whose use is limited at September 30, 2016 and 2015, are included in the consolidated statements of financial position as follows (in thousands):

	2016	2015
Cash and cash equivalents	\$ 192,890	\$ 182,971
Investments	328,509	303,285
Long-term investments	56,885	57,798
Board-designated cash and investments	269,526	246,977
Investments of captive insurance company	84,808	108,576
Investments held by trustee under debt agreements	15,272	34,390
Beneficial interests in perpetual trusts	35,569	34,162
Deferred compensation investments	<u>46,200</u>	<u>38,461</u>
	<u>\$ 1,029,659</u>	<u>\$ 1,006,620</u>
Investment income included in other revenue	<u>\$ 4,752</u>	<u>\$ 8,978</u>

5. FAIR VALUE MEASUREMENTS

Baystate Health calculates fair value as described in Accounting Standards Codification (ASC) 820-10, *Fair Value Measurements and Disclosures: Overall*, to value its financial assets and liabilities, when applicable. Fair value is based on 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. In order to increase consistency and comparability in fair value measurements, ASC 820-10 establishes a three-level valuation hierarchy that prioritizes observable and unobservable inputs used to measure fair value. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

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

Level 2—Observable inputs that are based on inputs not quoted in active markets, but corroborated by market data.

Level 3—Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. In determining fair value, Baystate Health utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, as well as consider counterparty credit risk in its assessment of fair value.

As a result of the adoption of ASU No. 2015-07 *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, investments for which the fair value is measured using the net asset value (NAV) per share as a practical expedient are not categorized within the fair value hierarchy.

Financial assets and liabilities carried at fair value for the years ended September 30, 2016 and 2015, are classified in the table below in one of the three categories described above (in thousands):

	Assets at Fair Value at September 30, 2016			
	Level 1	Level 2	Level 3	Total
Assets:				
Cash equivalents	<u>\$207,041</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 207,041</u>
Mutual funds:				
Corporate bond fund	83,147	-	-	83,147
Deferred compensation investments:				
Corporate bond fund	5,970	-	-	5,970
Other	40,230	-	-	40,230
Other	<u>88,988</u>	<u>-</u>	<u>-</u>	<u>88,988</u>
Total mutual funds	<u>218,335</u>	<u>-</u>	<u>-</u>	<u>218,335</u>
Fixed-income securities—corporate bonds and US government securities	<u>-</u>	<u>163,932</u>	<u>-</u>	<u>163,932</u>
Total fixed-income securities	<u>-</u>	<u>163,932</u>	<u>-</u>	<u>163,932</u>
Domestic equity securities	<u>49,595</u>	<u>-</u>	<u>-</u>	<u>49,595</u>
Beneficial interests in perpetual trusts	<u>-</u>	<u>-</u>	<u>35,569</u>	<u>35,569</u>
Total assets at fair value	<u>\$474,971</u>	<u>\$163,932</u>	<u>\$35,569</u>	<u>674,472</u>
Alternative investments (at cost)				<u>33,126</u>
Investments measured at NAV:				
Commingled domestic equity funds				19,360
Commingled international equity funds				39,786
Commingled emerging markets funds				53,239
Commingled commodity funds				10,474
Commingled—other funds				68,281
Hedge fund of funds				67,303
Commingled master limited partnerships				37,216
Commingled hedge fund				<u>26,402</u>
Total investments measured at NAV				<u>322,061</u>
Total assets				<u>\$1,029,659</u>
Liabilities—interest rate swap agreements	<u>\$ -</u>	<u>\$ 5,156</u>	<u>\$ -</u>	<u>\$ 5,156</u>

	Assets at Fair Value at September 30, 2015			
	Level 1	Level 2	Level 3	Total
Assets:				
Cash equivalents	<u>\$ 166,457</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 166,457</u>
Mutual funds:				
Corporate bond fund	133,960	-	-	133,960
Deferred compensation investments:				-
Corporate bond fund	5,516	-	-	5,516
Other	32,945	-	-	32,945
Other	<u>127,266</u>	<u>5,728</u>	<u>-</u>	<u>132,994</u>
Total mutual funds	<u>299,687</u>	<u>5,728</u>	<u>-</u>	<u>305,415</u>
Fixed-income securities—corporate bonds and US government securities	<u>-</u>	<u>161,333</u>	<u>-</u>	<u>161,333</u>
Total fixed-income securities	<u>-</u>	<u>161,333</u>	<u>-</u>	<u>161,333</u>
Domestic equity securities	<u>2,874</u>	<u>-</u>	<u>-</u>	<u>2,874</u>
Beneficial interests in perpetual trusts	<u>-</u>	<u>-</u>	<u>34,162</u>	<u>34,162</u>
Total assets at fair value	<u>\$ 469,018</u>	<u>\$ 167,061</u>	<u>\$ 34,162</u>	<u>670,241</u>
Alternative investments (at cost)				<u>36,467</u>
Investments measured at NAV:				
Commingled domestic equity funds				67,577
Commingled international equity funds				37,240
Commingled emerging markets funds				16,579
Commingled commodity funds				24,528
Commingled—other funds				83,800
Hedge fund of funds				<u>70,188</u>
Total investments measured at NAV				<u>299,912</u>
Total assets				<u>\$1,006,620</u>
Liabilities—interest rate swap agreements	<u>\$ -</u>	<u>\$ 5,707</u>	<u>\$ -</u>	<u>\$ 5,707</u>

The amounts classified in the tables above exclude assets invested in Baystate Health's defined benefit plan and limited partnership interests that Baystate Health has recorded at cost.

A summary of changes in the fair value of the Level 3 assets for the years ended September 30, 2016 and 2015, is as follows (in thousands):

	2016	2015
Balance at beginning of year	\$ 34,162	\$ 37,388
Unrealized gains (losses) relating to investments still held at the reporting date	<u>1,407</u>	<u>(3,226)</u>
Balance at end of year	<u>\$ 35,569</u>	<u>\$ 34,162</u>

A summary of investments (by major class) that use NAV or a NAV equivalent as a practical expedient to estimate fair value, that have restrictions on Baystate Health's ability to redeem its investment at the measurement date as of September 30, 2016 and 2015, is as follows (in thousands):

Description of Investment	September 30, 2016		
	Fair Value	Redemption Frequency	Redemption Notice Period
Commingled domestic equity funds	\$ 19,360	Monthly	5 days
Commingled international equity funds	39,786	Monthly	5–30 days
Commingled emerging markets funds	53,239	Daily/ Monthly	1–30 days
Commingled master limited partnership	37,216	Monthly	30 days
Commingled commodity funds	10,474	Monthly	5 days
Commingled hedge fund	26,402	Weekly	5 days
Commingled—other funds	68,281	Monthly	1–30 days
Hedge fund of funds	58,062	Quarterly	65–95 days
Hedge fund of funds	<u>9,241</u>	Every 2–3 years	95 days
Total	<u>\$ 322,061</u>		

Description of Investment	September 30, 2015		
	Fair Value	Redemption Frequency	Redemption Notice Period
Commingled equity mutual funds	\$ 104,817	Monthly	5 days
Commingled emerging markets funds	16,579	Monthly	15 days
Commingled commodity funds	24,528	Monthly	30 days
Commingled other funds	83,800	Monthly	30 days
Hedge fund of funds	67,581	Annually	65–95 days
Hedge fund of funds	<u>2,607</u>	Every three years	65–95 days
Total	<u>\$ 299,912</u>		

Valuation Techniques—Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis. There have been no changes in the methodologies used at September 30, 2016 and 2015.

The fair value of investments is determined in accordance with the current fair value guidance and as described below.

Cash Equivalents—The carrying value of cash equivalents approximates fair value as maturities are less than three months and/or include money market funds that are based on quoted prices and are actively traded.

Mutual Funds—The fair values of mutual funds are based on quoted market prices or net assets value. These funds are required to publish their NAV and to transact at that price. The mutual funds held by Baystate Health are deemed to be actively traded.

Commingled Funds—The fair value of common collective trusts is based on the NAV of the fund, representing the fair value of the underlying investments, which is generally securities traded on an active market. The NAV is used as a practical expedient to estimate fair value.

Limited Partnerships—The estimated fair values of limited partnerships, for which no quoted market prices are readily available, are determined based upon the information provided by the fund managers. Such information is generally based on NAV of the fund, which is used as a practical expedient to estimate fair value. Certain funds are subject to a minimum holding period or lockup, cannot be redeemed at the measurement date or within 90 days thereof, are subject to redemption notice periods in excess of 90 days, or have the ability to limit the aggregate amount of shareholder redemptions. The limited partnerships allocate gains, losses, and expenses to the partners based on the ownership percentage as described in the respective partnership or hedge fund agreements.

Fixed-Income Securities—Certain bonds are valued at the closing price reported in the active market in which the bond is traded. Other bonds are valued based on yields currently available on comparable securities of issuers with similar credit ratings. When quoted prices are not available for identical or similar bonds, the bond is valued under a discounted cash flows approach that maximizes observable inputs, such as current yields of similar instruments, but includes adjustments for certain risks that may not be observable, such as credit and liquidity risks.

Domestic Equity Securities—The fair value of domestic equity securities are principally based on quoted market prices that are traded in an active market.

Beneficial Interest in Perpetual Trusts—The estimated fair values of Baystate Health's beneficial interests in perpetual trusts are determined based upon information provided by the trustees. Such information is generally based on the pro rata interest in the net assets of the underlying investments. The assets held in trust consist primarily of cash equivalents and marketable securities. The fair values of the perpetual trusts are measured using the fair value of the assets contributed to the trusts. The measurement for a beneficial interest in a perpetual trust is categorized as a Level 3 fair value measurement because Baystate Health will never receive the trusts' assets.

Interest Rate Swaps—Baystate Health uses inputs other than quoted prices that are observable to value the interest rate swaps. Baystate Health considers these inputs to be Level 2 inputs in the context of the fair value hierarchy. The fair values represent the estimated amounts Baystate Health would receive or pay to terminate agreements, taking into consideration current interest rates and the current creditworthiness of the counterparty.

The following methods and assumptions were used by Baystate Health in estimating the fair value of its financial instruments that are not measured at fair value on a recurring basis for disclosures in the consolidated financial statements:

Receivables and Payables—The carrying value of Baystate Health’s receivables and payables approximates fair value, as maturities are short term.

Long-Term Debt—The estimated fair value of Baystate Health’s bonds is based on current traded value or a discounted cash flows analysis based on Baystate Health’s current incremental borrowing rates for similar types of borrowing arrangements. The fair value inputs for long-term debt are considered to be Level 2.

The fair value of long-term debt at September 30, 2016 and 2015, approximates \$601,366,000 and \$566,422,000, respectively.

6. PLEDGES RECEIVABLE

Pledges receivable at September 30, 2016 and 2015, are as follows (in thousands):

	2016	2015
Receivable in less than one year	\$ 1,748	\$ 2,056
Receivable in one to five years	3,520	3,146
Receivable in more than five years	<u>143</u>	<u>14</u>
Total pledges receivable	5,411	5,216
Less allowance for uncollectible pledges	<u>(561)</u>	<u>(602)</u>
Net pledges receivable	<u>\$ 4,850</u>	<u>\$ 4,614</u>

The current portion of net pledges receivable are included in accounts receivable, other in the consolidated statements of financial position. The long-term portion of net pledges receivable is recorded in deferred expense and other long-term assets in the consolidated statements of financial position.

7. LAND, BUILDINGS, AND EQUIPMENT

Details of land, buildings, and equipment at September 30, 2016 and 2015, are as follows (in thousands):

	2016	2015
Land, land improvements, and leasehold improvements	\$ 55,481	\$ 54,089
Buildings	886,849	806,285
Fixed equipment	106,448	105,801
Moveable equipment	673,128	616,403
Assets under capital leases	29,154	31,621
Construction in progress	<u>8,767</u>	<u>70,479</u>
	1,759,827	1,684,678
Less accumulated depreciation and amortization	<u>(1,045,195)</u>	<u>(973,058)</u>
Total land, buildings, and equipment—net	<u>\$ 714,632</u>	<u>\$ 711,620</u>

Depreciation expense for the years ended September 30, 2016 and 2015, was \$75,344,000 and \$69,115,000, respectively. As of September 30, 2016 and 2015, the accumulated amortization on equipment under capital lease is approximately \$20,950,000 and \$17,969,000, respectively.

8. SHORT-TERM OBLIGATIONS AND COMMITMENTS

Baystate Health has a 50% ownership in Baycare Health Partners, Inc., a physician hospital organization. BMC has provided an unconditional guarantee for a \$6,000,000 line of credit from a financial institution. There were no amounts outstanding under the line of credit at September 30, 2016. This line of credit expires on July 31, 2017.

At September 30, 2016 and 2015, a financial institution has issued irrevocable letters of credit on behalf of BHIC totaling \$300,000 and \$1,300,000 as of September 30, 2016 and 2015, respectively. Investments with a fair value of approximately \$2,950,516 and \$2,856,000 were pledged as security for these letters of credit as of September 30, 2016 and 2015, respectively. The letters of credit are subject to annual renewal and there are no amounts outstanding under the letters of credit as of September 30, 2016 and 2015.

9. LEASES

Baystate Health and its subsidiaries lease certain real property and equipment under noncancelable leases expiring at various dates through 2023 with varying renewal options. Rentals generally include insurance and maintenance costs.

On September 22, 2016, BMC entered into a tax-exempt lease financing agreement with the Massachusetts Development Finance Agency (MDFFA) and a financial institution in the amount of \$14,063,000. Proceeds from the financing are held in an acquisition escrow fund to be used to fund certain equipment related to a cogenerational combined heat and power plant project. Interest on the borrowing is fixed at 1.593% with principal and interest payments due monthly until maturity on September 22, 2026. This lease is classified as a capital lease and is included in the table below.

On November 2, 2011, BMC entered into a tax-exempt lease financing agreement with the MDFA and a financial institution in the amount of \$20,000,000. Proceeds from the financing were used to fund certain equipment, some of which are related to the BMC Expansion Project. Interest on the borrowing is fixed at 2.19%, with principal and interest payments due monthly until maturity on November 2, 2018. This lease is classified as a capital lease and is included in the table below.

Future minimum lease payments at September 30, 2016, are as follows (in thousands):

Year Ending September 30	Capital Leases	Operating Leases
2017	\$ 5,407	\$ 13,461
2018	5,374	11,827
2019	2,585	10,517
2020	1,563	7,938
2021	1,548	6,264
Thereafter	<u>7,655</u>	<u>28,196</u>
Total minimum lease payments	24,132	<u>\$ 78,203</u>
Less amount representing interest	<u>(1,396)</u>	
Present value of net minimum lease payments	22,736	
Less current portion	<u>(5,063)</u>	
Long-term portion	<u>\$ 17,673</u>	

Rental expense of operating leases amounted to approximately \$16,011,000 and \$17,788,000 for the years ended September 30, 2016 and 2015, respectively.

