

Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Independent Auditor's Reports and Financial Statements
December 31, 2017 and 2016



Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
December 31, 2017 and 2016

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Independent Auditor's Report

Board of Trustees
Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
Stillwater, Oklahoma

Report on the Financial Statements

We have audited the accompanying financial statements of Stillwater Medical Center Authority d/b/a Stillwater Medical Center (the Authority), a component unit of the City of Stillwater, Oklahoma, as of and for the years ended December 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Stillwater Medical Center Authority d/b/a Stillwater Medical Center as of December 31, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 18, 2018, on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

BKD, LLP

Tulsa, Oklahoma
June 18, 2018

Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Management's Discussion and Analysis
Years Ended December 31, 2017 and 2016

Introduction

This management's discussion and analysis of the financial performance of Stillwater Medical Center Authority d/b/a Stillwater Medical Center (the Authority), a component unit of the City of Stillwater, Oklahoma, provides an overview of the Authority's financial activities for the years ended December 31, 2017 and 2016. It should be read in conjunction with the accompanying financial statements of the Authority.

Financial Highlights

- Cash and cash equivalents decreased by \$15,324,635 (47%) and \$1,090,882 (3%) in 2017 and 2016, respectively.
- Investments increased by \$48,650,681 (104%) and \$3,770,426 (9%) in 2017 and 2016, respectively.
- The Authority's net position increased by \$23,851,096 (15%) and \$21,712,145 (15%) in 2017 and 2016, respectively.
- The Authority reported operating income in 2017 and 2016 of \$17,358,660 and \$17,893,232, respectively. The operating income in 2017 decreased by \$535,172 (3%) from the operating income reported in 2016. The operating income in 2016 decreased by \$1,121,995 (6%) from the operating income reported in 2015.
- Nonoperating revenues (expenses) increased by \$3,611,969 (125%) in 2017 compared to 2016 and increased by \$3,706,617 (449%) in 2016 compared to 2015.

Using This Annual Report

The Authority's financial statements consist of three statements—a balance sheet; a statement of revenues, expenses and changes in net position; and a statement of cash flows. These statements provide information about the activities of the Authority, including resources held by the Authority but restricted for specific purposes by creditors, contributors, grantors or enabling legislation. The Authority is accounted for as a business-type activity and presents its financial statements using the economic resources measurement focus and the accrual basis of accounting.

The Balance Sheet and Statement of Revenues, Expenses and Changes in Net Position

One of the most important questions asked about any organization's finances is, "Is the organization as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues, expenses and changes in net position report information about the Authority's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and deferred outflows of resources and all liabilities using the accrual basis of accounting. Using the accrual basis of accounting means that all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Authority’s net position and changes in it. The Authority’s total net position—the difference between assets and deferred outflows of resources and liabilities—is one measure of the Authority’s financial health or financial position. Over time, increases or decreases in the Authority’s net position are an indicator of whether its financial health is improving or deteriorating. Other nonfinancial factors, such as changes in the Authority’s patient base, changes in legislation and regulations, measures of the quantity and quality of services provided to its patients and local economic factors, should also be considered to assess the overall financial health of the Authority.

The Statement of Cash Flows

The statement of cash flows reports cash receipts, cash payments and net changes in cash and cash equivalents resulting from four defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for and what was the change in cash and cash equivalents during the reporting period.

The Authority’s Net Position

The Authority’s net position is the difference between its assets and deferred outflows of resources and liabilities reported in the balance sheet. The Authority’s net position increased by \$23,851,096 and \$21,712,145 in 2017 and 2016, respectively, as shown in Table 1.

Table 1: Assets, Deferred Outflows of Resources, Liabilities and Net Position

| | 2017 | 2016 | 2015 |
|---|-----------------------|-----------------------|-----------------------|
| Assets | | | |
| Cash and cash equivalents | \$ 17,600,003 | \$ 32,924,638 | \$ 34,015,520 |
| Patient accounts receivable, net | 22,086,048 | 20,281,637 | 16,930,847 |
| Investments | 95,435,328 | 46,784,647 | 43,014,221 |
| Other current assets | 9,037,570 | 7,321,319 | 5,034,990 |
| Capital assets, net | 92,410,707 | 75,854,361 | 62,598,074 |
| Other assets | 4,338,713 | 3,389,692 | 3,436,273 |
| Total assets | 240,908,369 | 186,556,294 | 165,029,925 |
| Deferred Outflows of Resources | 5,750,198 | 6,810,803 | 5,159,962 |
| Total assets and deferred outflows of resources | <u>\$ 246,658,567</u> | <u>\$ 193,367,097</u> | <u>\$ 170,189,887</u> |
| Liabilities | | | |
| Long-term debt (including current portion) | \$ 40,651,100 | \$ 12,152,772 | \$ 14,070,486 |
| Other current liabilities | 17,570,882 | 16,628,836 | 13,246,057 |
| Total liabilities | <u>58,221,982</u> | <u>28,781,608</u> | <u>27,316,543</u> |
| Net Position | | | |
| Net investment in capital assets | 79,932,955 | 62,393,006 | 48,452,215 |
| Restricted – expendable | 2,136,962 | 2,245,834 | 2,153,382 |
| Unrestricted | 106,366,668 | 99,946,649 | 92,267,747 |
| Total net position | <u>188,436,585</u> | <u>164,585,489</u> | <u>142,873,344</u> |
| Total liabilities and net position | <u>\$ 246,658,567</u> | <u>\$ 193,367,097</u> | <u>\$ 170,189,887</u> |

A significant change in the Authority's assets in 2017 is the decrease in cash and cash equivalents of \$15,324,635 (47%), the results of which are described in the Authority's cash flows disclosure on page 6. Investments, including assets limited as to use, increased by \$48,650,681 (104%) as a result of significant improvements in market returns as well as the incurrence of \$35,000,000 in debt during the year, approximately \$28,417,000 of which is restricted for capital acquisitions. Capital assets increased \$16,556,346 (22%) primarily due to ongoing construction projects and the purchase of equipment.

A significant change in the Authority's assets in 2016 is the decrease in cash and cash equivalents of \$1,090,882 (3%), the results of which are described in the Authority's cash flows disclosure on page 6. Investments increased \$3,770,426 (9%) as a result of higher performance in investment markets. Capital assets increased \$13,256,287 (21%) primarily due to ongoing construction projects and the purchase of equipment.

Operating Results and Changes in the Authority's Net Position

In 2017, the Authority's net position increased by \$23,851,096 as shown in Table 2. This increase is made up of several different components and represents an increase of \$2,138,951 (10%) compared with the increase in net position for 2016 of \$21,712,145. The Authority's change in net position increased from \$18,403,677 in 2015 to \$21,712,145 in 2016, an increase of \$3,308,468 (18%).