10. LONG-TERM DEBT

BMC and BFMC have loan agreements with the MDFA (effective October 1, 2010, Massachusetts Health and Educational Facilities Authority (MHEFA) merged into MDFA) and with the MHEFA for

construction projects and equipment. Long-term obligations outstanding at September 30, 2016 and 2015, consist of the following (in thousands):

	<u>Amount Outstanding</u>	
	<u>2016</u>	<u>2015</u>
M DFA and M HEFA issues:		
BMC Series O	\$ 19,719	\$ -
BMC Series N	55,115	55,115
BFMC Series A	21,868	22,000
BMC Series M	35,602	36,832
BMC Series L	22,359	22,955
BMC Series I	63,380	63,380
BMC Series J-1	45,000	45,000
BMC Series J-2	45,000	45,000
BMC Series K-1	20,045	20,045
BMC Series K-2	26,365	26,365
BMC Series M-2	5,863	6,519
BMC Series H	3,556	4,222
BFMC Series M-4A	5,010	5,487
BMC Series G	39,965	43,345
BTHC NMTC debt	<u>81,789</u>	<u>107,791</u>
Subtotal	490,636	504,056
BH note payable - line of credit	37,241	-
BH note payable - Wing	17,020	17,760
BWH note payable	13,074	13,429
BNH commercial mortgages	-	4,545
BNH financing arrangements	1,125	2,890
Original issue premium	<u>3,567</u>	<u>4,135</u>
Total long-term debt	562,663	546,815
Less current portion	<u>(13,016)</u>	<u>(30,960)</u>
Long-term debt, excluding current portion	<u>\$ 549,647</u>	<u>\$ 515,855</u>

Summary information for each issue is as follows:

On May 12, 2016, BMC issued Series O MDFA Revenue Bonds in the aggregate principal amount of \$20,000,000. Proceeds from the bonds were used to redeem 100% of the BTHC A loan from the Banc of America CDE, included in the BTHC NMTC debt above. The bonds are subject to a mandatory tender on May 12, 2026. Interest on the bonds is fixed at 1.98% through May 12, 2026, with final maturity on May 12, 2036.

Pursuant to the redemption of the A loan, the B loan from the Banc of America-controlled CDE of \$6,084,000 included in the BTHC NMTC debt above was forgiven. The loan forgiveness is reported in the statement of operations within other changes in unrestricted net assets as a capital contribution.

On October 6, 2014, BMC issued Series N MDFA Revenue Bonds in the aggregate principal amount of \$55,115,000. The proceeds from the bonds are financing the build-out of inpatient rooms, operating rooms, inpatient pharmacy, medical equipment, information technology equipment, and other capital projects. The bonds are 30-year bonds with final maturity on July 1, 2044, and carry a fixed 5% interest rate. In connection with the construction project, BMC has entered into a construction contract in the amount of approximately \$39,773,000.

On December 4, 2014, BFMC issued Series A MDFA Revenue Bonds in the aggregate principal amount of \$22,000,000. The proceeds from the bonds are financing the construction of a new surgical unit at BFMC. The bonds are 30-year bonds with final maturity on December 4, 2044, and carry a fixed 2.9% interest rate. BMC has entered into a guaranty agreement on behalf of BFMC in connection with this bond.

Series M Bonds—On August 9, 2012, BMC issued Series M MDFA Revenue Bonds in the aggregate principal amount of \$40,137,000. BMC used the proceeds from the bonds to redeem 100% of Series F MHEFA Revenue Bonds, exercising an early redemption option related to the Series F obligation. The bonds are subject to mandatory tender on August 8, 2022. Interest on the bonds is fixed at 2.37% through August 8, 2022, with final maturity on July 1, 2033. An annual average balance of \$15,000,000 must be maintained on deposit with the financial institution or the interest rate on such bonds may be adjusted upward, not to exceed 2.97%.

The Series F bonds were issued on June 1, 2002, to reimburse and fund certain capital renovation and equipment expenditures and fund the construction of a new cancer center known as the D'Amour Center for Cancer Care.

Series L Bonds—On November 2, 2011, BMC issued Series L MDFA Revenue Bonds in the aggregate principal amount of \$25,000,000. Proceeds from the bonds were used to fund the construction of a new emergency department in conjunction with the BMC Expansion Project. Interest on the bonds is initially fixed at 2.95% through November 1, 2021, with final maturity on July 1, 2041.

BMC Hospital Expansion MHEFA Bond Issuances—On June 25, 2009, BMC issued Series I, Series J-1, Series J-2, Series K-1, and Series K-2 MHEFA Revenue Bonds in a combined aggregate principal amount of \$199,790,000. Proceeds from the bonds were used to pay off the Banc of America, NA loan of \$65,000,000 (borrowed in October 2008) and fund the construction, improvement, equipping, and other related capital expenditures of a seven-story building located at 759 Chestnut Street in Springfield, Massachusetts (“BMC Expansion Project”). Details of the related MHEFA bond issuances are as follows:

Series I Bonds—BMC issued Series I MHEFA Revenue Bonds in the aggregate amount of \$63,380,000. Interest rates range from 5.5% to 5.75%. Final maturity on the bonds is July 1, 2036.

Series J-1 Bonds—BMC issued Series J-1 MHEFA Revenue Bonds in the aggregate amount of \$45,000,000. Interest on the bonds is variable and is 0.83% and 0.01% at September 30, 2016 and 2015, respectively. Final maturity on the bonds is July 1, 2044. The bonds are secured by an irrevocable letter of credit issued by a financial institution that terminates in January 2020.

Series J-2 Bonds—BMC issued Series J-2 MHEFA Revenue Bonds in the aggregate amount of \$45,000,000. Interest on the bonds is variable and was 0.85% and 0.01% at September 30, 2016 and 2015, respectively. Final maturity on the bonds is July 1, 2044. The bonds are secured by an irrevocable letter of credit issued by a financial institution that terminates in January 2020.

Series K-1 Bonds—BMC issued Series K-1 MHEFA Revenue Bonds in the aggregate amount of \$20,045,000. The bonds were subject to mandatory tender on July 1, 2013. The initial interest on the bonds was fixed at 5% through June 30, 2013, with final maturity on July 1, 2039.

On July 1, 2013, the Series K-1 MHEFA Revenue Bonds were purchased pursuant to a mandatory tender and remarketed on such date. The reoffering of the bonds contained a conversion of the interest rate from the long-term fixed rate to a daily rate of 0.78% at September 30, 2016, along with a provision of a letter of credit from a financial institution. The daily rate at September 30, 2015, was 0.01%. The daily interest rate is determined by the remarketing agent and the letter of credit will expire on October 21, 2020.

Series K-2 Bonds—BMC issued Series K-2 MHEFA Revenue Bonds in the aggregate amount of \$26,365,000. The bonds were subject to mandatory tender on July 1, 2015. The initial interest on the bonds was fixed at 5% through June 30, 2015, with final maturity on July 1, 2039.

On July 1, 2015, the Series K-2 MHEFA Revenue Bonds were purchased pursuant to the mandatory tender and remarketed on such date. The reoffering of the bonds contained a conversion of the interest rate from the long-term fixed rate to a weekly rate of 0.83% and 0.01% at September 30, 2016 and 2015, respectively, along with a provision of a letter of credit from a financial institution. The weekly rate is determined by the remarketing agent and the letter of credit will expire on July 1, 2020.

Series M-2—On June 30, 2008, BMC entered into a loan commitment under a capital asset program financed by MHEFA through the issuance of variable-rate demand Revenue Bonds, Series M-2. Proceeds of \$10,158,000 were used to refund the then-outstanding Revenue Bonds, BMC Issue, Series J-2, which were issued in 1995 (“Series J-2-1995”). The Series J-2-1995 bonds were issued to reimburse and fund certain capital renovation and equipment expenditures and fund the purchase of an office building. Interest on the Series M-2 bonds is variable and resets weekly to reflect current market rates and was 0.91% and 0.03% at September 30, 2016 and 2015, respectively. Final maturity of the bonds is June 15, 2023. These bonds are supported by a pooled letter of credit, which expires on October 31, 2017.

Series H Bonds—On January 18, 2007, BMC issued Series H MHEFA Revenue Bonds in the aggregate principal amount of \$10,000,000. Proceeds from the bonds were used to reimburse and fund certain capital additions and fund the construction of a new parking garage. Interest on the bonds is variable based on monthly resets and was 0.38% and 0.90% at September 30, 2016 and 2015, respectively. Final maturity of the bonds is January 1, 2022.

Series M-4A Bonds—On February 1, 2005, BFMC entered into a loan commitment under a capital asset program financed by MHEFA through the issuance of variable-rate demand Revenue Bonds, Series M-4A. Proceeds of \$9,100,000 were used to fund certain capital additions, renovations, and equipment expenditures related to the emergency department, radiology department, and in-patient facilities. Interest on the bonds is variable and resets weekly to reflect current market rates and was 0.91% and 0.03% at September 30, 2016 and 2015, respectively. Final maturity of the bonds is June 15, 2024. These bonds are supported by a pooled letter of credit, which expires on October 31, 2017.

Series G Bonds—On October 27, 2005, BMC issued Series G MHEFA Revenue Bonds in the aggregate principal amount of \$71,740,000. Proceeds from the bonds were used to advance refund a portion of the outstanding Revenue Bonds, BMC Issue, Series E. The Series E bonds were issued to finance or refinance the following: (a) construction of a new 104,500 gross square foot ambulatory care center; (b) construction of a new 100,000 gross square foot building to house the ambulatory surgery center, medical library, and education space; (c) renovation of various existing spaces within BMC; and (d) acquisition of equipment for the new facilities. Series G bonds' proceeds were also used to finance routine capital construction, renovations, and equipping of various facilities of BMC. Interest on the bonds is variable and resets every 35 days and was 0.78% and 0.01% at September 30, 2016 and 2015, respectively. Final maturity of the bonds is July 1, 2026. The bonds are secured by an irrevocable letter of credit issued by a financial institution that terminates November 13, 2017.

Significant Debt Covenants—The bond agreements include various financial covenants, the most restrictive of which are a pledge of revenues and the maintenance of a ratio of net revenue available to meet debt service to total principal and interest requirements of at least 1.1 (as defined by the agreement). Baystate Health was in compliance with those bond covenants during the fiscal years ended September 30, 2016 and 2015.

A debt service fund has been established in accordance with these debt agreements. Debt services fund balances amounted to approximately \$1,209,000 and \$3,627,000 at September 30, 2016 and 2015, respectively.

During 2015, a construction fund was established in accordance with these debt agreements. Construction fund balances amounted to approximately \$14,063,000 and \$30,763,000 at September 30, 2016 and 2015, respectively.

NMTC Debt—In December and May 2009, BMC entered into financing arrangements with US Bancorp Community Development Corporation (“US Bancorp”), Banc of America Community Development Corporation (“Banc of America”), and MHIC New Markets Fund II, LLC (MHIC) to fund a portion of the costs of the construction of a new hospital facility (“BMC Expansion Project”) in Springfield, Massachusetts, using the NMTC Program. The NMTC Program is a program of the Community Development Financial Institutions Fund, a bureau of the US Treasury. The NMTC Program permits taxpayers to receive a credit against federal income taxes for making qualified equity investments in designated community development entities (CDEs).

In connection with the December and May 2009 financing arrangements, BMC loaned \$23,580,283 and \$32,617,500, respectively, to USBCDE Investment Fund XXXIII, LLC (the “Investment Fund”), a wholly owned subsidiary of US Bancorp. The notes bear interest at 2.139% annually, with annual cash payments during the first seven years of each 33-year term based on an interest rate of 1.00%. Also in connection with the December 2009 financing arrangement, BMC loaned \$7,606,500 to MHIC. The notes bear interest at 1% annually, with no cash payments during the first seven years of the 33-year term. The notes are recorded as notes receivable in the consolidated statements of financial position as of September 30, 2016 and 2015.

Under the December 2009 financing arrangement, BTHC has borrowed \$37,692,500 from four CDEs established for the purpose of providing funds under the NMTC Program. US Bancorp through the Investment Fund controls two of the CDEs and MHIC controls the other two. As of September 30, 2016 and 2015, BTHC has outstanding loans of \$27,490,000 and \$10,202,500 due to US Bancorp CDEs and MHIC CDEs, respectively, related to the December 2009 financing. The loans were issued in four tranches from each of the controlling entities. US Bancorp loans were issued in tranches A, B, C, and D. The US Bancorp CDEs A loan totaled \$19,886,783, the B loan \$2,653,217, the C loan \$3,693,500, and

the D loan \$1,256,500. Each of the loans has a 33-year term and bear interest at rates ranging from 0.8911% to 1.8315% annually. MHIC loans were issued in tranches A, B, Series 2, and Series 4. The MHIC CDEs A loan totaled \$7,606,500, the B loan \$1,366,000, the Series 2 loan \$1,000,000, and the Series 4 loan \$230,000. Each of the loans has a 33-year term and bear interest at rates ranging from 1.00% to 1.935%.

Under the May 2009 financing arrangement, BTHC has borrowed approximately \$69,424,000 from CDEs established for the purpose of providing funds under the NMTC Program. US Bancorp, through the Investment Fund, controls four of the CDEs and Banc of America (BOA) controls the other CDE. As of September 30, 2016 and 2015, BTHC has outstanding loans of approximately \$43,340,000 due to US Bancorp CDEs. As of September 30, 2016 no amounts were outstanding related to the BOA CDE and \$26,084,000 was outstanding at September 30, 2015. The loans were issued in two tranches, an A tranche and a B tranche. The A loans from the US Bancorp CDEs totaled \$32,617,500, have a 33-year term, and bear interest at rates ranging from 0.816% to 1.00% annually. The B loans from the US Bancorp CDEs totaled \$10,722,500, have a 33-year term, and bear interest at rates ranging from 0.5% to 1.2832% annually. The A loan from the BOA CDE of \$20,000,000 has a seven-year term and bears interest at 5.992% annually. This amount was reported in the current portion of long-term debt at September 30, 2015, and was paid in full in May 2016. The B loan from the BOA-controlled CDE of \$6,084,000 has a seven-year term, bears interest at 2% annually and provides that if there has been no default, the principal balance will be forgiven at the end of the seven-year term. This B loan was forgiven in 2016 and resulted in a contribution of a capital asset of \$6,084,000 in the consolidated statements of operations and changes in net assets for the year ended September 30, 2016.

Certain buildings and equipment have been pledged as collateral for the borrowings.

BMC recorded interest income of approximately \$1,402,000 and \$1,382,000 in 2016 and 2015, respectively, related to the financing arrangement agreements. No interest was capitalized at BTHC in 2016 and 2015 relating to the financing arrangement agreements.

In 2016, US Bancorp may put its interest in the Investment Fund to BMC for a put price of \$1,000. If US Bancorp does not exercise its put rights, BMC may call its interest in the Investment Fund for a call price equal to the fair value of US Bancorp's interest in the Investment Fund.

In December 2016, BMC executed the put option agreements and paid to US Bancorp and MHIC \$1,000 each for the purchase of each member's interest in the USBCDE Investments Fund XXXIII, LLC and MHIC Investment Fund, LLC, respectively. BMC is now the sole owner of both investment funds and will forgive the notes receivable and payable of the investment funds. All of the net assets of BTHC will then be transferred to BMC. The entire transaction will result in a net increase in unrestricted net assets of approximately \$11,800,000 in 2017.

BH Notes Payable—On December 28, 2015, Baystate Health entered into a three-year \$40,000,000 line of credit with a financial institution, maturing on December 28, 2018. The interest rate on the borrowing is variable at London InterBank Offered Rate (LIBOR), plus 0.70% per annum. An initial borrowing of \$20,000,000 was made as described in Note 14. The interest rate on this loan was 1.55% on September 30, 2016.

On August 29, 2014, BH entered into a variable rate, 10-year term loan through a financial institution in the amount of \$18,500,000. The interest rate on this term loan is equivalent to LIBOR, plus 0.475%. The interest rate on this loan was 1% on September 30, 2016. Proceeds from the term loan were used in the financing of BH's September 1, 2014, purchase of BWH. Cash and short-term investments have been pledged as collateral for this borrowing.

BWH Note Payable—On September 30, 2014, BWH entered into a 10-year loan through a financial institution in the amount of \$13,745,000 at a fixed rate of 3.542%. Proceeds from the loan were used to repay debt held by BWH in the same amount at a rate of 5.15%. As of September 30, 2016 or 2015, BWH was not in compliance with its debt service coverage ratio requirement. BWH obtained a waiver directly from the financial institution.

BNH Long-Term Debt—BNH consolidated has various current and long-term debt outstanding totaling approximately \$1,125,000 as of September 30, 2016, of which approximately \$225,000 is classified as current. The agreement with the longest duration extends through 2024. BNH consolidated has a combination of fixed-rate debt, with interest rates ranging from 0% to 5.05% as of September 30, 2016 and 2015.

The combined aggregate future principal payments of all long-term debt are as follows (in thousands):

Year Ending September 30	
2017	\$ 13,016
2018	13,046
2019	50,552
2020	13,944
2021	14,290
Thereafter	<u>454,248</u>
	<u>\$ 559,096</u>

BMC has entered into a guaranty agreement on behalf of BFMC and BWH in connection with outstanding MHEFA bonds and BWH note payable, respectively.

Interest Rate Swap Agreements—BMC periodically enters into interest rate swap agreements to moderate its exposure to interest rate changes and to lower the overall cost of borrowings. Gains and losses realized on termination of contracts are deferred and amortized over the remaining life of the associated contract.

In 2004, BMC entered into an interest rate swap agreement with a financial institution with an original notional amount of \$67,470,000. The notional amount outstanding at September 30, 2016 and 2015, was \$12,160,000 and \$18,245,000, respectively. Under the terms of the agreement, BMC pays a fixed rate of 3.26% and receives variable payments based upon the Securities Industry and Financial Markets Association rate. The agreement, in effect, converts \$29,394,000 of notional variable-rate debt to fixed-rate debt.

In September 2005, BMC, in anticipation of the issuance of the Series G bonds, entered into an interest rate swap agreement with a financial institution with an original notional amount of \$71,740,000. The notional amount outstanding at September 30, 2016 and 2015, was \$39,965,000 and \$43,345,000, respectively. The agreement provides for the financial institution to pay variable-rate payments to BMC equal to 56.9% of one-month LIBOR, plus 0.32%, and for BMC to pay the financial institution a fixed rate of 3.021%. The LIBOR was 0.53% and 0.2% at September 30, 2016 and 2015, respectively. The agreement, in effect, converts \$46,630,000 of variable-rate debt to a fixed rate of interest. There are termination provisions to this contract for each party.

The fair value of these agreements resulted in swap liabilities of approximately \$5,156,000 and \$5,707,000 at September 30, 2016 and 2015, respectively, and is included in other long-term liabilities in the consolidated statements of financial position.

The net interest cost and the change in the fair value of the associated interest rate swaps are included in nonoperating income in the consolidated statements of operations.

11. INTEREST EXPENSE

Baystate Health and its subsidiaries capitalize interest cost as part of the historical cost of acquiring certain significant qualifying assets. During the years ended September 30, 2016 and 2015, interest cost was as follows (in thousands):

	2016	2015
Total interest cost	\$ 13,765	\$ 13,938
Net interest cost capitalized	<u>(2,378)</u>	<u>(3,046)</u>
Net interest cost expensed	<u>\$ 11,387</u>	<u>\$ 10,892</u>

12. INSURANCE LIABILITY LOSS RESERVES

Baystate Health, with the exception of HNE, addresses its professional and general liability expense, in part, by depositing funds with BHIC, which utilizes these funds to pay claims and, in part, to purchase commercial excess liability insurance. The commercial insurance generally provides coverage on a “claims-made” basis. Under the claims-made policies, claims based on occurrences during their term, but reported subsequently, will be uninsured should the policy not be renewed or replaced with other coverage. Management has the intention of renewing its insurance policies in the future and believes it will have the ability to obtain such policy renewals. Baystate Health and certain of its subsidiaries have also purchased excess professional and general coverage from other insurers. In addition, BHIC insures the workers’ compensation, employer’s liability, excess workers’ compensation, and long-term disability of certain of Baystate Health’s subsidiaries.

BHIC reinsures a portion of its risks in order to limit its exposure to losses. Reinsurance contracts do not relieve Baystate Health from its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to Baystate Health. Consequently, Baystate Health evaluates the financial condition of its reinsurers to minimize its exposure to significant losses from reinsurer insolvencies.

Reinsurance recoverables were based on actuarial reports prepared by independent consulting actuaries. At September 30, 2016 and 2015, reinsurance recoverables of \$17,500,000 and \$10,250,000, respectively, were recorded as deferred expense and other long-term assets in the consolidated statements of financial position. There were no specifically identified claims subject to reinsurance recoverables at September 30, 2016 and 2015, or deducted from losses incurred and paid during the years then ended.

Reserves have been provided with the assistance of a consulting actuary for asserted claims and for unasserted claims probable of assertion arising from both reported and unreported incidents, which are based on historical experience and existing reported incidents.

Activity in the BHIC liability for losses and loss adjustment expenses for the years ended September 30, 2016 and 2015, is summarized as follows (in thousands):

	2016	2015
Balance at beginning of year	<u>\$ 15,400</u>	<u>\$ 15,543</u>
Incurred (recovered) related to:		
Current year	3,373	3,400
Prior years	<u>(257)</u>	<u>(2,352)</u>
Total incurred	<u>3,116</u>	<u>1,048</u>
Paid related to:		
Current year	(20)	(25)
Prior years	<u>(2,944)</u>	<u>(1,166)</u>
Total paid	<u>(2,964)</u>	<u>(1,191)</u>
Balance at end of year	<u><u>\$ 15,552</u></u>	<u><u>\$ 15,400</u></u>

13. MEDICAL CLAIMS AND CAPITATION EXPENSE

Medical claims and capitation expense for the years ended September 30, 2016 and 2015, include the following components (in thousands):

	2016	2015
Physician and other outpatient specialty services	\$ 320,569	\$ 294,157
Inpatient care and same-day surgery	116,780	110,944
Pharmacy	173,140	155,903
Primary care capitation	6,322	6,269
Other medical services	25,038	25,785
Coordination of benefits	(515)	(614)
Net reinsurance losses	<u>1,063</u>	<u>444</u>
	642,397	592,888
Provider risk-sharing—net	<u>(16,934)</u>	<u>(23,192)</u>
Total medical claims and capitation expense	<u><u>\$ 625,463</u></u>	<u><u>\$ 569,696</u></u>

Activity in medical claims payable for 2016 and 2015 is as follows (in thousands):

	2016	2015
Medical claims payable:		
Claims payable—beginning of year	\$ 47,350	\$ 13,286
Risk-sharing payable—beginning of year	<u>26,992</u>	<u>35,287</u>
	<u>74,342</u>	<u>48,573</u>
Claims incurred:		
Current year	652,793	607,249
Prior years	<u>(7,026)</u>	<u>(2,489)</u>
	<u>645,767</u>	<u>604,760</u>
Claims paid:		
Current year	(601,463)	(535,545)
Prior years	<u>(76,611)</u>	<u>(43,446)</u>
	<u>(678,074)</u>	<u>(578,991)</u>
Risk-sharing payable—end of year	24,522	26,992
Medical claims payable—end of year	<u>35,356</u>	<u>47,350</u>
Total medical claims payable	<u>\$ 59,878</u>	<u>\$ 74,342</u>

Amounts incurred related to prior years vary from previously estimated liabilities as the claims are ultimately settled. HNE’s accounting for the provisions included in the Affordable Care Act (ACA) regarding reinsurance, risk adjustment, and risk corridor (the “3Rs”) is as follows:

Transitional Reinsurance Program—The ACA established a temporary three-year transitional reinsurance program, under which all issuers of major medical commercial insurance products and self-insured plan sponsors are required to contribute funding in amounts set by HHS. Funds collected will be utilized to reimburse issuers’ high claims costs incurred for qualified individual members. HNE is entitled to certain reimbursements from this program. HNE recorded a receivable and offset health care costs to reflect our estimate of these recoveries. At September 30, 2016 and 2015, HNE recorded a receivable under the temporary three-year reinsurance program of approximately \$103,139 and \$877,000, respectively.

Risk Adjustment—The ACA established a permanent risk adjustment program to transfer funds from qualified individual and small group insurance plans with below-average risk scores to plans with above-average risk scores. Based on the risk score of our qualified plan members relative to the average risk score of members of other qualified plans throughout the Commonwealth, HNE estimates the ultimate 2014 risk adjustment receivables or payables and reflects the impact as an adjustment to premium revenue. At September 30, 2016 and 2015, HNE recorded a net payable of approximately \$3,033,000 and \$4,320,000, respectively, under the risk adjustment program.

Risk Corridor—The ACA established a temporary three-year risk-sharing program for qualified individual and small group insurance plans. Under this program, HNE makes or receives a payment to (or from) HHS based on the ratio of allowable costs to target costs (as defined by the ACA). HNE records a risk corridor receivable or payable as an adjustment to premium revenue based on our estimate of the ultimate 2015 risk-sharing amount. At September 30, 2016 and 2015, no receivables or payables were recorded under the risk corridor program.

14. STATUTORY SURPLUS/CAPITAL

Minimum Surplus Requirements under Commonwealth of Massachusetts Law—In accordance with insurance laws and regulations established by the Commonwealth of Massachusetts, HNE is required to maintain a minimum surplus of \$53,111,215, the largest of the four following tests:

- a) \$1,000,000
- b) The total of 2% of the first \$150,000,000 of premium and 1% of the premium in excess of \$150,000,000
- c) Three months of uncovered health care expenditures
- d) 4% of annual hospital expenditures, plus 8% of all other medical expenditures, excluding capitated arrangements

Based on calendar 2015 activity, the minimum capital amount as determined by each of the above tests is as follows: a) \$1,000,000; b) \$10,484,785; c) \$5,850,292; and d) \$53,111,215. At December 31, 2015, the Company's surplus was below the Commonwealth of Massachusetts' laws and regulations regarding minimum surplus. HNE will submit a comprehensive financial plan to the insurance commissioner and the commissioner may issue corrective orders.

National Association of Insurance Commissioners' (NAICs) Model Regulation—The Managed Care Organization Risk-Based Capital (RBC) Model Regulation ("Model Regulation") was adopted by the NAIC in December 1997 to establish benchmarks for minimum levels of statutory RBC. The Model Regulation prescribes specific actions that insurance departments should take (i.e., action levels) when certain RBC thresholds are not met. Calculation of RBC in accordance with the Model Regulation RBC formula is required in connection with the annual statutory filing. HNE's statutory capital at December 31, 2015, was at the Regulatory Action Level. HNE has submitted a comprehensive financial plan to the insurance commissioner and the commissioner may issue corrective orders.

Surplus Notes—On December 28, 2015, HNE entered into a surplus notes agreement, borrowing \$20,000,000 from Baystate Health. HNE entered into the surplus notes to maintain minimum levels of surplus and RBC as of December 31, 2015. The surplus notes accrue interest payable to Baystate Health at a rate per annum equal to the three-year US Treasury rate until the principal is paid in full.

15. INCOME TAXES

As of September 30, 2016, operating loss carryforwards for federal income tax purposes were approximately \$25,376,000 for BMC, which expire in various years ranging from 2017 to 2033. This results in a deferred tax asset; however, because utilization of these net operating losses is not reasonably assured, BMC has recorded a full valuation allowance offsetting this deferred tax asset.

16. FUNDS HELD IN TRUST BY OTHERS

Baystate Health and its subsidiaries are beneficiaries of certain perpetual trusts (the "Trusts"), from which they receive unrestricted income. Appreciation or depreciation in the value of the Trusts is recorded as an increase or decrease to permanently restricted net assets. During fiscal years 2016 and 2015, distributions from the Trusts were approximately \$1,470,000 and \$1,661,000, respectively, and are included in operating revenue.

17. BENEFIT PLANS

Baystate Health and certain of its consolidated subsidiaries and other ownership interests participate in a noncontributory, defined benefit cash balance retirement plan (the “plan”) covering substantially all of their eligible employees.

Baystate Health’s policy is to fund amounts as are necessary on an actuarial basis to provide for benefits in accordance with the Employee Retirement Income Security Act of 1974, using the accrued benefit (net credit) actuarial cost method.

Plan Freeze—On September 9, 2015, the Board of Trustees voted to approve an amendment to freeze the plan. Effective December 31, 2015, participants in the plan will cease to accrue benefits. On January 1, 2016, the plan participants from the plan became participants in the redesigned Baystate Health defined contribution plan (the “DC plan”). In connection with the plan freeze, the period for amortizing actuarial gains and losses was changed from the average expected future service of active participants to the average expected future lifetime as a plan participant for all participants. As shown in the tables below, the plan freeze was accounted for as a curtailment and resulted in a one-time credit to net periodic pension cost of approximately \$71,931,000 (\$71,400,000 exclusive of other ownership interest). This curtailment credit is recorded in other income, net in the consolidated statement of operations for the year ended September 30, 2015. Additionally, in 2015 a curtailment gain of approximately \$47,898,000 reduced the pension obligation and is recorded as an increase to unrestricted net assets.