Table 2: Operating Results and Changes in Net Position

| | 2017 | 2016 | 2015 |
|---|----------------------|----------------------|----------------------|
| Operating Revenues | | | |
| Net patient service revenue | \$ 176,736,295 | \$ 157,825,578 | \$ 150,085,978 |
| Gain on investment in joint venture | 1,856,397 | 868,925 | 1,192,750 |
| Other | 5,765,318 | 5,073,672 | 3,602,706 |
| Total operating revenues | <u>184,358,010</u> | <u>163,768,175</u> | <u>154,881,434</u> |
| Operating Expenses | | | |
| Salaries, wages and employee benefits | 89,596,822 | 79,526,025 | 72,290,999 |
| Purchased services and professional fees | 15,901,418 | 15,839,148 | 16,132,807 |
| Supplies and other expenses | 51,501,839 | 41,653,719 | 38,831,425 |
| Depreciation and amortization | 9,999,871 | 8,856,051 | 8,610,976 |
| Total operating expenses | <u>166,999,950</u> | <u>145,874,943</u> | <u>135,866,207</u> |
| Operating Income | <u>17,358,060</u> | <u>17,893,232</u> | <u>19,015,227</u> |
| Nonoperating Revenues (Expenses) | | | |
| Noncapital grants and gifts | 139,949 | 20,909 | 136,800 |
| Gain (loss) on investments in joint ventures | 759,617 | 90,898 | (108,002) |
| Investment income (loss) | 6,408,994 | 2,991,155 | (682,142) |
| Interest expense and financing costs | (815,524) | (221,895) | (172,206) |
| Total nonoperating revenues (expenses) | <u>6,493,036</u> | <u>2,881,067</u> | <u>(825,550)</u> |
| Capital Gifts | <u>-</u> | <u>1,532,436</u> | <u>214,000</u> |
| Capital Contribution to the City of Stillwater, Oklahoma | <u>-</u> | <u>(594,590)</u> | <u>-</u> |
| Increase in Net Position | <u>\$ 23,851,096</u> | <u>\$ 21,712,145</u> | <u>\$ 18,403,677</u> |

Operating Income

The first component of the overall change in the Authority's net position is its operating income or loss—generally, the difference between net patient service revenue and other operating revenues and the expenses incurred to perform those services. In each of the past three years, the Authority has reported operating income.

Operating income for 2017 decreased by \$111,622 (1%) as compared to 2016. The primary components of the decreased operating income are:

- An increase in net patient service revenue of \$18,910,717 (12%) as a result of higher inpatient, outpatient and clinic volumes during 2017
- An increase in salaries, wages and employee benefits of \$10,070,797 (13%) as a result of pay increases in combination with the additional employees needed to cover the increase in patient volumes
- An increase in supplies and other expenses of \$9,848,120 (24%) as a result of the increased use of supplies due to corresponding higher patient volumes

Operating income for 2016 decreased by \$1,121,995 (6%) as compared to 2015. The primary components of the decreased operating income are:

- An increase in net patient service revenue of \$7,739,600 (5%) as a result of higher inpatient, outpatient and clinic volumes during 2016
- An increase in salaries, wages and employee benefits of \$7,235,026 (10%) as a result of pay increases in combination with the additional employees needed to cover the increase in patient volumes
- An increase in supplies and other expenses of \$2,822,294 (7%) as a result of the increased use of supplies due to corresponding higher patient volumes

Nonoperating Revenues and Expenses

Nonoperating revenues and expenses consist of the Authority's investments in joint ventures, investment income, noncapital grants and gifts and interest expense. In 2017, the Authority's investment income increased by \$3,417,839 compared to 2016. In 2016, the Authority's investment income increased by \$3,673,297 compared to 2015. In both years, improvements in investment returns related primarily to higher performance in investment markets.

The Authority's Cash Flows

Net cash provided by operating activities increased in 2017 by \$2,872,183 (12%) compared to 2016. The increase is attributable to increases in payments from patients offsetting increases in payments to suppliers, contractors and employees. A significant portion of the cash generated from operating activities was reinvested back into the facility through construction projects, new equipment purchases and infrastructure improvements. Additionally, the Authority reinvested some of the cash historically maintained into its investment portfolio, resulting in the overall decrease in cash and cash equivalents in 2017 as compared to 2016.

Capital Asset and Debt Administration

Capital Assets

At the end of 2017, the Authority had \$92,410,707 invested in capital assets, net of accumulated depreciation, as detailed in *Note 6* to the financial statements. In 2017, the Authority invested \$13,962,828 into ongoing construction projects and purchased new equipment and infrastructure improvements costing \$11,890,484. Of this amount, \$1,740,090 was acquired through incursion of capital lease obligations.

At the end of 2016, the Authority had \$75,854,361 invested in capital assets, net of accumulated depreciation, as detailed in *Note 6* to the financial statements. In 2016, the Authority invested \$14,044,973 into ongoing construction projects and purchased new equipment and infrastructure improvements costing \$7,329,661. Of this amount, \$1,829,653 was acquired through incursion of capital lease obligations.

Debt

At December 31, 2017 and 2016, the Authority had \$40,651,100 and \$12,152,772, respectively, in revenue bonds and capital lease obligations outstanding as discussed in *Note 9* to the financial statements. The Authority incurred \$36,740,090 and \$1,829,653 of new debt in 2017 and 2016, respectively.

Contacting the Authority's Financial Management

This financial report is designed to provide the Authority's patients, suppliers, taxpayers and creditors with a general overview of the Authority's finances and to show the Authority's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Authority's Business Administration by telephoning 405.372.1480.

Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Balance Sheets
December 31, 2017 and 2016

Assets and Deferred Outflows of Resources

| | <u>2017</u> | <u>2016</u> |
|--|-----------------------|-----------------------|
| Current Assets | | |
| Cash and cash equivalents | \$ 17,600,003 | \$ 32,924,638 |
| Short-term investments | 34,271,423 | 24,448,242 |
| Restricted cash and investments – current | 3,570,865 | 2,110,654 |
| Patient accounts receivable, net of allowance; 2017 – \$4,434,000, 2016 – \$5,308,000 | 22,086,048 | 20,281,637 |
| Supplies | 5,508,089 | 4,358,040 |
| Prepaid expenses and other | <u>3,529,481</u> | <u>2,963,279</u> |
| Total current assets | <u>86,565,909</u> | <u>87,086,490</u> |
| Noncurrent Cash and Investments | | |
| Held by trustee for debt service | 1,900,855 | 1,959,259 |
| Held by trustee for specific operating activities | 300,000 | 300,000 |
| Held by trustee for specific capital acquisition | <u>28,416,682</u> | <u>-</u> |
| | 30,617,537 | 2,259,259 |
| Less amount required to meet current obligations | <u>3,570,865</u> | <u>2,110,654</u> |
| | 27,046,672 | 148,605 |
| Other long-term investments | <u>30,546,368</u> | <u>20,077,146</u> |
| Noncurrent cash and investments, net | <u>57,593,040</u> | <u>20,225,751</u> |
| Capital Assets, Net | <u>92,410,707</u> | <u>75,854,361</u> |
| Other Assets | | |
| Investments in joint ventures | 3,034,305 | 2,189,130 |
| Other | <u>1,304,408</u> | <u>1,200,562</u> |
| Total other assets | <u>4,338,713</u> | <u>3,389,692</u> |
| Deferred Outflows of Resources | <u>5,750,198</u> | <u>6,810,803</u> |
| Total assets and deferred outflows of resources | <u>\$ 246,658,567</u> | <u>\$ 193,367,097</u> |