The following table presents the change in the plan's projected benefit obligation, change in plan assets, and funded status of the plan as of September 30, 2016 and 2015, (in thousands):

	2016	2015
Change in Pension Obligation		
Pension obligation—beginning of year	\$ 920,017	\$ 913,489
Service cost	7,004	28,756
Interest cost	40,172	40,054
Actuarial loss	107,455	37,385
Benefits paid	(64,428)	(51,769)
Curtailment	<u> </u>	<u>(47,898)</u>
Pension obligation—end of year	<u>\$ 1,010,220</u>	<u>\$ 920,017</u>
Change in Plan Assets		
Fair value of plan assets—beginning of year	\$ 805,609	\$ 813,718
Actual return on plan assets	103,723	(6,340)
Employer contributions	35,000	50,000
Benefits paid	<u>(64,428)</u>	<u>(51,769)</u>
Fair value of plan assets—end of year	<u>\$ 879,904</u>	<u>\$ 805,609</u>
Funded Status		
Funded status of the plan	<u>\$ (130,317)</u>	<u>\$ (114,408)</u>
Pension liability	<u>\$ (130,317)</u>	<u>\$ (114,408)</u>
Amounts Recognized in Unrestricted Net Assets Consist of		
Net actuarial loss	<u>\$ 407,418</u>	<u>\$ 348,683</u>
Accumulated pension adjustment	<u>\$ 407,418</u>	<u>\$ 348,683</u>

Exclusive of other ownership interest, the underfunded status of the plan at September 30, 2016, is approximately \$131,169,000, the change in the pension adjustment is \$58,400,000 and the total pension liability is \$405,452,000.

Exclusive of other ownership interest, the underfunded status of the plan at September 30, 2015, is approximately \$114,951,000, the change in the pension adjustment is \$115,780,000, and the total pension liability is \$347,052,000.

The net actuarial loss and prior service credit expected to be recognized in benefit cost in 2017 is approximately \$12,266,000 and \$0, respectively.

The assumptions used to develop the projected benefit obligation as of September 30, 2016 and 2015, are as follows:

	2016	2015
Discount rate	3.70 %	4.55 %
Rate of compensation increase	N/A	3.00

At September 30, 2016, and September 30, 2015, the mortality assumption was determined using the noncollar adjusted RP-2014 mortality tables.

The accumulated benefit obligation was approximately \$1,010,220,335 and \$917,918,000 at September 30, 2016 and 2015, respectively.

Net Periodic Pension Cost—Net pension cost for the defined benefit plan for the years ended September 30, 2016 and 2015, includes the following components (in thousands):

	2016	2015
Service cost	\$ 7,004	\$ 28,756
Interest cost	40,172	40,054
Expected return on plan assets	(64,106)	(61,054)
Amortization of prior service credit	-	(12,997)
Recognized net actuarial loss	9,104	25,375
Curtailment	<u>-</u>	<u>(71,931)</u>
Net pension cost	<u>\$ (7,826)</u>	<u>\$ (51,797)</u>

The assumptions used to determine net pension cost for the years ended September 30, 2015 and 2014, are as follows:

	2016	2015
Discount rate	4.55 %	4.50 %
Expected return on plan assets	7.75	7.75
Rate of compensation increase	3.00	3.00

Plan Assets—The plan's investment objectives are to achieve long-term growth in excess of inflation and to provide a rate of return that meets or exceeds the actuarial expected long-term rate of return on plan assets. In order to minimize risk, the plan attempts to minimize the variability in yearly returns. The plan diversifies its holdings among sectors, industries, and companies. The target allocations of assets at September 30, 2016, were equities 30%, fixed income 40%, and other 30%.

To develop the expected long-term rate of return on plan assets assumption, Baystate Health considered the historical return and the future expectations for returns for each asset class, as well as the target asset allocation of the pension investment portfolio.

Baystate Health's pension plan asset allocation, by asset category, as of September 30, 2016 and 2015, is as follows:

	2016	2015
Common and preferred equity securities	42 %	35 %
US government and domestic fixed-income securities	44	43
Other investments	<u>14</u>	<u>22</u>
	<u>100 %</u>	<u>100 %</u>

Financial assets invested in the plan, in one of the three categories described previously, as of September 30, 2016 and 2015, are classified as follows (in thousands). See Note 5 for definitions of Level 1, Level 2, and Level 3 of the fair value hierarchy.

	Assets at Fair Value as of September 30, 2016			
	Level 1	Level 2	Level 3	Total
Money market	<u>\$ 7,959</u>	<u>\$ 3,954</u>	<u>\$ -</u>	<u>\$ 11,913</u>
Mutual funds:				
Corporate bond fund	187,665	-	-	187,665
Other	<u>60,488</u>	<u>-</u>	<u>-</u>	<u>60,488</u>
Total mutual funds	<u>248,153</u>	<u>-</u>	<u>-</u>	<u>248,153</u>
Fixed-income securities—US government securities	<u>-</u>	<u>172,636</u>	<u>-</u>	<u>172,636</u>
Domestic equity securities	<u>78,736</u>		<u>-</u>	<u>78,736</u>
Total assets—at fair value	<u>\$ 334,848</u>	<u>\$ 176,590</u>	<u>\$ -</u>	<u>511,438</u>
Plan assets—at contract value				<u>15,122</u>
Investments measured at NAV:				
Commingled domestic equity funds				30,571
Commingled international equity funds				55,571
Commingled emerging markets funds				82,214
Commingled master limited partnerships				58,726
Commingled hedge funds				42,688
Hedge fund of funds				44,434
Private market funds				<u>39,140</u>
Total investments measured at NAV				<u>353,344</u>
Total plan assets				<u>\$ 879,904</u>

	Assets at Fair Value as of September 30, 2015			
	Level 1	Level 2	Level 3	Total
Money market	\$ 1,506	\$ 6,236	\$ -	\$ 7,742
Mutual funds:				
Corporate bond fund	177,554	-	-	177,554
Other	<u>86,294</u>	<u>-</u>	<u>-</u>	<u>86,294</u>
Total mutual funds	<u>263,848</u>	<u>-</u>	<u>-</u>	<u>263,848</u>
Fixed-income securities—US government securities	<u>-</u>	<u>144,705</u>	<u>-</u>	<u>144,705</u>
Total assets—at fair value	<u>\$ 265,354</u>	<u>\$ 150,941</u>	<u>\$ -</u>	<u>416,295</u>
Plan assets—at contract value				<u>14,706</u>
Investments measured at NAV:				
Commingled domestic equity funds				80,687
Commingled international equity funds				50,106
Commingled commodity funds				36,843
Commingled emerging markets funds				31,946
Hedge fund of funds				130,343
Private equity funds				<u>44,683</u>
Total investments measured at NAV				<u>374,608</u>
Total plan assets				<u>\$ 805,609</u>

A summary of investments (by major class) that use NAV or a NAV equivalent as a practical expedient to estimate fair value, that have restrictions on the plan's ability to redeem its investment at the measurement date as of September 30, 2016 and 2015, is as follows (in thousands):

Description of Investment	September 30, 2016		
	Fair Value	Redemption Frequency	Redemption Notice Period
Commingled equity mutual funds	\$ 30,571	Monthly	5 days
Commingled international equity funds	55,571	Monthly	5–30 days
Commingled emerging markets funds	82,214	Daily/Monthly	1–30 days
Commingled master limited partnerships	58,726	Monthly	30 days
Commingled hedge funds	42,688	Weekly	5 days
Hedge fund of funds	28,346	Quarterly	65–95 days
Hedge fund of funds	16,088	Every 2-3 years	95 days
Private market investments	<u>39,140</u>	*	*
Total	<u>\$ 353,344</u>		

Description of Investment	September 30, 2015		
	Fair Value	Redemption Frequency	Redemption Notice Period
Commingled equity mutual funds	\$ 130,793	Monthly	5 days
Commingled emerging markets funds	31,946	Monthly	15 days
Commingled commodity funds	36,843	Monthly	30 days
Hedge fund of funds	116,820	Annually	65–95 days
Hedge fund of funds	13,523	Every three years	65–95 days
Private market investments	<u>44,683</u>	*	*
Total	<u>\$ 374,608</u>		

* Liquidity data not available, funds are considered to be highly illiquid.

Contributions—Baystate Health does not expect to contribute to the plan in 2017.

Estimated Future Benefit Payments—The following approximate benefit payments, which reflect expected future service, as appropriate, are expected to be paid over the next 10 calendar years (in thousands):

Calendar Years	Pension Benefits
2017	\$ 72,839
2018	63,362
2019	60,362
2020	57,889
2022	55,253
Years 2022–2026	<u>265,847</u>
	<u>\$ 575,552</u>

Defined Contribution Plans—Baystate Health and certain of its consolidated subsidiaries and other ownership interest participate in the DC plan, which covers all employees hired after December 31, 2004. Effective December 31, 2015, the DC plan will also cover all employees previously in the defined benefit plan. Under the DC plan, Baystate Health contributes up to 7.5% of the employee’s compensation based on age and years of service. Excluding the deferred compensation plan discussed below, total expense under the DC plan was approximately \$39,471,000 in 2016 and \$12,342,000 in 2015. Effective January 1, 2016, the DC plan will offer an employee contribution matching feature where the employer will contribute equal to 50% of the employees contribution, subject to a maximum match of 2% of the employees compensation. For those defined benefit participants aged 55 or older as of January 1, 2016, Baystate Health will be contributing an additional 4% transition benefit for the next five plan years.

HNE provides a 401(k) retirement plan (the “HNE Plan”) to its employees. Each year, employees may contribute up to 75% of pretax annual compensation, as defined in the HNE Plan document. HNE matches 100% of the first 6% of employee contributions to the HNE Plan. Additional contributions may be made by HNE at its discretion. Contributions and compensation levels are subject to certain limitations under the IRC. The HNE Plan expense amounted to approximately \$1,830,000 and \$1,570,000 in 2016 and 2015, respectively.

Deferred Compensation Plan—As a component of its defined contribution retirement plan, Baystate Health established a nonqualified deferred compensation plan (the “Plan”), effective January 1, 2002, which allows certain highly compensated employees the option to defer specified amounts of their annual compensation on a pretax basis and also allows Baystate Health, at its discretion, the option to provide deferred compensation to key employees. A participant in the Plan is notified if a voluntary contribution is made by Baystate Health to that participant’s account. In addition, the participant’s account is credited to reflect investment returns based on measuring investments selected by either the participant or the Plan administrator in accordance with the plan document. The participant has the option to take a distribution of their account in its entirety, upon severance from employment with Baystate Health. Baystate Health has recorded \$46,200,000 and \$38,461,000 within other liabilities in the consolidated statements of financial position as of September 30, 2016 and 2015, respectively, which represents its obligation for benefits payable under the Plan. All amounts of compensation deferred under the Plan remain the assets of Baystate Health, until paid out to a participant or his/her beneficiary. Baystate Health is not required to segregate or set aside any assets to meet its obligation under the Plan. Baystate Health’s contributions amounted to approximately \$1,825,000 and \$1,429,000 in 2016 and 2015, respectively.

Baystate Noble Retirement Plans and Other Postretirement Benefits:

Retirement Plan—Through March 2005, Noble maintained a noncontributory defined benefit pension plan (the “Noble Plan”) covering certain eligible employees of BNH and its subsidiaries, who have completed one year of service. The benefits were based on years of service and final average earnings. Noble’s policy was to make annual cash contributions to the Noble Plan in amounts at least equal to the minimum contribution as determined by the Noble Plan’s actuary.

Effective April 1, 2006, Noble amended the Noble Plan to freeze all accrued benefits for certain participants in the Noble Plan whose benefits are not subject to collective bargaining agreements. The accrued benefit for these participants is equal to the accrued benefit determined as of April 1, 2006. The amendment prohibits new or rehired employees, not subject to a collective bargaining agreement, from becoming participants in the Noble Plan. This curtailment resulted in a reduction in the Noble Plan’s projected benefit obligation and unrecognized prior service cost which was recorded in 2006.

Pursuant to Noble's application for a distressed termination, the Pension Benefit Guaranty Corporation (PBGC) became the trustee of the Noble Plan on May 1, 2013. As part of the settlement, Noble has agreed to enter into a note payable to the PBGC totaling \$4,200,000. The amount is payable over 15 years. The balance due at September 30, 2016, is approximately \$2,896,000 of which \$2,739,000 included is classified as long term and included as a pension liability in the consolidated statements of financial position.

There were no contributions made during the years ended September 30, 2016 and 2015.

Defined Contribution Plan—The Noble 403(b) Savings Plan became effective on April 1, 2006. All eligible employees may elect to make contributions and BNH matches certain contributions up to the defined limits. In addition, BNH contributes between 2% and 10% of certain employee's eligible compensation based upon the employee's age and years of vesting service. Employees are fully vested in BNH's contributions after four years of employment.

18. CONCENTRATIONS OF CREDIT RISK

Baystate Health and its subsidiaries grant credit without collateral to its patients, most of whom are local residents and are insured under third-party payer agreements. The mix of receivables from patients and third-party payers at September 30, 2016 and 2015, is as follows:

	2016	2015
Medicare	20 %	22 %
Medicaid	21	16
Blue Cross	1	2
Health maintenance organizations	34	36
Commercial	13	13
Self-pay patients	<u>11</u>	<u>11</u>
	<u>100 %</u>	<u>100 %</u>

19. FUNCTIONAL EXPENSES

Baystate Health and its subsidiaries provide general health care services to residents within their geographic location. Expenses related to providing these services for the years ended September 30, 2016 and 2015, are as follows (in thousands):

	2016	2015
Health care services	\$ 2,226,147	\$ 2,072,114
General and administrative	<u>80,164</u>	<u>76,313</u>
	<u>\$ 2,306,311</u>	<u>\$ 2,148,427</u>

20. TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS

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

	2016	2015
Research and education	\$ 6,951	\$ 6,759
Patient care services	<u>50,430</u>	<u>48,281</u>
Total	<u>\$ 57,381</u>	<u>\$ 55,040</u>

Permanently restricted net assets are invested in perpetuity, the income which is generally expendable to support the delivery of health care services.

ASC 958-205, *Endowment of Not-for-Profit Organizations*, provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). Massachusetts enacted UPMIFA on July 2, 2009. Baystate Health is subject to ASC 958-205 disclosure requirements regarding its endowment funds.

Baystate Health's endowments consist of numerous individual funds established for a variety of purposes. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Baystate Health requires the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Baystate Health classifies as permanently restricted net assets: (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts 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 the donor-restricted endowment funds that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure. Baystate Health considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (a) the duration and preservation of the fund, (b) the purpose of Baystate Health and the donor-restricted endowment fund, (c) general economic conditions, (d) the possible effect of inflation and deflation, (e) the expected total return from income and the appreciation of investments, and (f) the investment policies of Baystate Health.