Liabilities and Net Position

| | <u>2017</u> | <u>2016</u> |
|---|------------------------------|------------------------------|
| Current Liabilities | | |
| Current maturities of long-term debt | \$ 9,794,271 | \$ 4,069,083 |
| Accounts payable | 7,210,444 | 5,398,426 |
| Accrued expenses | 10,325,438 | 11,230,410 |
| Estimated amounts due to third-party payers | <u>35,000</u> | <u>-</u> |
| Total current liabilities | 27,365,153 | 20,697,919 |
| | | |
| Long-Term Debt | <u>30,856,829</u> | <u>8,083,689</u> |
| Total liabilities | <u>58,221,982</u> | <u>28,781,608</u> |
| | | |
| Net Position | | |
| Net investment in capital assets | 79,932,955 | 62,393,006 |
| Restricted – expendable for | | |
| Debt service | 1,836,962 | 1,945,834 |
| Specific operating activities | 300,000 | 300,000 |
| Unrestricted | <u>106,366,668</u> | <u>99,946,649</u> |
| Total net position | <u>188,436,585</u> | <u>164,585,489</u> |
| Total liabilities and net position | <u><u>\$ 246,658,567</u></u> | <u><u>\$ 193,367,097</u></u> |

Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2017 and 2016

| | <u>2017</u> | <u>2016</u> |
|--|-----------------------|-----------------------|
| Operating Revenues | | |
| Net patient service revenue, net of provision for uncollectible accounts; 2017 – \$17,747,231, 2016 – \$15,151,917 | \$ 176,736,295 | \$ 157,825,578 |
| Gain on investment in joint venture | 1,856,397 | 868,925 |
| Other | <u>5,765,318</u> | <u>5,073,672</u> |
| Total operating revenues | <u>184,358,010</u> | <u>163,768,175</u> |
| Operating Expenses | | |
| Salaries and wages | 71,473,094 | 62,131,059 |
| Employee benefits | 18,123,728 | 17,394,966 |
| Purchased services and professional fees | 15,901,418 | 15,839,148 |
| Supplies and other expenses | 50,805,034 | 41,641,225 |
| Depreciation and amortization | 9,999,871 | 8,856,051 |
| Loss on sale of capital assets | <u>696,805</u> | <u>12,494</u> |
| Total operating expenses | <u>166,999,950</u> | <u>145,874,943</u> |
| Operating Income | <u>17,358,060</u> | <u>17,893,232</u> |
| Nonoperating Revenues (Expenses) | | |
| Noncapital grants and gifts | 139,949 | 20,909 |
| Gain on investments in joint ventures | 759,617 | 90,898 |
| Investment income | 6,408,994 | 2,991,155 |
| Interest expense and financing costs | <u>(815,524)</u> | <u>(221,895)</u> |
| Total nonoperating revenues (expenses) | <u>6,493,036</u> | <u>2,881,067</u> |
| Excess of Revenues over Expenses Before Capital Gifts and Contribution | 23,851,096 | 20,774,299 |
| Capital Gifts | - | 1,532,436 |
| Capital Contribution to the City of Stillwater, Oklahoma | <u>-</u> | <u>(594,590)</u> |
| Increase in Net Position | 23,851,096 | 21,712,145 |
| Net Position, Beginning of Year | <u>164,585,489</u> | <u>142,873,344</u> |
| Net Position, End of Year | <u>\$ 188,436,585</u> | <u>\$ 164,585,489</u> |

Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Statements of Cash Flows
Years Ended December 31, 2017 and 2016

| | <u>2017</u> | <u>2016</u> |
|--|---------------------|---------------------|
| Operating Activities | | |
| Receipts from and on behalf of patients | \$ 174,966,884 | \$ 154,794,788 |
| Payments to suppliers and contractors | (65,506,887) | (59,760,761) |
| Payments to employees | (90,556,147) | (77,868,176) |
| Other receipts and payments, net | <u>7,366,931</u> | <u>6,232,747</u> |
| Net cash provided by operating activities | <u>26,270,781</u> | <u>23,398,598</u> |
| Noncapital Financing Activities | | |
| Noncapital grants and gifts | <u>139,949</u> | <u>20,909</u> |
| Net cash provided by noncapital financing activities | <u>139,949</u> | <u>20,909</u> |
| Capital and Related Financing Activities | | |
| Capital gifts | - | 1,532,436 |
| Proceeds from issuance of long-term debt | 35,000,000 | - |
| Proceeds from disposal of capital assets | 117,916 | 4,375 |
| Principal paid on long-term debt | (8,241,762) | (3,747,367) |
| Interest paid on long-term debt | (765,056) | (226,341) |
| Purchase of capital assets | <u>(25,178,471)</u> | <u>(16,935,771)</u> |
| Net cash provided by (used in) capital and related financing activities | <u>932,627</u> | <u>(19,372,668)</u> |
| Investing Activities | | |
| Purchases of restricted assets whose use is limited under bond agreements | (8,059,232) | (3,101,472) |
| Proceeds from disposition of restricted assets whose use is limited under bond agreements | 8,117,636 | 3,013,466 |
| Purchases of restricted assets whose use is limited for capital acquisitions | (75,554,720) | - |
| Proceeds from disposition of restricted assets whose use is limited for capital acquisitions | 47,138,038 | - |
| Purchases of investments | (56,853,250) | (9,431,210) |
| Proceeds from disposition of investments | 35,028,620 | 7,145,617 |
| Advances to and investments in joint ventures | 19,297 | 17,550 |
| Acquisition of cancer center | - | (4,376,000) |
| Acquisition of JKBH | (445,602) | - |
| Investment income received | <u>7,941,221</u> | <u>1,594,328</u> |
| Net cash used in investing activities | <u>(42,667,992)</u> | <u>(5,137,721)</u> |

See Notes to Financial Statements

| | <u>2017</u> | <u>2016</u> |
|--|-----------------------------|-----------------------------|
| Decrease in Cash and Cash Equivalents | \$ (15,324,635) | \$ (1,090,882) |
| Cash and Cash Equivalents, Beginning of Year | <u>32,924,638</u> | <u>34,015,520</u> |
| Cash and Cash Equivalents, End of Year | <u><u>\$ 17,600,003</u></u> | <u><u>\$ 32,924,638</u></u> |
| Reconciliation of Operating Income to Net Cash Provided by Operating Activities | | |
| Operating income | \$ 17,358,060 | \$ 17,893,232 |
| Depreciation and amortization | 9,999,871 | 8,856,051 |
| Accrued self-insurance costs | (650,584) | (263,602) |
| Loss on sale of capital assets | 696,805 | 12,494 |
| Provision for uncollectible accounts | 17,747,231 | 15,151,917 |
| Changes in operating assets and liabilities | | |
| Patient accounts receivable | (19,551,642) | (18,502,707) |
| Supplies, prepaid expenses and other assets | (1,820,097) | (2,776,554) |
| Estimated amounts due to/from third-party payers | 35,000 | 320,000 |
| Change in investments in joint ventures | (254,784) | 290,150 |
| Accounts payable and accrued expenses | <u>2,710,921</u> | <u>2,417,617</u> |
| Net cash provided by operating activities | <u><u>\$ 26,270,781</u></u> | <u><u>\$ 23,398,598</u></u> |
| Noncash Investing, Capital and Financing Activities | | |
| Capital asset purchases in accounts payable | \$ 243,334 | \$ 1,308,583 |
| Capital lease obligations incurred for equipment | \$ 1,740,090 | \$ 1,829,653 |
| Capital contribution to the City of Stillwater, Oklahoma (see Note 6) | \$ - | \$ 594,590 |

Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Notes to Financial Statements
December 31, 2017 and 2016

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

Nature of Operations and Reporting Entity

Stillwater Medical Center Authority d/b/a Stillwater Medical Center (the Authority) is a public trust and an agency of the state of Oklahoma. The Authority is a component unit of the City of Stillwater, Oklahoma (the City) as the Board of Commissioners of the City appoints the majority of the members of the Board of Trustees of the Authority. The Authority operates, as its sole activity, Stillwater Medical Center under the terms of a trust indenture originally dated December 14, 1971.

The Authority primarily earns revenues by providing inpatient, outpatient and emergency care services to patients in Stillwater, Oklahoma, and surrounding communities. The Authority also operates physician clinics, a rehabilitation unit and provides home health and hospice services in the same geographic area.

Basis of Accounting and Presentation

The accompanying financial statements of the Authority have been prepared on the accrual basis of accounting using the economic resources measurement focus. Revenues, expenses, gains, losses, assets and deferred outflows of resources and liabilities from exchange and exchange-like transactions are recognized when the exchange transaction takes place, while those from government-mandated nonexchange transactions (principally, federal and state grants and county appropriations) are recognized when all applicable eligibility requirements are met. Operating revenues and expenses include exchange transactions and program-specific, government-mandated nonexchange transactions. Noncapital grants and gifts that are not program-specific, investment income and interest on capital assets-related debt are included in nonoperating revenues and expenses. The Authority first applies restricted net position when an expense or outlay is incurred for purposes for which both restricted and unrestricted net position are available.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and deferred outflows of resources and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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Cash and Cash Equivalents

The Authority considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2017 and 2016, cash equivalents consisted primarily of money market accounts with brokers.

Included in restricted cash and investments – current on the accompanying balance sheets are money market mutual funds with brokers the Authority does not consider cash equivalents.

Risk Management

The Authority is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than those related to workers' compensation and employee health claims. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

The Authority is self-insured for a portion of its exposure to the risk of loss from workers' compensation and employee health claims. Annual estimated provisions are accrued for the self-insured portion of these claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Investments and Investment Income

Investments in U.S. Treasury, agency and instrumentality obligations with a remaining maturity of one year or less at the time of acquisition and non-negotiable certificates of deposit are carried at amortized cost. The investments in joint ventures are reported on the cost and equity methods of accounting (see *Note 5* for additional information on joint ventures). All other investments are carried at fair value. Fair value is determined using quoted market prices.

Investment income includes dividend and interest income, realized gains and losses on investments carried at other than fair value and the net change for the year in the fair value of investments carried at fair value.

Patient Accounts Receivable

The Authority reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Authority provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information and existing economic conditions.

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Supplies

Supply inventories are stated at the lower of cost, determined using the first-in, first-out method, or market.

Capital Assets

Capital assets are recorded at cost at the date of acquisition or acquisition value at the date of donation if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives. The following estimated useful lives are being used by the Authority:

| | |
|--------------------------------------|-------------|
| Land improvements | 8–20 years |
| Buildings and leasehold improvements | 10–40 years |
| Equipment | 3–20 years |

Deferred Outflows of Resources

The Authority reports the consumption of net position that is applicable to a future period as deferred outflows of resources in a separate section of its balance sheets.

Compensated Absences

Authority policies permit most employees to accumulate paid time off benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as benefits are earned whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments, such as Social Security and Medicare taxes, computed using rates in effect at that date.

Net Position

Net position of the Authority is classified in three components. Net investment in capital assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Restricted expendable net position is made up of noncapital assets that must be used for a particular purpose, as specified by creditors, grantors or donors external to the Authority, including amounts deposited with trustees as required by bond indentures, reduced by the outstanding balances of any related borrowings. Unrestricted net position is the remaining net position that does not meet the definition of net investment in capital assets or restricted net position.

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Net Patient Service Revenue

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

Charity Care

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

Income Taxes

As an essential government function of the City, the Authority is generally exempt from federal and state income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law. However, the Authority is subject to federal income tax on any unrelated business taxable income.

Supplemental Hospital Offset Payment Program

On January 17, 2012, CMS approved the State of Oklahoma’s Supplemental Hospital Offset Payment Program (SHOPP). The SHOPP is currently scheduled to sunset on December 31, 2020. The SHOPP is designed to assess Oklahoma hospitals a supplemental hospital offset fee which will be placed in pools after receiving federal matching funds. The total fees and matching funds will then be allocated to hospitals as directed by legislation.

During the years ended December 31, the Authority had the following activity related to the SHOPP:

| | 2017 | 2016 |
|----------------------------|--------------|--------------|
| SHOPP funds received | \$ 6,852,000 | \$ 4,668,000 |
| SHOPP assessment fees paid | 4,552,000 | 3,793,000 |
| Net benefit under SHOPP | \$ 2,300,000 | \$ 875,000 |

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The annual amounts to be received and paid by the Authority over the term of the SHOPP are subject to change annually based on various factors involved in determining the amount of federal matching funds. Based on the current information available, the annual net benefit to the Authority over the term of the SHOPP is expected to be consistent with 2016. SHOPP revenue is recorded as part of net patient service revenue and SHOPP assessment fees are recorded as part of other expenses on the accompanying statements of revenues, expenses and changes in net position.

Reclassifications

Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 financial statement presentation. These reclassifications had no effect on the changes in financial position.

Note 2: Net Patient Service Revenue

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

- **Medicare** – Substantially all services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The Authority is reimbursed for certain services at tentative rates with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare administrative contractor. The Medicare administrative contractor has audited the Authority's cost reports through December 31, 2014.
- **Medicaid** – The Authority has also been reimbursed for services rendered to patients covered by the state Medicaid program at prospectively determined rates per discharge and fee schedules with no retroactive adjustment. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Approximately 72% and 61% of net patient service revenue is from participation in the Medicare and state-sponsored Medicaid programs for the years ended December 31, 2017 and 2016, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

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

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Note 3: Deposits, Investments and Investment Income

Deposits

Custodial credit risk is the risk that in the event of a bank failure a government's deposits may not be returned to it. The Authority's deposit policy for custodial credit risk requires compliance with the provisions of state law, which requires the collateralization of all deposits with federal depository insurance and other acceptable collateral in specific amounts.

At December 31, 2017 and 2016, approximately \$2,127,000 and \$5,942,000 of the Authority's bank balances of \$24,444,971 and \$7,388,057, respectively, were uninsured and uncollateralized.

Investments

The Authority may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in corporate bonds and equity securities.

At December 31, the Authority had the following investments and maturities:

| Type | Fair Value | 2017 | | | |
|---------------------------------------|----------------------|----------------------|----------------------|---------------------|-------------------|
| | | Maturities in Years | | | |
| | | Less than 1 | 1-5 | 6-10 | More than 10 |
| U.S. Treasury obligations | \$ 2,040,361 | \$ 2,040,361 | \$ - | \$ - | \$ - |
| U.S. agencies obligations | 135,918 | - | - | - | 135,918 |
| Money market mutual funds | 22,982,139 | 22,982,139 | - | - | - |
| Mutual funds – fixed income | 30,410,451 | - | 21,290,286 | 9,120,165 | - |
| Mutual funds – domestic equities | 25,314,853 | 25,314,853 | - | - | - |
| Mutual funds – international equities | 8,576,199 | 8,576,199 | - | - | - |
| Total investments | <u>\$ 89,459,921</u> | <u>\$ 58,913,552</u> | <u>\$ 21,290,286</u> | <u>\$ 9,120,165</u> | <u>\$ 135,918</u> |

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| Type | 2016 | | | | |
|---------------------------------------|----------------------|----------------------|---------------------|---------------------|---------------------|
| | Fair Value | Maturities in Years | | | |
| | | Less than 1 | 1-5 | 6-10 | More than 10 |
| U.S. Treasury obligations | \$ 2,654,504 | \$ - | \$ 655,919 | \$ 663,942 | \$ 1,334,643 |
| U.S. agencies obligations | 4,455,373 | - | 412,063 | 972,437 | 3,070,873 |
| Corporate bonds | 5,091,891 | 101,540 | 2,283,818 | 819,588 | 1,886,945 |
| Money market mutual funds | 27,508,328 | 27,508,328 | - | - | - |
| Mutual funds – fixed income | 7,918,548 | - | 3,321,766 | 4,596,782 | - |
| Mutual funds – domestic equities | 7,665,244 | 7,665,244 | - | - | - |
| Mutual funds – international equities | 1,926,940 | 1,926,940 | - | - | - |
| | <u>57,220,828</u> | <u>\$ 37,202,052</u> | <u>\$ 6,673,566</u> | <u>\$ 7,052,749</u> | <u>\$ 6,292,461</u> |
| Corporate stocks | 14,332,792 | | | | |
| Accrued investment income | <u>104,826</u> | | | | |
| Total investments | <u>\$ 71,658,446</u> | | | | |

Interest Rate Risk – As a means of limiting its exposure to fair value losses arising from rising interest rates, the Authority’s investment policy limits its fixed income investment portfolio to an average overall portfolio duration no greater than 7.5 years. The money market mutual funds are presented as an investment with a maturity of less than one year because the average maturity of the funds is less than one year.

Credit Risk – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. It is the Authority’s policy to limit its domestic fixed income investments to a credit rating of no less than investment grade and an overall weighted-average rating of A by Standard & Poor’s (S & P), Moody’s or Fitch. At December 31, the Authority’s investments not directly guaranteed by the U.S. government were rated as follows:

| Investments | 2017 | |
|---------------------------|-----------|-----------|
| | Moody’s | S & P |
| U.S. agencies obligations | Aaa | AA+ |
| Money market mutual funds | Aaa | AAAm |
| Mutual funds | Not Rated | Not Rated |

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| Investments | 2016 | |
|---------------------------|------------------|------------------|
| | Moody's | S & P |
| U.S. agencies obligations | Aaa | AA+ |
| Corporate bonds | Not rated to Aaa | Not rated to AAA |
| Money market mutual funds | Aaa | AAAm |
| Mutual funds | Not Rated | Not Rated |

Custodial Credit Risk – For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty the Authority will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Authority’s investment policy does not address custodial credit risk.

Concentration of Credit Risk – The Authority limits exposure of the portfolio to any one issuer, other than the U.S. government or its agencies, to 10% of the market value of the fixed income portfolio and to 5% of the market value of the equity portfolio.

At December 31, 2017 and 2016, no investments exceeded 5% of the total fair value of all investments.

Summary of Carrying Values

The carrying values of deposits and investments shown above are included in the accompanying balance sheets as follows:

| | 2017 | 2016 |
|--|-----------------------|----------------------|
| Carrying value | | |
| Deposits | \$ 23,575,410 | \$ 8,050,839 |
| Investments | 89,459,921 | 71,658,446 |
| | <u>\$ 113,035,331</u> | <u>\$ 79,709,285</u> |
| Included in the following balance sheet captions | | |
| Cash and cash equivalents | \$ 17,600,003 | \$ 32,924,638 |
| Short-term investments | 34,271,423 | 24,448,242 |
| Restricted cash and investments – current | 3,570,865 | 2,110,654 |
| Noncurrent cash and investments | 57,593,040 | 20,225,751 |
| | <u>\$ 113,035,331</u> | <u>\$ 79,709,285</u> |

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Investment Income

Investment income for the years ended December 31 consisted of:

| | <u>2017</u> | <u>2016</u> |
|---|---------------------|---------------------|
| Interest, dividends and realized gain on sales of investments | \$ 7,941,221 | \$ 1,594,328 |
| Net increase (decrease) in fair value of investments | (1,532,227) | 1,396,827 |
| | <u>\$ 6,408,994</u> | <u>\$ 2,991,155</u> |

Note 4: Patient Accounts Receivable

The Authority grants credit without collateral to its patients, many of whom are area residents and are insured under third-party payer agreements. Patient accounts receivable at December 31 consisted of:

| | <u>2017</u> | <u>2016</u> |
|---|----------------------|----------------------|
| Medicare | \$ 4,944,579 | \$ 4,402,868 |
| Medicaid | 1,029,868 | 931,959 |
| Other third-party payers | 12,517,977 | 12,104,827 |
| Patients | 8,027,624 | 8,149,983 |
| | <u>26,520,048</u> | <u>25,589,637</u> |
| Less allowance for uncollectible accounts | 4,434,000 | 5,308,000 |
| | <u>\$ 22,086,048</u> | <u>\$ 20,281,637</u> |

Note 5: Investments in Joint Ventures

The investments in joint ventures relate to an approximate 63% ownership in Stillwater Medical Imaging, LLC (SMI), an approximate 9% ownership in Fresenius Medical Care – Stillwater, LLC (Fresenius), an approximate 1% ownership interest in Upper Midwest Consolidated Services Center, LLC (UMCSC), and an approximate 10% ownership interest in LifeCare Health Services, LLC (LifeCare). The Authority had an approximate 10% ownership in Heartland Healthcare Reciprocal Risk Retention Group (Heartland) through December 31, 2016. Effective January 1, 2017, Heartland merged with another entity to form Tecumseh Health Reciprocal Risk Retention Group (Tecumseh); the Authority has an approximate 4% ownership in Tecumseh at December 31, 2017. In addition, the Authority had a 50% ownership in Bristol Hospice and Homecare – Stillwater, LLC (BHHC). During 2017, the Authority acquired the remaining 50% ownership interest in BHHC.