Endowment net asset composition, by type of fund, as of September 30, 2016 and 2015, consisted of the following (in thousands):

As of September 30, 2016	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 38,819	\$ 17,930	\$ 56,749
Board-designated endowment funds	<u>25,267</u>	<u>-</u>	<u>-</u>	<u>25,267</u>
Total endowment net assets	<u>\$ 25,267</u>	<u>\$ 38,819</u>	<u>\$ 17,930</u>	<u>\$ 82,016</u>
As of September 30, 2015	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 36,332	\$ 17,732	\$ 54,064
Board-designated endowment funds	<u>24,008</u>	<u>-</u>	<u>-</u>	<u>24,008</u>
Total endowment net assets	<u>\$ 24,008</u>	<u>\$ 36,332</u>	<u>\$ 17,732</u>	<u>\$ 78,072</u>

For the year ended September 30, 2016, Baystate Health had the following endowment-related activities (in thousands):

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets—October 1, 2015	<u>\$ 24,008</u>	<u>\$ 36,332</u>	<u>\$ 17,732</u>	<u>\$ 78,072</u>
Investment return:				
Investment income	172	304	-	476
Net appreciation	<u>1,974</u>	<u>4,293</u>	<u>-</u>	<u>6,267</u>
Total investment return	2,146	4,597	-	6,743
Contributions	189	-	198	387
Prior year reclassification	-	(90)	-	(90)
Amounts appropriated for expenditures	<u>(1,076)</u>	<u>(2,020)</u>	<u>-</u>	<u>(3,096)</u>
Total change in endowment funds	<u>1,259</u>	<u>2,487</u>	<u>198</u>	<u>3,944</u>
Endowment net assets—September 30, 2016	<u>\$ 25,267</u>	<u>\$ 38,819</u>	<u>\$ 17,930</u>	<u>\$ 82,016</u>

For the year ended September 30, 2015, Baystate Health had the following endowment-related activities (in thousands):

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets—October 1, 2014	<u>\$ 22,920</u>	<u>\$ 37,843</u>	<u>\$ 16,492</u>	<u>\$ 77,255</u>
Investment return:				
Investment income	169	91	-	260
Net appreciation	<u>(924)</u>	<u>(2,349)</u>	<u>-</u>	<u>(3,273)</u>
Total investment return	(755)	(2,258)	-	(3,013)
Contributions	103	-	359	462
Net asset reclassifications	-	140	-	140
Prior year reclassification	(211)	(231)	-	(442)
Board-designated funds transferred in	3,000	-	-	3,000
Transferred in—Noble acquisition	-	2,993	881	3,874
Amounts appropriated for expenditures	<u>(1,049)</u>	<u>(2,155)</u>	<u>-</u>	<u>(3,204)</u>
Total change in endowment funds	<u>1,088</u>	<u>(1,511)</u>	<u>1,240</u>	<u>817</u>
Endowment net assets—September 30, 2015	<u>\$ 24,008</u>	<u>\$ 36,332</u>	<u>\$ 17,732</u>	<u>\$ 78,072</u>

Baystate Health's investment and spending policies for endowment assets are intended to provide a predictable stream of funding to programs supported by its endowment, while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that Baystate Health must hold in perpetuity or for a donor-specified term. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that will generate an 8.5% over the long term. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, Baystate Health relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). Baystate Health targets a diversified asset allocation that consists of equities, fixed income, and alternative investments.

Baystate Health has a policy of appropriating for distribution each year, no more than 5% of its endowment funds' current fair value. In establishing this policy, Baystate Health considered the long-term expected return on its endowments.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires Baystate Health to retain as a fund of perpetual duration. There was no deficiency of this nature at September 30, 2016 and 2015.

21. STATE SURPLUS REVENUE RETENTION

Through September 30, 2015, BMC had no surplus in excess of the Commonwealth of Massachusetts' regulations governing the excess of state revenues over expenses for not-for-profit organizations. The total deficit attributable to state contracting for BMC was approximately \$158,000 (2015—\$148,000). As of September 30, 2016, the cumulative deficit attributable to state contracting of approximately \$6,705,000 and \$6,547,000, respectively, is included in the unrestricted net assets of BMC.

22. SUBSEQUENT EVENTS

See Note 10 for the subsequent event related to the NMTC unwind.

Subsequent events have been evaluated for potential recognition in the consolidated financial statements through January 10, 2017, which is the date the consolidated financial statements were issued.

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CONSOLIDATING SUPPLEMENTARY FINANCIAL INFORMATION

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF ASSETS AS OF SEPTEMBER 30, 2015 (In thousands)

	Consolidated BMC	BFMC	BWH	BNH Consolidated	BMLH	BMP	BVNAH	HNE	Consolidated IC	Other Entities	Eliminations and Reclass	Consolidated Total
ASSETS												
CURRENT ASSETS:												
Cash and cash equivalents	\$ 83,637	\$ 9,900	\$ 5,861	\$ 2,197	\$ -	\$ 2,507	\$ 364	\$ 43,043	\$ 28	\$ 45,353	\$ -	\$ 192,890
Investments	196,752	8,042	6,237	702	-	-	-	103,985	-	12,791	-	328,509
Accounts receivable, patients—net	109,074	10,427	10,354	7,002	-	14,296	3,800	-	-	-	(18,779)	136,174
Accounts receivable, other	6,323	137	236	225	-	4,973	23	39,466	72	5,430	-	56,885
Estimated final settlements receivable	16,374	252	922	386	-	-	-	-	-	-	-	17,934
Inventories	25,078	1,583	1,174	972	-	-	-	-	-	56	-	28,863
Prepaid expenses and other current assets	6,122	198	196	209	-	1,162	74	7,178	12	9,354	-	24,505
Due from affiliated companies	28,969	422	169	-	-	9,249	128	-	39	117,589	(156,565)	-
Line of credit, affiliate	-	-	-	-	-	-	-	-	-	1,116	(1,116)	-
Total current assets	<u>472,329</u>	<u>30,961</u>	<u>25,149</u>	<u>11,693</u>	<u>-</u>	<u>32,187</u>	<u>4,389</u>	<u>193,672</u>	<u>151</u>	<u>191,689</u>	<u>(176,460)</u>	<u>785,760</u>
LONG-TERM ASSETS:												
Investments	-	-	-	-	-	-	-	861	-	56,144	(120)	56,885
Equity investment in consolidated subsidiaries	-	-	-	-	-	-	-	-	-	48,213	(48,213)	-
Equity investment in unconsolidated affiliate	2,061	536	-	-	-	-	-	-	-	76	-	2,673
Notes receivable	69,344	-	-	-	-	-	-	-	-	-	-	69,344
Beneficial interest in net assets of BHF	13,829	13,472	2,147	-	-	-	811	-	-	-	(30,259)	-
Deferred expense and other long-term assets	13,372	564	258	130	-	292	-	433	-	21,568	-	36,617
Goodwill	1,552	-	-	-	-	-	-	-	-	4,132	-	5,684
Land, buildings, and equipment—net	<u>571,804</u>	<u>55,674</u>	<u>45,730</u>	<u>20,701</u>	<u>-</u>	<u>10,877</u>	<u>1,597</u>	<u>4,274</u>	<u>1,687</u>	<u>2,288</u>	<u>-</u>	<u>714,632</u>
	<u>671,962</u>	<u>70,246</u>	<u>48,135</u>	<u>20,831</u>	<u>-</u>	<u>11,169</u>	<u>2,408</u>	<u>5,568</u>	<u>1,687</u>	<u>132,421</u>	<u>(78,592)</u>	<u>885,835</u>
ASSETS WHOSE USE IS LIMITED:												
Board-designated funds:												
Cash and investments	225,194	-	7,588	3,918	-	-	-	-	-	32,826	-	269,526
Beneficial interest in net assets of BHF	-	-	198	-	-	-	343	-	-	1,872	(2,413)	-
Due from unrestricted funds	1,019	-	-	-	-	-	-	-	-	-	(1,019)	-
Investments of captive insurance company	-	-	-	-	-	-	-	-	-	84,808	-	84,808
Investments held by trustee under debt agreements	15,206	66	-	-	-	-	-	-	-	-	-	15,272
Beneficial interest in net assets of BHF	1,340	4,815	6,646	-	-	-	899	-	-	19,790	(33,490)	-
Beneficial interest in perpetual trusts	-	-	2,079	-	-	-	-	-	-	33,490	-	35,569
Deferred compensation investments	-	-	-	-	-	-	-	-	-	46,200	-	46,200
	<u>242,759</u>	<u>4,881</u>	<u>16,511</u>	<u>3,918</u>	<u>-</u>	<u>-</u>	<u>1,242</u>	<u>-</u>	<u>-</u>	<u>218,986</u>	<u>(36,922)</u>	<u>451,375</u>
TOTAL ASSETS	<u>\$1,387,050</u>	<u>\$106,088</u>	<u>\$89,795</u>	<u>\$36,442</u>	<u>\$ -</u>	<u>\$43,356</u>	<u>\$8,039</u>	<u>\$199,240</u>	<u>\$1,838</u>	<u>\$543,096</u>	<u>\$(291,974)</u>	<u>\$2,122,970</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF LIABILITIES AND NET ASSETS

AS OF SEPTEMBER 30, 2016

(In thousands)

LIABILITIES AND NET ASSETS (DEFICIT)	Consolidated BMC	BFMC	BWH	BNH Consolidated	BMLH	BMP	BVNAH	HNE	Consolidated IC	Other Entities	Eliminations and Reclass	Consolidated Total
CURRENT LIABILITIES:												
Accounts payable	\$ 72,000	\$ 6,760	\$ 7,729	\$ 6,837	\$ -	\$ 14,676	\$ 2,001	\$ 18,914	\$ 205	\$ 20,623	\$ 595	\$ 150,340
Medical claims payable	-	-	-	-	-	-	-	78,657	-	-	(18,779)	59,878
Accrued salaries and wages	41,315	3,299	4,407	2,157	-	27,485	1,279	3,845	-	11,878	-	95,665
Accrued interest payable	2,071	-	39	133	-	-	-	-	-	-	-	2,243
Estimated final settlements payable	29,874	2,692	3,482	2,799	-	-	709	-	-	-	-	39,556
Deferred revenue	906	462	224	378	-	16	502	21,907	40	305	-	24,740
Current portion of long-term debt	10,711	1,007	371	8,413	-	-	-	-	-	740	(8,226)	13,016
Current portion of capital lease obligations	4,568	-	32	463	-	-	-	-	-	-	-	5,063
Due to affiliated companies	8,384	3,748	3,991	7,111	-	18,650	2,527	6,095	638	3,476	(54,620)	-
Line of credit, affiliate	-	-	-	-	-	532	-	-	584	-	(1,116)	-
Due to board-designated funds	-	-	-	-	-	-	-	-	-	1,019	(1,019)	-
Total current liabilities	169,829	17,968	20,275	28,291	-	61,359	7,018	129,418	1,467	38,041	(83,165)	390,501
Long-term debt	456,984	25,871	12,703	568	-	-	-	20,000	-	53,521	(20,000)	549,647
Capital lease obligations	16,603	-	32	1,038	-	-	-	-	-	-	-	17,673
Pension liability	71,757	11,686	2,885	2,738	-	25,272	2,998	-	-	16,572	-	133,908
Insurance liability loss reserves	8,489	144	301	298	-	10,888	63	-	-	106,527	(94)	126,616
Deposit liability	-	-	-	-	-	-	-	-	-	73,475	(73,475)	-
Other liabilities	6,083	492	1,092	572	-	-	-	369	-	46,278	-	54,886
Total liabilities	729,745	56,161	37,288	33,505	-	97,519	10,079	149,787	1,467	334,414	(176,734)	1,273,231
NET ASSETS (DEFICIT):												
Unrestricted:												
Operating	880,889	60,341	48,177	(1,913)	-	30,034	3,541	49,453	371	111,397	(37,979)	1,144,311
Pension adjustment	(238,753)	(28,701)	(7,831)	-	-	(84,197)	(7,291)	-	-	(38,679)	-	(405,452)
Unrestricted	642,136	31,640	40,346	(1,913)	-	(54,163)	(3,750)	49,453	371	72,718	(37,979)	738,859
Temporarily restricted	10,889	9,965	3,107	3,969	-	-	137	-	-	62,579	(33,265)	57,381
Permanently restricted	4,280	8,322	9,054	881	-	-	1,573	-	-	73,385	(43,996)	53,499
Total net assets (deficit)	657,305	49,927	52,507	2,937	-	(54,163)	(2,040)	49,453	371	208,682	(115,240)	849,739
TOTAL LIABILITIES AND NET ASSETS (DEFICIT)	\$1,387,050	\$106,088	\$89,795	\$36,442	\$ -	\$ 43,356	\$ 8,039	\$199,240	\$1,838	\$543,096	\$(291,974)	\$2,122,970

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF OPERATIONS FOR THE YEAR ENDED SEPTEMBER 30, 2016

(In thousands)