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The financial position and results of operations from the unaudited financial statements of Tecumseh/Heartland, SMI, LifeCare and BHHC for the fiscal years ended December 31 are summarized below:

| | 2017 | | |
|--|----------------------|---------------------|---------------------|
| | Tecumseh | SMI | LifeCare |
| Current assets | \$ 53,083,540 | \$ 3,097,882 | \$ 6,529,137 |
| Property and other long-term assets, net | - | 196,739 | 479,599 |
| Total assets | <u>\$ 53,083,540</u> | <u>\$ 3,294,621</u> | <u>\$ 7,008,736</u> |
| Total liabilities | \$ 20,235,243 | \$ 239,121 | \$ 284,484 |
| Partners' equity | 32,848,297 | 3,055,500 | 6,724,252 |
| Total liabilities and partners' equity | <u>\$ 53,083,540</u> | <u>\$ 3,294,621</u> | <u>\$ 7,008,736</u> |
| Revenues | <u>\$ 9,259,343</u> | <u>\$ 3,955,588</u> | <u>\$ 2,148,195</u> |
| Excess of revenues over expenses | <u>\$ 5,328,231</u> | <u>\$ 2,934,088</u> | <u>\$ 392,928</u> |
| | | 2016 | |
| | Heartland | SMI | BHHC |
| Current assets | \$ 12,952,360 | \$ 1,889,184 | \$ 492,486 |
| Property and other long-term assets, net | - | 329,109 | 12,009 |
| Total assets | <u>\$ 12,952,360</u> | <u>\$ 2,218,293</u> | <u>\$ 504,495</u> |
| Total liabilities | \$ 4,772,360 | \$ 320,530 | \$ 529,636 |
| Partners' equity (deficit) | 8,180,000 | 1,897,763 | (25,141) |
| Total liabilities and partners' equity (deficit) | <u>\$ 12,952,360</u> | <u>\$ 2,218,293</u> | <u>\$ 504,495</u> |
| Revenues | <u>\$ 2,994,822</u> | <u>\$ 2,550,057</u> | <u>\$ 2,002,172</u> |
| Excess (deficiency) of revenues over expenses | <u>\$ 1,201,959</u> | <u>\$ 1,396,031</u> | <u>\$ (76,961)</u> |

Complete financial statements of the joint venture entities may be obtained by contacting the Authority's management.

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The Authority purchases its professional liability (medical malpractice) and general liability insurance coverage from Tecumseh (see *Note 7*). For the years ended December 31, 2017 and 2016, the Authority paid approximately \$276,000 and \$255,000 to Tecumseh and Heartland, respectively, for the coverage. The Authority's investment in Tecumseh and Heartland was \$1,110,642 and \$973,923 at December 31, 2017 and 2016, respectively.

SMI owns and operates MRI, CT and other imaging equipment. The Authority utilizes SMI to provide imaging services for its patients. The equipment is located within Stillwater Medical Center, and the Authority manages the operations and provides all staffing and supplies for SMI. The Authority performs all billing and collection services on behalf of SMI in exchange for a percentage of cash collections. SMI functions as if it were a department within the Authority. As a result, management has elected to record the gain on investment in SMI within operating revenues. Included in accrued expenses of the Authority is approximately \$705,000 and \$593,000 due to the joint venture at December 31, 2017 and 2016, respectively. During the years ended December 31, 2017 and 2016, the Authority earned approximately \$1,202,000 and \$1,019,000, respectively, in fees from billing and collections services, which are recorded in other operating revenues. The Authority's investment in SMI was \$983,287 and \$728,503 at December 31, 2017 and 2016, respectively.

LifeCare is a joint venture between certain hospitals in Oklahoma organized to collaborate and share expenses and expertise to expand or enhance health care services in the communities served by each participating hospital in furtherance of their independent missions. The Authority's investment in LifeCare was \$603,601 as of December 31, 2017.

BHHC was formed to own and operate hospice and home care subsidiary companies. BHHC is the sole member of Judith Karman Bristol Hospice, L.L.C. (JKBH). JKBH provides hospice services to residents of Stillwater and the surrounding area. During 2015, the Authority invested \$325,000 in capital contributions to BHHC. The Authority's investment in BHHC was \$149,929 at December 31, 2016. During 2017, the Authority purchased the remaining shares of JKBH for \$600,428.

Fresenius provides dialysis services to residents of Stillwater and the surrounding area. The Authority's investment in Fresenius was \$261,775 at December 31, 2017 and 2016.

UMCSC is a health care supply purchasing and management organization. The Authority's investment in UMCSC was \$75,000 at December 31, 2017 and 2016.

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During 2016, the Authority constructed and transferred to the City assets totaling \$594,590, which is included in the accompanying statements of revenues, expenses and changes in net position as capital contributed to the City of Stillwater, Oklahoma.

Note 7: Medical Malpractice Claims

The Authority purchases medical malpractice insurance under a claims-made policy on a fixed premium basis. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. Based upon the Authority's claims experience, an accrual of approximately \$58,000 has been made as of December 31, 2017 and 2016. It is reasonably possible that this estimate could change materially in the near term.

The Authority is a subscriber (member) of Tecumseh, an entity approved by the state of Vermont to provide hospital professional and general liability coverage to its subscribers. Tecumseh was formed in order to stabilize the cost and availability of hospital professional and general liability insurance by taking advantage of the self-funding capabilities of a homogenous group of health care providers. Tecumseh members are provided hospital professional and general liability insurance under claims-made policies on a fixed premium basis. See *Note 5* for additional information about Tecumseh.

Note 8: Self-Insured Claims

Substantially all of the Authority's employees and their dependents are eligible to participate in the Authority's employee health insurance plan. The Authority is self-insured for health claims of participating employees and dependents up to an annual aggregate amount of approximately \$175,000 and any amounts over \$1,000,000. Commercial stop-loss insurance coverage is purchased for claims in excess of the aggregate annual amount of \$175,000 up to \$1,000,000.

The Authority is self-insured for risks related to workers' compensation claims up to \$500,000 per occurrence with an annual liability limit of \$1,000,000 in the aggregate. In connection with the self-insured workers' compensation policy, the Authority had a \$300,000 certificate of deposit held in escrow at a local bank during the years ended December 31, 2017 and 2016. No draws were made on the certificate of deposit held in escrow through 2017.

A provision is accrued for self-insured employee health claims and workers' compensation claims, including both claims reported and claims incurred but not yet reported. The accruals are estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Authority's estimates will change by a material amount in the near term.