	Consolidated BMC	BFMC	BWH	BNH Consolidated	BMLH	BMP	BVNAH	HNE	Consolidated IC	Other Entities	Eliminations and Reclass	Consolidated Total
OPERATING REVENUES:												
Net patient service revenue	\$1,110,825	\$ 95,604	\$ 74,340	\$ 81,498	\$ 21,068	\$ 161,343	\$19,605	\$ -	\$ -	\$ -	\$(225,420)	\$1,338,863
Bad debts	15,122	2,167	2,427	4,007	686	5,434	3	-	-	-	-	29,846
Net patient service revenue, net of bad debts	1,095,703	93,437	71,913	77,491	20,382	155,909	19,602	-	-	-	(225,420)	1,309,017
Premiums	-	-	-	-	-	-	-	940,877	-	3,295	-	944,172
Other revenue	79,973	4,039	3,251	3,452	1,581	106,936	801	14,372	753	131,108	(252,154)	94,112
Net assets released from restrictions for operations	1,608	588	3	544	-	180	31	-	-	4,864	(2,184)	5,634
Total operating revenues	1,177,284	98,064	75,167	81,487	21,963	263,025	20,434	955,249	753	139,267	(479,758)	2,352,935
OPERATING EXPENSES:												
Salaries and wages	414,624	37,730	36,298	42,603	8,043	219,900	11,926	42,970	-	54,457	-	868,551
Supplies and expense	624,186	52,798	39,814	38,216	13,720	73,907	8,985	44,105	504	81,810	(252,677)	725,368
Medical claims and capitation	-	-	-	-	-	-	-	852,544	-	-	(227,081)	625,463
Depreciation and amortization	59,551	4,569	3,478	2,480	1,266	1,679	249	2,042	116	112	-	75,542
Interest expense	9,783	287	531	362	-	6	-	-	7	411	-	11,387
Total operating expenses	1,108,144	95,384	80,121	83,661	23,029	295,492	21,160	941,661	627	136,790	(479,758)	2,306,311
INCOME (LOSS) FROM OPERATIONS BEFORE OTHER												
INCOME—Net	69,140	2,680	(4,954)	(2,174)	(1,066)	(32,467)	(726)	13,588	126	2,477	-	46,624
OTHER INCOME (LOSS)—Net	(7,891)	(514)	(1,880)	(522)	(473)	(2,428)	(499)	(581)	-	(2,855)	-	(17,643)
INCOME (LOSS) FROM OPERATIONS	61,249	2,166	(6,834)	(2,696)	(1,539)	(34,895)	(1,225)	13,007	126	(378)	-	28,981
NONOPERATING INCOME (LOSS):												
Investment income	1,665	-	19	-	1	-	-	-	-	49	609	2,343
Net realized gain (loss) on investments	35,422	-	249	-	19	-	20	(258)	-	1,393	1,515	38,360
Net unrealized gain (loss) on investments	354	42	375	-	13	-	8	1,949	-	5,777	2,516	11,034
Equity gain (loss) in consolidated for-profit subsidiaries	-	-	-	-	-	-	-	-	-	123	(123)	-
Equity gain (loss) in unconsolidated affiliates	(7)	-	-	-	-	-	-	-	-	81	-	74
Net interest cost on swap agreements	(1,633)	-	-	-	-	-	-	-	-	-	-	(1,633)
Change in fair value of swap agreements	702	-	-	-	-	-	-	-	-	-	-	702
Income taxes and other	-	-	-	-	-	-	(13)	467	(5)	(6,915)	(12,988)	(19,454)
Total nonoperating (loss) income	36,503	42	643	-	33	-	15	2,158	(5)	508	(8,471)	31,426
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	97,752	2,208	(6,191)	(2,696)	(1,506)	(34,895)	(1,210)	15,165	121	130	(8,471)	60,407
OTHER CHANGES IN UNRESTRICTED NET ASSETS:												
Net assets released from restrictions for capital	1,603	1,634	4	-	46	40	-	-	-	-	-	3,327
Funds utilized for property and equipment	400	-	-	-	-	-	-	-	-	-	-	400
Transfers for the cost of land, buildings, and equipment	1,272	-	364	1,727	-	705	-	-	-	(4,068)	-	-
Transfers (to) from affiliated companies—net	(53,543)	-	8,151	1,000	(8,151)	43,871	1,472	-	-	7,200	-	-
Contributed capital asset	6,084	-	-	-	-	-	-	-	-	-	-	6,084
Pension adjustment	(34,660)	(3,669)	(1,250)	-	-	(12,330)	(993)	-	-	(5,498)	-	(58,400)
Other	-	(1)	(92)	-	-	2	-	1	-	89	-	(1)
(DECREASE) INCREASE IN UNRESTRICTED NET ASSETS	\$ 18,908	\$ 172	\$ 986	\$ 31	\$ (9,611)	\$ (2,607)	\$ (731)	\$ 15,166	\$ 121	\$ (2,147)	\$ (8,471)	\$ 11,817

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF CHANGES IN NET ASSETS

FOR THE YEAR ENDED SEPTEMBER 30, 2016

(In thousands)

	Consolidated BMC	BFMC	BWH	BNH Consolidated	BMLH	BMP	BVNAH	HNE	Consolidated IC	Other Entities	Eliminations and Reclass	Consolidated Total
UNRESTRICTED NET ASSETS:												
Excess (deficiency) of revenues over expenses	\$ 97,752	\$ 2,208	\$ (6,191)	\$ (2,696)	\$ (1,506)	\$ (34,895)	\$ (1,210)	\$ 15,165	\$ 121	\$ 130	\$ (8,471)	\$ 60,407
Net assets released from restrictions for capital	1,603	1,634	4	-	46	40	-	-	-	-	-	3,327
Funds utilized for property and equipment	400	-	-	-	-	-	-	-	-	-	-	400
Transfers for the cost of land, buildings, and equipment	1,272	-	364	1,727	-	705	-	-	-	(4,068)	-	-
Transfers (to) from restricted net assets	-	-	-	-	-	-	-	-	-	-	-	-
Transfers (to) from affiliated companies—net	(53,543)	-	8,151	1,000	(8,151)	43,871	1,472	-	-	7,200	-	-
Contributed capital asset	6,084	-	-	-	-	-	-	-	-	-	-	6,084
Pension adjustment	(34,660)	(3,669)	(1,250)	-	-	(12,330)	(993)	-	-	(5,498)	-	(58,400)
Other	-	(1)	(92)	-	-	2	-	1	-	89	-	(1)
(Decrease) increase in unrestricted net assets	<u>18,908</u>	<u>172</u>	<u>986</u>	<u>31</u>	<u>(9,611)</u>	<u>(2,607)</u>	<u>(731)</u>	<u>15,166</u>	<u>121</u>	<u>(2,147)</u>	<u>(8,471)</u>	<u>11,817</u>
TEMPORARILY RESTRICTED NET ASSETS:												
Restricted investment income	-	-	-	-	-	-	-	-	-	223	-	223
Net realized and unrealized gain on investments	-	-	-	388	-	-	-	-	-	4,461	-	4,849
Contributions	-	-	20	334	-	-	-	-	-	6,134	-	6,488
Transfers for the cost of land, buildings, and equipment	-	-	-	-	-	-	-	-	-	(3,321)	3,321	-
Transfers from affiliated companies, net	-	-	-	-	-	-	-	-	-	(74)	74	-
Net assets released from restrictions:												
For operations	-	-	(3)	(544)	-	-	-	-	-	(5,087)	-	(5,634)
For capital	-	-	(4)	-	-	-	-	-	-	-	(3,323)	(3,327)
Change in value of beneficial interest in net assets of BHF	(398)	66	1,166	-	58	-	(5)	-	-	-	(887)	-
Transfers (to) from affiliated companies—net	-	-	664	-	(664)	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-	-	-	12	(270)	(258)
(Decrease) increase in temporarily restricted net assets	<u>(398)</u>	<u>66</u>	<u>1,843</u>	<u>178</u>	<u>(606)</u>	<u>-</u>	<u>(5)</u>	<u>-</u>	<u>-</u>	<u>2,348</u>	<u>(1,085)</u>	<u>2,341</u>
PERMANENTLY RESTRICTED NET ASSETS:												
Contributions	-	-	-	-	-	-	-	-	-	199	(1)	198
Change in value of perpetual trusts	-	-	96	-	-	-	-	-	-	1,311	-	1,407
Change in value of beneficial interest in net assets of BHF	53	178	170	-	99	-	86	-	-	774	(1,360)	-
Transfers (to) from affiliated companies—net	-	-	6,647	-	(6,645)	-	-	-	-	-	(2)	-
Increase (decrease) in permanently restricted net assets	<u>53</u>	<u>178</u>	<u>6,913</u>	<u>-</u>	<u>(6,546)</u>	<u>-</u>	<u>86</u>	<u>-</u>	<u>-</u>	<u>2,284</u>	<u>(1,363)</u>	<u>1,605</u>
(DECREASE) INCREASE IN NET ASSETS	18,563	416	9,742	209	(16,763)	(2,607)	(650)	15,166	121	2,485	(10,919)	15,763
NET ASSETS (DEFICIT)—Beginning of year	<u>638,742</u>	<u>49,511</u>	<u>42,765</u>	<u>2,728</u>	<u>16,763</u>	<u>(51,556)</u>	<u>(1,390)</u>	<u>34,287</u>	<u>250</u>	<u>206,197</u>	<u>(104,321)</u>	<u>833,976</u>
NET ASSETS (DEFICIT)—End of year	<u>\$657,305</u>	<u>\$49,927</u>	<u>\$52,507</u>	<u>\$ 2,937</u>	<u>\$ -</u>	<u>\$ (54,163)</u>	<u>\$ (2,040)</u>	<u>\$ 49,453</u>	<u>\$ 371</u>	<u>\$208,682</u>	<u>\$ (115,240)</u>	<u>\$ 849,739</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF CASH FLOWS FOR THE YEAR ENDED SEPTEMBER 30, 2016

(In thousands)

	Consolidated BMC	BFMC	BWH	BNH Consol.	BMLH	BMP	BVNAH	HNE	Consolidated IC	Other Entities	Elim. & Reclass.	Consolidated Total
OPERATING ACTIVITIES:												
(Decrease) increase in net assets	\$ 18,563	\$ 416	\$ 9,742	\$ 209	\$ (16,763)	\$ (2,607)	\$ (650)	\$ 15,166	\$ 121	\$ 2,485	\$ (10,919)	\$ 15,763
Adjustments to reconcile (decrease) increase in net assets to net cash provided by (used in) operating activities:												
Depreciation and amortization	59,551	4,569	3,478	2,480	1,266	1,679	249	2,042	116	112	-	75,542
Accretion on notes receivable	(1,401)	-	-	-	-	-	-	-	-	-	-	(1,401)
Pension adjustment	34,660	3,669	1,250	-	-	12,330	993	-	-	5,498	-	58,400
Net realized and unrealized loss (gain) on investments	(36,766)	-	(624)	(388)	(32)	-	(28)	(2,596)	-	(11,631)	(4,031)	(56,096)
Provision for bad debts	15,122	2,167	2,427	4,007	686	5,434	3	-	-	-	-	29,846
Change in fair value of perpetual trusts	-	-	(96)	-	-	-	-	-	-	(1,311)	-	(1,407)
Restricted contributions	-	-	(20)	(334)	-	-	-	-	-	(6,332)	-	(6,686)
Changes in equity investment of affiliate	(317)	-	-	-	-	-	-	-	-	-	123	(194)
Contributed capital asset	(6,084)	-	-	-	-	-	-	-	-	-	-	(6,084)
Changes in operating assets and liabilities:												
(Increase) decrease in accounts receivable, patients	(21,505)	(2,766)	(3,815)	(3,731)	8	(3,800)	45	-	-	-	936	(34,628)
Net estimated final settlements	1,931	(423)	(1,584)	(1,873)	(405)	-	-	-	-	-	-	(2,354)
Accounts payable and accrued expenses	14,489	(2,460)	856	(4,022)	(1,275)	2,402	491	(12,931)	2	992	213	(1,243)
Pension liability	(25,193)	(2,476)	(328)	(37)	(479)	(9,826)	(602)	-	-	(3,275)	-	(42,216)
Medical claims payable	-	-	-	-	-	-	-	(13,528)	-	-	(936)	(14,464)
Transfers to (from) affiliated companies—net	53,543	-	(12,460)	(1,000)	12,460	(43,871)	(1,472)	-	-	(7,200)	-	-
Transfers for the cost of land, buildings, and equipment	(1,272)	-	(364)	(1,727)	-	(705)	-	-	-	4,068	-	-
Insurance liability loss reserves	-	-	-	-	-	567	-	-	-	(5,507)	8,021	3,081
Other	1,742	1,873	992	6,196	1,405	(12,912)	(525)	(2,474)	(97)	(45,099)	28,512	(20,387)
Net cash provided by (used in) operating activities	107,063	4,569	(546)	(220)	(3,129)	(51,309)	(1,496)	(14,321)	142	(67,200)	21,919	(4,528)
INVESTING ACTIVITIES:												
Proceeds from sale and maturities of investments	707,552	11,908	8,251	446	2,328	-	-	57,012	-	113,146	4,031	904,674
Purchase of investments	(713,632)	(8,042)	(1,876)	(76)	-	-	28	(50,090)	-	(78,659)	-	(852,347)
Purchase of land, buildings, and equipment	(53,376)	(12,677)	(1,521)	(3,673)	(293)	(778)	(53)	(3,838)	-	(1,814)	-	(78,023)
Transfers for the cost of land, buildings, and equipment	1,272	-	364	1,727	-	705	-	-	-	(4,068)	-	-
Change in beneficial interest in net assets of BHF	345	(244)	(1,167)	-	(170)	-	(96)	-	-	(944)	2,276	-
Net cash (used in) provided by investing activities	(57,839)	(9,055)	4,051	(1,576)	1,865	(73)	(121)	3,084	-	27,661	6,307	(25,696)
FINANCING ACTIVITIES:												
Proceeds from restricted contributions	-	-	20	334	-	-	-	-	-	6,332	-	6,686
Transfers (to) from affiliated companies—net	(53,543)	-	-	1,000	-	43,871	1,472	-	-	7,200	-	-
Repayment of notes receivable	573	-	-	-	-	-	-	-	-	-	-	573
Change in line of credit, affiliate	-	-	-	-	-	(95)	-	-	(137)	232	-	-
Proceeds from debt issuance	34,063	-	-	8,226	-	-	-	20,000	-	37,241	(28,226)	71,304
Repayments of debt and capital lease obligations	(30,083)	(609)	(386)	(6,602)	-	-	-	-	-	(740)	-	(38,420)
Net cash provided by (used in) financing activities	(48,990)	(609)	(366)	2,958	-	43,776	1,472	20,000	(137)	50,265	(28,226)	40,143
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	234	(5,095)	3,139	1,162	(1,264)	(7,606)	(145)	8,763	5	10,726	-	9,919
CASH AND CASH EQUIVALENTS—Beginning of year	83,403	14,995	2,722	1,035	1,264	10,113	509	34,280	23	34,627	-	182,971
CASH AND CASH EQUIVALENTS—End of year	\$ 83,637	\$ 9,900	\$ 5,861	\$ 2,197	\$ -	\$ 2,507	\$ 364	\$ 43,043	\$ 28	\$ 45,353	\$ -	\$ 192,890

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF ASSETS—BAYSTATE MEDICAL CENTER AND SUBSIDIARY AS OF SEPTEMBER 30, 2016 (In thousands)

	BMC	BTHC	Eliminations and Reclass	Consolidated Total
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents	\$ 83,627	\$ 10	\$ -	\$ 83,637
Investments	196,752	-	-	196,752
Accounts receivable, patients—net	109,074	-	-	109,074
Accounts receivable, other	6,323	-	-	6,323
Estimated final settlements receivable	16,374	-	-	16,374
Inventories	25,078	-	-	25,078
Prepaid expenses and other current assets	6,122	25	(25)	6,122
Due from affiliated companies	67,931	-	(38,962)	28,969
	<u>511,281</u>	<u>35</u>	<u>(38,987)</u>	<u>472,329</u>
Total current assets				
LONG-TERM ASSETS:				
Equity investment in unconsolidated affiliates	2,061	-	-	2,061
Notes receivable	192,566	-	(123,222)	69,344
Beneficial interest in net assets of BHF	13,829	-	-	13,829
Deferred expense and other long-term assets	12,372	1,000	-	13,372
Goodwill	1,552	-	-	1,552
Land, buildings, and equipment—net	353,604	223,148	(4,948)	571,804
	<u>575,984</u>	<u>224,148</u>	<u>(128,170)</u>	<u>671,962</u>
ASSETS WHOSE USE IS LIMITED:				
Board-designated funds:				
Cash and investments	225,194	-	-	225,194
Due from unrestricted funds	1,019	-	-	1,019
Investments held by trustee under debt agreements	15,109	97	-	15,206
Beneficial interest in net assets of BHF	1,340	-	-	1,340
	<u>242,662</u>	<u>97</u>	<u>-</u>	<u>242,759</u>
TOTAL ASSETS	<u>\$ 1,329,927</u>	<u>\$ 224,280</u>	<u>\$(167,157)</u>	<u>\$ 1,387,050</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF LIABILITIES AND NET ASSETS—BAYSTATE MEDICAL CENTER AND SUBSIDIARY AS OF SEPTEMBER 30, 2016 (In thousands)

	BMC	BTHC	Eliminations and Reclass	Consolidated Total
LIABILITIES AND NET ASSETS (DEFICIT)				
CURRENT LIABILITIES:				
Accounts payable	\$ 71,999	\$ 1	\$ -	\$ 72,000
Accrued salaries and wages	41,315	-	-	41,315
Accrued interest payable	2,071	1,521	(1,521)	2,071
Estimated final settlements payable	29,874	-	-	29,874
Deferred revenue	931	-	(25)	906
Current portion of long-term debt	7,571	3,140	-	10,711
Current portion of capital lease obligations	4,568	-	-	4,568
Due to affiliated companies	8,384	38,962	(38,962)	8,384
Total current liabilities	166,713	43,624	(40,508)	169,829
LONG-TERM DEBT	378,335	200,350	(121,701)	456,984
CAPITAL LEASE OBLIGATIONS	16,603	-	-	16,603
PENSION LIABILITY	71,757	-	-	71,757
INSURANCE LIABILITY LOSS RESERVES	8,489	-	-	8,489
OTHER LIABILITIES	6,083	-	-	6,083
Total liabilities	647,980	243,974	(162,209)	729,745
NET ASSETS (DEFICIT):				
Unrestricted:				
Operating	905,531	(19,694)	(4,948)	880,889
Pension adjustment	(238,753)	-	-	(238,753)
Unrestricted	666,778	(19,694)	(4,948)	642,136
Temporarily restricted	10,889	-	-	10,889
Permanently restricted	4,280	-	-	4,280
Total net assets (deficit)	681,947	(19,694)	(4,948)	657,305
TOTAL LIABILITIES AND NET ASSETS (DEFICIT)	\$1,329,927	\$224,280	\$(167,157)	\$1,387,050

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF OPERATIONS—BAYSTATE MEDICAL CENTER AND SUBSIDIARY FOR THE YEAR ENDED SEPTEMBER 30, 2016

(In thousands)

	BMC	BTHC	Eliminations and Reclass	Consolidated Total
OPERATING REVENUES:				
Net patient service revenue	\$ 1,110,825	\$ -	\$ -	\$ 1,110,825
Bad debts	<u>15,122</u>	<u>-</u>	<u>-</u>	<u>15,122</u>
Net patient service revenue—net of bad debts	1,095,703	-	-	1,095,703
Other revenue	86,229	10,595	(16,851)	79,973
Net assets released from restrictions for operations	<u>1,608</u>	<u>-</u>	<u>-</u>	<u>1,608</u>
Total operating revenues	<u>1,183,540</u>	<u>10,595</u>	<u>(16,851)</u>	<u>1,177,284</u>
OPERATING EXPENSES:				
Salaries and wages	414,624	-	-	414,624
Supplies and expense	634,711	170	(10,695)	624,186
Depreciation and amortization	49,451	10,263	(163)	59,551
Interest expense	<u>8,075</u>	<u>7,864</u>	<u>(6,156)</u>	<u>9,783</u>
Total operating expenses	<u>1,106,861</u>	<u>18,297</u>	<u>(17,014)</u>	<u>1,108,144</u>
INCOME (LOSS) FROM OPERATIONS BEFORE OTHER INCOME—Net	76,679	(7,702)	163	69,140
OTHER INCOME—Net	<u>(7,891)</u>	<u>-</u>	<u>-</u>	<u>(7,891)</u>
INCOME (LOSS) FROM OPERATIONS	<u>68,788</u>	<u>(7,702)</u>	<u>163</u>	<u>61,249</u>
NONOPERATING INCOME (LOSS):				
Investment income	1,665	-	-	1,665
Net realized gain on investments	35,422	-	-	35,422
Net unrealized gain on investments	354	-	-	354
Equity gain in unconsolidated affiliates	(7)	-	-	(7)
Net interest cost on swap agreements	(1,633)	-	-	(1,633)
Change in fair value of swap agreements	<u>702</u>	<u>-</u>	<u>-</u>	<u>702</u>
Total nonoperating loss	<u>36,503</u>	<u>-</u>	<u>-</u>	<u>36,503</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	105,291	(7,702)	163	97,752
OTHER CHANGES IN UNRESTRICTED NET ASSETS:				
Net assets released from restrictions for capital	1,603	-	-	1,603
Funds utilized for property and equipment	400	-	-	400
Transfers for the cost of land, buildings, and equipment	1,272	-	-	1,272
Transfers to affiliated companies—net	(53,543)	-	-	(53,543)
Contributed capital asset	-	6,084	-	6,084
Pension adjustment	<u>(34,660)</u>	<u>-</u>	<u>-</u>	<u>(34,660)</u>
(DECREASE) INCREASE IN UNRESTRICTED NET ASSETS	<u>\$ 20,363</u>	<u>\$ (1,618)</u>	<u>\$ 163</u>	<u>\$ 18,908</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING STATEMENT OF CHANGES IN NET ASSETS—BAYSTATE MEDICAL CENTER AND SUBSIDIARY FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BMC	BTHC	Eliminations and Reclass	Consolidated Total
UNRESTRICTED NET ASSETS:				
Excess (deficiency) of revenues over expenses	\$105,291	\$ (7,702)	\$ 163	\$ 97,752
Net assets released from restrictions for capital	1,603	-	-	1,603
Funds utilized for property and equipment	400	-	-	400
Transfers for the cost of land, buildings, and equipment	1,272	-	-	1,272
Transfers to affiliated companies—net	(53,543)	-	-	(53,543)
Contributed capital asset	-	6,084	-	6,084
Pension adjustment	(34,660)	-	-	(34,660)
	<u>20,363</u>	<u>(1,618)</u>	<u>163</u>	<u>18,908</u>
(Decrease) increase in unrestricted net assets				
TEMPORARILY RESTRICTED NET ASSETS—Change in value of beneficial interest in net assets of BHF				
	<u>(398)</u>	<u>-</u>	<u>-</u>	<u>(398)</u>
Decrease in temporarily restricted net assets				
	<u>(398)</u>	<u>-</u>	<u>-</u>	<u>(398)</u>
PERMANENTLY RESTRICTED NET ASSETS—Change in value of beneficial interest in net assets of BHF				
	<u>53</u>	<u>-</u>	<u>-</u>	<u>53</u>
Increase in permanently restricted net assets				
	<u>53</u>	<u>-</u>	<u>-</u>	<u>53</u>
(DECREASE) INCREASE IN NET ASSETS	20,018	(1,618)	163	18,563
NET ASSETS (DEFICIT)—Beginning of year	<u>661,929</u>	<u>(18,076)</u>	<u>(5,111)</u>	<u>638,742</u>
NET ASSETS (DEFICIT)—End of year	<u>\$681,947</u>	<u>\$(19,694)</u>	<u>\$(4,948)</u>	<u>\$657,305</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF CASH FLOWS—BAYSTATE MEDICAL CENTER AND SUBSIDIARY FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BMC	BTHC	Eliminations and Reclass	Consolidated Total
OPERATING ACTIVITIES:				
Increase (decrease) in net assets	\$ 20,018	\$ (1,618)	\$ 163	\$ 18,563
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:				
Depreciation and amortization	49,451	10,263	(163)	59,551
Accretion on notes receivable	(1,401)	-	-	(1,401)
Pension adjustment	34,660	-	-	34,660
Net realized and unrealized gain on investments	(36,766)	-	-	(36,766)
Provision for bad debts	15,122	-	-	15,122
Changes in equity investment of affiliate	(317)	-	-	(317)
Contributed capital asset	-	(6,084)	-	(6,084)
Changes in operating assets and liabilities:				
Accounts receivable, patients	(21,505)	-	-	(21,505)
Net estimated final settlements	1,931	-	-	1,931
Accounts payable and accrued expenses	15,013	(559)	35	14,489
Pension liability	(25,193)	-	-	(25,193)
Transfers to affiliated companies—net	53,543	-	-	53,543
Transfers for the cost of land, buildings, and equipment	(1,272)	-	-	(1,272)
Insurance liability loss reserves	-	-	-	-
Other	(21,278)	20,212	2,808	1,742
Net cash provided by (used in) operating activities	<u>82,006</u>	<u>22,214</u>	<u>2,843</u>	<u>107,063</u>
INVESTING ACTIVITIES:				
Proceeds from sale and maturities of investments	707,468	84	-	707,552
Purchase of investments	(713,632)	-	-	(713,632)
Purchase of land, buildings, and equipment—net	(53,376)	-	-	(53,376)
Transfers for the cost of land, buildings, and equipment	1,272	-	-	1,272
Change in beneficial interest in net assets of BHF	345	-	-	345
Net cash (used in) provided by investing activities	<u>(57,923)</u>	<u>84</u>	<u>-</u>	<u>(57,839)</u>
FINANCING ACTIVITIES:				
Transfers to affiliated companies—net	(53,543)	-	-	(53,543)
Repayment of notes receivable	3,416	-	(2,843)	573
Proceeds from bond issuance	34,063	-	-	34,063
Repayment of debt and capital lease obligations	(7,275)	(22,808)	-	(30,083)
Net cash provided by (used in) financing activities	<u>(23,339)</u>	<u>(22,808)</u>	<u>(2,843)</u>	<u>(48,990)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	744	(510)	-	234
CASH AND CASH EQUIVALENTS—Beginning of year	<u>82,883</u>	<u>520</u>	<u>-</u>	<u>83,403</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 83,627</u>	<u>\$ 10</u>	<u>\$ -</u>	<u>\$ 83,637</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF ASSETS—BAYSTATE NOBLE HOSPITAL AND SUBSIDIARIES AS OF SEPTEMBER 30, 2016 (In thousands)

	BNH	BWMC	BNVNAH	Eliminations and Reclass	Consolidated Total
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	\$ 1,907	\$ 207	\$ 83	\$-	\$ 2,197
Investments	702	-	-	-	702
Accounts receivable, patients—net	3,868	736	2,398	-	7,002
Accounts receivable—other	154	71	-	-	225
Estimated final settlements receivable	386	-	-	-	386
Inventories	972	-	-	-	972
Prepaid expenses and other current assets	157	52	-	-	209
Due from affiliated companies	<u>359</u>	<u>-</u>	<u>-</u>	<u>(359)</u>	<u>-</u>
Total current assets	<u>8,505</u>	<u>1,066</u>	<u>2,481</u>	<u>(359)</u>	<u>11,693</u>
LONG-TERM ASSETS:					
Deferred expense and other long-term assets	110	20	-	-	130
Land, buildings, and equipment—net	<u>18,972</u>	<u>1,578</u>	<u>151</u>	<u>-</u>	<u>20,701</u>
	<u>19,082</u>	<u>1,598</u>	<u>151</u>	<u>-</u>	<u>20,831</u>
ASSETS WHOSE USE IS LIMITED—Board-designated funds—cash and investments	<u>3,918</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,918</u>
	<u>3,918</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,918</u>
TOTAL ASSETS	<u>\$31,505</u>	<u>\$2,664</u>	<u>\$2,632</u>	<u>\$(359)</u>	<u>\$36,442</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF LIABILITIES AND NET ASSETS—BAYSTATE NOBLE HOSPITAL AND SUBSIDIARIES AS OF SEPTEMBER 30, 2016 (In thousands)