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Activity in the Authority's accrued employee health and workers' compensation claims liability during 2017 and 2016 is summarized as follows:

| | December 31, 2017 | |
|--|--------------------------|------------------------------|
| | Employee Health | Workers' Compensation |
| Balance, beginning of year | \$ 1,862,654 | \$ 151,395 |
| Current year claims incurred and changes in estimates for claims incurred in prior years | 8,816,237 | 32,504 |
| Claims and expenses paid | <u>(9,378,396)</u> | <u>(120,929)</u> |
| Balance, end of year | <u>\$ 1,300,495</u> | <u>\$ 62,970</u> |
| | December 31, 2016 | |
| | Employee Health | Workers' Compensation |
| Balance, beginning of year | \$ 2,100,000 | \$ 177,651 |
| Current year claims incurred and changes in estimates for claims incurred in prior years | 9,199,989 | 107,767 |
| Claims and expenses paid | <u>(9,437,335)</u> | <u>(134,023)</u> |
| Balance, end of year | <u>\$ 1,862,654</u> | <u>\$ 151,395</u> |

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Note 9: Long-Term Debt

The following is a summary of long-term obligation transactions for the Authority for the years ended December 31:

| | 2017 | | | | |
|-------------------------------------|--------------------------|----------------------|---------------------|-----------------------|------------------------|
| | Beginning Balance | Additions | Deductions | Ending Balance | Current Portion |
| Revenue bonds payable – Series 2014 | \$ 9,480,000 | \$ - | \$ 3,125,000 | \$ 6,355,000 | \$ 3,150,000 |
| Revenue bond payable – Series 2017 | - | 35,000,000 | 4,166,666 | 30,833,334 | 5,000,000 |
| Capital lease obligations | 2,672,772 | 1,740,090 | 950,096 | 3,462,766 | 1,644,271 |
| Total long-term debt | <u>\$ 12,152,772</u> | <u>\$ 36,740,090</u> | <u>\$ 8,241,762</u> | <u>\$ 40,651,100</u> | <u>\$ 9,794,271</u> |
| | 2016 | | | | |
| | Beginning Balance | Additions | Deductions | Ending Balance | Current Portion |
| Revenue bonds payable – Series 2014 | \$ 12,550,000 | \$ - | \$ 3,070,000 | \$ 9,480,000 | \$ 3,125,000 |
| Capital lease obligations | 1,520,486 | 1,829,653 | 677,367 | 2,672,772 | 944,083 |
| Total long-term debt | <u>\$ 14,070,486</u> | <u>\$ 1,829,653</u> | <u>\$ 3,747,367</u> | <u>\$ 12,152,772</u> | <u>\$ 4,069,083</u> |

Revenue Bonds Payable – Series 2014

The Series 2014 revenue bonds payable consist of Hospital Revenue Bonds (the 2014 Bonds) in the original amount of \$15,570,000 dated March 28, 2014, which bear interest at 1.69%. The 2014 Bonds are payable in annual installments through May 15, 2019, with interest payable semiannually. The 2014 Bonds outstanding may be redeemed at the Authority’s option. The redemption price is 101% and decreases to 100% on or after May 16, 2017. The 2014 Bonds are secured by the gross revenues of the Authority, certain property and the trustee-held assets restricted under the bond indenture agreement.

The indenture agreements require that certain funds be established with the trustee. Accordingly, these funds are included as assets held by trustee for debt service in the accompanying balance sheets. The indenture agreements also require the Authority to comply with certain restrictive covenants, including minimum insurance coverage, maintaining a historical debt service coverage ratio of at least 1.2 to 1.0 and restrictions on incurrence of additional debt.

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Revenue Bond Payable – Series 2017

The Series 2017 revenue bond payable consists of a Hospital Revenue Bond (the 2017 Bond) in the original amount of \$35,000,000 dated January 26, 2017, which bears interest annually at 2.16%. The 2017 Bond is payable in monthly principal and interest installments through February 15, 2024. The 2017 Bond outstanding may be redeemed at the Authority’s option at a premium. The 2017 Bond is secured by the gross revenues of the Authority and is to be used for capital asset acquisitions.

The indenture agreements require that certain funds be established with the trustee. Accordingly, these funds are included as assets held by trustee for debt service and capital acquisition in the accompanying balance sheets. The indenture agreements also require the Authority to comply with certain restrictive covenants, including minimum insurance coverage, maintaining a historical debt service coverage ratio of at least 1.2 to 1.0, maintaining at least 75 days cash on hand and restrictions on incurrence of additional debt.

The debt service requirements for the Series 2014 and Series 2017 Revenue Bonds are as follows:

| Year Ending December 31, | Total to be Paid | Principal | Interest |
|--------------------------|----------------------|----------------------|---------------------|
| 2018 | \$ 8,848,182 | \$ 8,150,000 | \$ 698,182 |
| 2019 | 8,740,733 | 8,205,000 | 535,733 |
| 2020 | 5,400,500 | 5,000,000 | 400,500 |
| 2021 | 5,292,500 | 5,000,000 | 292,500 |
| 2022–2024 | <u>11,096,584</u> | <u>10,833,334</u> | <u>263,250</u> |
| | <u>\$ 39,378,499</u> | <u>\$ 37,188,334</u> | <u>\$ 2,190,165</u> |

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Capital Lease Obligations

The Authority is obligated under leases for equipment that are accounted for as capital leases. Assets under capital leases at December 31, 2017 and 2016, totaled \$5,584,459 and \$3,858,067, respectively, net of accumulated depreciation of \$2,095,772 and \$1,212,545, respectively. The following is a schedule by year of future minimum lease payments under capital leases, including interest rates between 1.69% and 5.00%, together with the present value of the future minimum lease payments:

| Year Ending December 31, | |
|--|--------------|
| 2018 | \$ 1,668,286 |
| 2019 | 1,101,135 |
| 2020 | 730,081 |
| Total minimum lease payments | 3,499,502 |
| Less amount representing interest | 36,736 |
| Present value of future minimum lease payments | \$ 3,462,766 |

Note 10: Charity Care and Uncompensated Care

In support of its mission, the Authority voluntarily provides free care to patients who lack financial resources and are deemed to be medically indigent. Because the Authority does not pursue collection of amounts determined to qualify as charity care, they are not reported in net patient service revenue. In addition, the Authority provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts which are less than established charges for the services provided to the recipients and many times the payments are less than the cost of rendering the services provided.

Uncompensated costs relating to these services are approximately as follows:

| | 2017 | 2016 |
|--|--------------|--------------|
| Charity allowances | \$ 2,768,000 | \$ 2,110,000 |
| State Medicaid and other public aid programs | 5,426,000 | 1,737,000 |
| | \$ 8,194,000 | \$ 3,847,000 |

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The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross uncompensated charges. In addition to uncompensated costs, the Authority also commits significant time and resources to endeavors and critical services which meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include health screenings and assessments, prenatal education and care, community educational services and various support groups.

Note 11: Operating Leases

Noncancellable operating leases for equipment and building space expire in various years through December 2027. These leases generally contain renewal options for periods ranging from five to ten years and require the Authority to pay all executory costs (property taxes, maintenance and insurance).

Future minimum lease payments at December 31, 2017, were approximately:

| | |
|-----------|----------------------------|
| 2018 | \$ 786,000 |
| 2019 | 788,000 |
| 2020 | 746,000 |
| 2021 | 759,000 |
| 2022 | 773,000 |
| 2023–2027 | <u>1,947,000</u> |
| | <u><u>\$ 5,799,000</u></u> |

Rental expense for the years ended December 31, 2017 and 2016, was approximately \$1,421,000 and \$1,537,000, respectively.