	BNH	BWMC	BNVNAH	Eliminations and Reclass	Consolidated Total
LIABILITIES AND NET ASSETS					
CURRENT LIABILITIES:					
Accounts payable	\$ 5,602	\$ 653	\$ 582	\$-	\$ 6,837
Accrued salaries and wages	1,619	219	319	-	2,157
Accrued interest payable	133	-	-	-	133
Estimated final settlements payable	2,597	(6)	208	-	2,799
Deferred revenue	-	-	378	-	378
Current portion of long-term debt	6,978	-	1,435	-	8,413
Current portion capital lease obligations	427	36	-	-	463
Due to affiliated companies	<u>6,997</u>	<u>-</u>	<u>473</u>	<u>(359)</u>	<u>7,111</u>
Total current liabilities	24,353	902	3,395	(359)	28,291
LONG-TERM DEBT	568	-	-	-	568
CAPITAL LEASE OBLIGATIONS	698	340	-	-	1,038
PENSION LIABILITY	2,738	-	-	-	2,738
INSURANCE LIABILITY LOSS RESERVES	221	77	-	-	298
OTHER LIABILITIES	<u>572</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>572</u>
Total liabilities	<u>29,150</u>	<u>1,319</u>	<u>3,395</u>	<u>(359)</u>	<u>33,505</u>
NET ASSETS (DEFICIT):					
Unrestricted:					
Operating	(2,495)	1,345	(763)	-	(1,913)
Pension adjustment	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Unrestricted	(2,495)	1,345	(763)	-	(1,913)
Temporarily restricted	3,969	-	-	-	3,969
Permanently restricted	<u>881</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>881</u>
Total net assets (deficit)	<u>2,355</u>	<u>1,345</u>	<u>(763)</u>	<u>-</u>	<u>2,937</u>
TOTAL LIABILITIES AND NET ASSETS (DEFICIT)	<u>\$31,505</u>	<u>\$2,664</u>	<u>\$2,632</u>	<u>\$(359)</u>	<u>\$36,442</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF OPERATIONS—BAYSTATE NOBLE HOSPITAL AND SUBSIDIARIES FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BNH	BWMC	BNVNAH	Eliminations and Reclass	Consolidated Total
OPERATING REVENUES:					
Net patient service revenue	\$60,975	\$ 10,555	\$9,968	\$ -	\$81,498
Bad debts	<u>3,066</u>	<u>504</u>	<u>437</u>	<u>-</u>	<u>4,007</u>
Net patient service revenue—net of bad debts	57,909	10,051	9,531	-	77,491
Other revenue	2,712	773	103	(136)	3,452
Net assets released from restrictions for operations	<u>544</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>544</u>
Total operating revenues	<u>61,165</u>	<u>10,824</u>	<u>9,634</u>	<u>(136)</u>	<u>81,487</u>
OPERATING EXPENSES:					
Salaries and wages	27,136	9,233	6,234	-	42,603
Supplies and expense	27,989	6,941	3,422	(136)	38,216
Depreciation and amortization	2,186	185	109	-	2,480
Interest expense	<u>323</u>	<u>17</u>	<u>22</u>	<u>-</u>	<u>362</u>
Total operating expenses	<u>57,634</u>	<u>16,376</u>	<u>9,787</u>	<u>(136)</u>	<u>83,661</u>
INCOME (LOSS) FROM OPERATIONS BEFORE OTHER INCOME	3,531	(5,552)	(153)	-	(2,174)
OTHER INCOME	<u>(267)</u>	<u>(255)</u>	<u>-</u>	<u>-</u>	<u>(522)</u>
INCOME (LOSS) FROM OPERATIONS	<u>3,264</u>	<u>(5,807)</u>	<u>(153)</u>	<u>-</u>	<u>(2,696)</u>
NONOPERATING INCOME:					
Total nonoperating income	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	3,264	(5,807)	(153)	-	(2,696)
OTHER CHANGES IN UNRESTRICTED NET ASSETS:					
Transfers for the cost of land, buildings and equipment	1,727	-	-	-	1,727
Transfers from affiliated companies—net	1,000	-	-	-	1,000
Other	<u>(5,689)</u>	<u>5,689</u>	<u>-</u>	<u>-</u>	<u>-</u>
(DECREASE) INCREASE IN UNRESTRICTED NET ASSETS	<u>\$ 302</u>	<u>\$ (118)</u>	<u>\$ (153)</u>	<u>\$ -</u>	<u>\$ 31</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF CHANGES IN NET ASSETS—BAYSTATE NOBLE HOSPITAL AND SUBSIDIARIES FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BNH	BWMC	BNVNAH	Eliminations and Reclass	Consolidated Total
UNRESTRICTED NET ASSETS:					
Excess (deficiency) of revenues over expenses	\$ 3,264	\$ (5,807)	\$ (153)	\$ -	\$ (2,696)
Transfers for the cost of land, buildings, and equipment	1,727	-	-	-	1,727
Transfers from affiliated companies—net	1,000	-	-	-	1,000
Other	(5,689)	5,689	-	-	-
(Decrease) increase in unrestricted net assets	<u>302</u>	<u>(118)</u>	<u>(153)</u>	<u>-</u>	<u>31</u>
TEMPORARILY RESTRICTED NET ASSETS:					
Net realized and unrealized loss on investments	388	-	-	-	388
Contributions	334	-	-	-	334
Net assets released from restrictions—for operations	(544)	-	-	-	(544)
Increase in temporarily restricted net assets	<u>178</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>178</u>
PERMANENTLY RESTRICTED NET ASSETS:					
Increase in permanently restricted net assets	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
INCREASE (DECREASE) IN NET ASSETS	480	(118)	(153)	-	209
NET ASSETS (DEFICIT)—Beginning of year	<u>1,875</u>	<u>1,463</u>	<u>(610)</u>	<u>-</u>	<u>2,728</u>
NET ASSETS (DEFICIT)—End of year	<u>\$ 2,355</u>	<u>\$ 1,345</u>	<u>\$ (763)</u>	<u>\$ -</u>	<u>\$ 2,937</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF ASSETS—OTHER ENTITIES AS OF SEPTEMBER 30, 2016 (In thousands)

	BH	BAS	BHF	BHIC	Other Entities Total
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	\$ 20,343	\$ 2,249	\$ 7,703	\$ 15,058	\$ 45,353
Investments	1,844	-	10,947	-	12,791
Accounts receivable, other	317	533	1,545	3,035	5,430
Inventories	-	56	-	-	56
Prepaid expenses and other current assets	28	9,255	17	54	9,354
Due from affiliated companies	111,296	5,891	402	-	117,589
Line of credit, affiliate	1,116	-	-	-	1,116
Total current assets	<u>134,944</u>	<u>17,984</u>	<u>20,614</u>	<u>18,147</u>	<u>191,689</u>
LONG-TERM ASSETS:					
Investments	1,085	-	55,059	-	56,144
Equity investment in consolidated subsidiaries	48,213	-	-	-	48,213
Equity investment in unconsolidated affiliates	76	-	-	-	76
Deferred expense and other long-term assets	18,422	-	3,146	-	21,568
Goodwill	4,132	-	-	-	4,132
Land, buildings, and equipment—net	1,984	294	10	-	2,288
	<u>73,912</u>	<u>294</u>	<u>58,215</u>	<u>-</u>	<u>132,421</u>
ASSETS WHOSE USE IS LIMITED:					
Board-designated funds:					
Cash and investments	29,752	-	3,074	-	32,826
Beneficial interest in net assets of BHF	1,872	-	-	-	1,872
Investments of captive insurance company	-	-	-	84,808	84,808
Beneficial interest in perpetual trusts	-	-	33,490	-	33,490
Beneficial interest in net assets of BHF	19,790	-	-	-	19,790
Deferred compensation investments	46,200	-	-	-	46,200
	<u>97,614</u>	<u>-</u>	<u>36,564</u>	<u>84,808</u>	<u>218,986</u>
TOTAL ASSETS	<u>\$306,470</u>	<u>\$18,278</u>	<u>\$115,393</u>	<u>\$102,955</u>	<u>\$543,096</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF LIABILITIES AND NET ASSETS—OTHER ENTITIES AS OF SEPTEMBER 30, 2016 (In thousands)

	BH	BAS	BHF	BHIC	Other Entities Total
LIABILITIES AND NET ASSETS (DEFICIT)					
CURRENT LIABILITIES:					
Accounts payable	\$ 2,475	\$ 17,428	\$ 330	\$ 390	\$ 20,623
Accrued salaries and wages	-	11,691	187	-	11,878
Deferred revenue	305	-	-	-	305
Current portion of long-term debt	740	-	-	-	740
Due to affiliated companies	1,913	989	574	-	3,476
Due to board-designated funds	1,019	-	-	-	1,019
Total current liabilities	6,452	30,108	1,091	390	38,041
LONG-TERM DEBT	53,521	-	-	-	53,521
PENSION LIABILITY	-	16,199	373	-	16,572
INSURANCE LIABILITY LOSS RESERVES	90,975	-	-	15,552	106,527
DEPOSIT LIABILITY	-	-	-	73,475	73,475
OTHER LIABILITIES	46,200	-	78	-	46,278
Total liabilities	197,148	46,307	1,542	89,417	334,414
NET ASSETS (DEFICIT):					
Unrestricted:					
Operating	83,214	7,901	6,744	13,538	111,397
Pension adjustment	(2,131)	(35,930)	(618)	-	(38,679)
Unrestricted	81,083	(28,029)	6,126	13,538	72,718
Temporarily restricted	5,234	-	57,345	-	62,579
Permanently restricted	23,005	-	50,380	-	73,385
Total net assets (deficit)	109,322	(28,029)	113,851	13,538	208,682
TOTAL LIABILITIES AND NET ASSETS	\$306,470	\$ 18,278	\$115,393	\$102,955	\$543,096

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF OPERATIONS—OTHER ENTITIES FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BH	BAS	BHF	BHIC	Other Entities Total
OPERATING REVENUES:					
Premiums	\$ -	\$ -	\$ -	\$ 3,295	\$ 3,295
Other revenue	15,422	113,199	2,487	-	131,108
Net assets released from restrictions for operations	932	579	3,353	-	4,864
Total operating revenues	16,354	113,778	5,840	3,295	139,267
OPERATING EXPENSES:					
Salaries and wages	1,168	50,632	2,657	-	54,457
Supplies and expense	14,185	61,629	3,060	2,936	81,810
Depreciation and amortization	3	105	4	-	112
Interest expense	411	-	-	-	411
Total operating expenses	15,767	112,366	5,721	2,936	136,790
INCOME (LOSS) FROM OPERATIONS BEFORE OTHER INCOME—Net	587	1,412	119	359	2,477
OTHER INCOME—Net	-	(2,855)	-	-	(2,855)
INCOME (LOSS) FROM OPERATIONS	587	(1,443)	119	359	(378)
NONOPERATING INCOME (LOSS):					
Investment income	7	-	42	-	49
Net realized gain (loss) on investments	1,267	(322)	55	393	1,393
Net unrealized gain (loss) on investments	4,751	323	49	654	5,777
Equity gain in consolidated for-profit subsidiaries	123	-	-	-	123
Equity gain in unconsolidated affiliates	81	-	-	-	81
Other	(6,915)	-	-	-	(6,915)
Total nonoperating (loss) income	(686)	1	146	1,047	508
(DEFICIENCY) EXCESS OF REVENUES OVER EXPENSES	(99)	(1,442)	265	1,406	130
OTHER CHANGES IN UNRESTRICTED NET ASSETS:					
Transfers for the cost of land, buildings, and equipment	(4,080)	12	-	-	(4,068)
Transfers from affiliated companies—net	6,868	-	332	-	7,200
Pension adjustment	-	(5,438)	(60)	-	(5,498)
Other	-	(1)	90	-	89
(DECREASE) INCREASE IN UNRESTRICTED NET ASSETS	\$ 2,689	\$ (6,869)	\$ 627	\$ 1,406	\$ (2,147)

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF CHANGES IN NET ASSETS—OTHER ENTITIES FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BH	BAS	BHF	BHIC	Other Entities Total
UNRESTRICTED NET ASSETS:					
(Deficiency) excess of revenues over expenses	\$ (99)	\$ (1,442)	\$ 265	\$ 1,406	\$ 130
Transfers for the cost of land, buildings, and equipment	(4,080)	12	-	-	(4,068)
Transfers from affiliated companies—net	6,868	-	332	-	7,200
Pension adjustment	-	(5,438)	(60)	-	(5,498)
Other	-	(1)	90	-	89
	<u>2,689</u>	<u>(6,869)</u>	<u>627</u>	<u>1,406</u>	<u>(2,147)</u>
Increase (decrease) in unrestricted net assets					
TEMPORARILY RESTRICTED NET ASSETS:					
Restricted investment income	-	-	223	-	223
Net realized and unrealized gain on investments	-	-	4,461	-	4,461
Contributions	-	-	6,134	-	6,134
Transfers for the cost of land, buildings, and equipment	-	-	(3,321)	-	(3,321)
Transfers to affiliated companies—net	-	-	(74)	-	(74)
Net assets released from restrictions—for operations	-	-	(5,087)	-	(5,087)
Other	-	-	12	-	12
	<u>-</u>	<u>-</u>	<u>2,348</u>	<u>-</u>	<u>2,348</u>
Increase in temporarily restricted net assets					
PERMANENTLY RESTRICTED NET ASSETS:					
Contributions	-	-	199	-	199
Change in fair value of perpetual trusts	-	-	1,311	-	1,311
Change in value of beneficial interest in net assets of BHF	774	-	-	-	774
	<u>774</u>	<u>-</u>	<u>1,510</u>	<u>-</u>	<u>2,284</u>
Increase in permanently restricted net assets					
INCREASE (DECREASE) IN NET ASSETS	3,463	(6,869)	4,485	1,406	2,485
NET ASSETS (DEFICIT)—Beginning of year	<u>105,859</u>	<u>(21,160)</u>	<u>109,366</u>	<u>12,132</u>	<u>206,197</u>
NET ASSETS (DEFICIT)—End of year	<u>\$109,322</u>	<u>\$(28,029)</u>	<u>\$113,851</u>	<u>\$13,538</u>	<u>\$208,682</u>

BAYSTATE HEALTH, INC. AND SUBSIDIARIES

CONSOLIDATING SCHEDULE OF CASH FLOWS—OTHER ENTITIES FOR THE YEAR ENDED SEPTEMBER 30, 2016 (In thousands)

	BH	BAS	BHF	BHIC	Other Entities Total
OPERATING ACTIVITIES:					
(Decrease) increase in net assets	\$ 3,463	\$ (6,869)	\$ 4,485	\$ 1,406	\$ 2,485
Adjustments to reconcile changes in net assets to net cash (used in) provided by operating activities:					
Depreciation and amortization	3	105	4	-	112
Pension adjustment	-	5,438	60	-	5,498
Net realized and unrealized (gain) loss on investments	(6,018)	(1)	(4,565)	(1,047)	(11,631)
Change in fair value of perpetual trusts	-	-	(1,311)	-	(1,311)
Restricted contributions	-	-	(6,332)	-	(6,332)
Changes in operating assets and liabilities:					
Accounts payable and accrued expenses	174	1,393	26	(601)	992
Pension liability	-	(3,237)	(38)	-	(3,275)
Transfers to (from) affiliated companies—net	(6,868)	-	(332)	-	(7,200)
Transfers for the cost of land, buildings, and equipment	4,080	(12)	-	-	4,068
Insurance liability loss reserves	7,250	-	-	(12,757)	(5,507)
Other	(42,055)	2,045	(1,025)	(4,064)	(45,099)
Net cash (used in) provided by operating activities	<u>(39,971)</u>	<u>(1,138)</u>	<u>(9,028)</u>	<u>(17,063)</u>	<u>(67,200)</u>
INVESTING ACTIVITIES:					
Proceeds from sale and maturities of investments	45,695	-	14,839	52,612	113,146
Purchase of investments	(38,895)	-	(15,997)	(23,767)	(78,659)
Purchase of land, buildings, and equipment, net	(1,866)	66	(14)	-	(1,814)
Transfers for the cost of land, buildings, and equipment	(4,080)	12	-	-	(4,068)
Change in beneficial interest in net assets of BHF	(944)	-	-	-	(944)
Net cash (used in) provided by investing activities	<u>(90)</u>	<u>78</u>	<u>(1,172)</u>	<u>28,845</u>	<u>27,661</u>
FINANCING ACTIVITIES:					
Proceeds from restricted contributions	-	-	6,332	-	6,332
Transfers (to) from affiliated companies—net	6,868	-	332	-	7,200
Change in line of credit, affiliate	232	-	-	-	232
Proceeds from debt issuance	37,241	-	-	-	37,241
Repayment of debt	(740)	-	-	-	(740)
Net cash provided by financing activities	<u>43,601</u>	<u>-</u>	<u>6,664</u>	<u>-</u>	<u>50,265</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	3,540	(1,060)	(3,536)	11,782	10,726
CASH AND CASH EQUIVALENTS—Beginning of year	<u>16,803</u>	<u>3,309</u>	<u>11,239</u>	<u>3,276</u>	<u>34,627</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 20,343</u>	<u>\$ 2,249</u>	<u>\$ 7,703</u>	<u>\$ 15,058</u>	<u>\$ 45,353</u>