Note 12: Pension Plan

The Authority contributes to a defined contribution pension plan covering substantially all employees. Pension expense is recorded for the amount of the Authority's required contributions, determined in accordance with the terms of the plan. The plan is administered by the Authority's Board of Trustees. The plan provides retirement and death benefits to plan members and their beneficiaries. Benefit provisions are contained in the plan document and were established and can be amended by action of the Authority's governing body. Contribution rates for plan members and the Authority expressed as a percentage of covered payroll were 3% and 6% for 2017 and 2016, respectively. Contributions actually made by plan members and the Authority aggregated approximately \$1,546,000 and \$2,958,000, respectively, during 2017 and \$1,341,000 and \$2,500,000, respectively, during 2016.

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Note 13: Government Acquisitions

The Authority has acquired multiple service lines since 2009 for which the consideration provided exceeded the net position acquired as of the date of acquisition. These service lines were acquired as they were considered strategic additions to the services already provided by the Authority.

Bristol Hospice and Homecare – Stillwater, LLC Acquisition

In May 2017, the Authority acquired the remaining 50% equity in BHHC for a total purchase price of \$445,602, which was paid for in cash. No contingent consideration was included in the transaction.

The Authority recorded deferred outflows of resources of \$453,136 as a result of the transaction, which the Authority has elected to amortize over a period of five years. Amortization expense is estimated to be approximately \$91,000 each year through 2021 and approximately \$45,000 in 2022.

Amortization of Deferred Outflows of Resources

Other acquisitions resulting in deferred outflows of resources include:

- The 2009 acquisition of Stillwater Surgery Center, L.L.C., which is being amortized over 15 years. Amortization expense is approximately \$388,000 annually through 2024
- The 2012 acquisition of OrthoOklahoma P.C., which was being amortized over five years. Amortization expense was approximately \$632,000 annually through 2017
- The 2014 acquisition of Women First, LLC, which was amortized over three years. Amortization expense was estimated to be approximately \$256,000 annually through 2016 and approximately \$128,000 in 2017
- The 2016 acquisition of assets and the oncology practice of Oklahoma Oncology and Hematology, Inc., and Oklahoma Cancer Specialists, which is being amortized over 10 years. Amortization expense is estimated to be approximately \$300,000 annually through 2026

The carrying basis and accumulated amortization of recognized deferred outflows of resources related to government acquisitions at December 31 were:

| | 2017 | 2016 |
|--------------------------------|---------------|---------------|
| Deferred outflows of resources | \$ 13,204,573 | \$ 12,751,437 |
| Accumulated amortization | 7,454,375 | 5,940,634 |
| | \$ 5,750,198 | \$ 6,810,803 |

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The changes in the carrying amount of deferred outflows of resources for the years ended December 31 were:

| | 2017 | 2016 |
|------------------------------|---------------|---------------|
| Balance as of January 1 | \$ 12,751,437 | \$ 9,751,437 |
| Acquisitions during the year | 453,136 | 3,000,000 |
| Balance as of December 31 | \$ 13,204,573 | \$ 12,751,437 |

Note 14: Contingencies

Litigation

In the normal course of business, the Authority is, from time to time, subject to allegations that may or do result in litigation. Some of these allegations are in areas not covered by commercial insurance, for example, allegations regarding employment practices or performance of contracts. The Authority evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

Note 15: Disclosures About Fair Value of Assets and Liabilities

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

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs supported by little or no market activity and significant to the fair value of the assets or liabilities

Stillwater Medical Center Authority
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Notes to Financial Statements
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Recurring Measurements

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying financial statements measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31:

| | Fair Value | Fair Value Measurements Using | | |
|--|---------------|---|---|--|
| | | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| 2017 | | | | |
| Money market mutual funds | \$ 22,982,139 | \$ 22,982,139 | \$ - | \$ - |
| Mutual funds – fixed income | \$ 30,410,451 | \$ 30,410,451 | \$ - | \$ - |
| Mutual funds – domestic equities | \$ 25,314,853 | \$ 25,314,853 | \$ - | \$ - |
| Mutual funds – international equities | \$ 8,576,199 | \$ 8,576,199 | \$ - | \$ - |
| U.S. Treasury obligations | \$ 2,040,361 | \$ 2,040,361 | \$ - | \$ - |
| U.S. agencies obligations | \$ 135,918 | \$ - | \$ 135,918 | \$ - |
| 2016 | | | | |
| Corporate stocks | \$ 14,332,792 | \$ 14,332,792 | \$ - | \$ - |
| Money market mutual funds | \$ 27,508,328 | \$ 27,508,328 | \$ - | \$ - |
| Mutual funds – fixed income | \$ 7,918,548 | \$ 7,918,548 | \$ - | \$ - |
| Mutual funds – domestic equities | \$ 7,665,244 | \$ 7,665,244 | \$ - | \$ - |
| Mutual funds – international equities | \$ 1,926,940 | \$ 1,926,940 | \$ - | \$ - |
| U.S. Treasury obligations | \$ 2,654,505 | \$ 2,654,505 | \$ - | \$ - |
| U.S. agencies obligations | \$ 4,455,373 | \$ 667,165 | \$ 3,788,208 | \$ - |
| Corporate bonds | \$ 5,091,891 | \$ 2,414,102 | \$ 2,677,789 | \$ - |

Stillwater Medical Center Authority
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Notes to Financial Statements
December 31, 2017 and 2016

Investments

Where quoted market prices are available in an active market, investments are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such investments are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, investments are classified within Level 3 of the hierarchy. The Authority had no Level 3 investments at December 31, 2017 and 2016.

Note 16: Subsequent Event

Subsequent to year-end, the Authority entered into an agreement with Perry Memorial Hospital Authority (Perry) to take over full use, operations, administration and management of Perry's hospital effective April 1, 2018. The term of the lease is for a period of five years with automatic extensions for four additional five-year terms. The Authority's consideration to Perry under the lease is \$1. Perry primarily earns revenues by operating a 26-bed hospital, two physician clinics and a home health agency in Perry, Oklahoma.

**Report on Internal Control over Financial Reporting and on
Compliance and Other Matters Based on an Audit of
Financial Statements Performed in Accordance with
Government Auditing Standards**

Independent Auditor's Report

Board of Trustees
Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
Stillwater, Oklahoma

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Stillwater Medical Center Authority d/b/a Stillwater Medical Center (the Authority), a component unit of the City of Stillwater, Oklahoma, which comprise the balance sheet as of December 31, 2017, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 18, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit, we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Board of Trustees
Stillwater Medical Center Authority
d/b/a Stillwater Medical Center

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Tulsa, Oklahoma
June 18, 2018

**Stillwater Medical Center Authority
d/b/a Stillwater Medical Center
A Component Unit of the City of Stillwater, Oklahoma
Schedule of Findings and Responses
Year Ended December 31, 2017**

| Reference Number | Finding |
|-----------------------------|----------------|
|-----------------------------|----------------|

No matters are reportable.