

**SPARTANBURG REGIONAL HEALTH  
SERVICES DISTRICT, INC.**

Combined Financial Statements

September 30, 2013 and 2012

(with Independent Auditors'  
Report thereon)

**SPARTANBURG REGIONAL HEALTH  
SERVICES DISTRICT, INC.**

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## **Independent Auditors' Report**

The Board of Directors  
Spartanburg Regional Health Services District, Inc.  
Spartanburg, South Carolina

### **Report on the Combined Financial Statements**

We have audited the accompanying combined financial statements of Spartanburg Regional Health Services District, Inc. (the "District"), which comprise the combined balance sheets as of September 30, 2013 and 2012, and the related combined statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the combined financial statements.

### ***Management's Responsibility for the Combined Financial Statements***

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined 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 combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the combined 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 District'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 combined 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 combined financial statements referred to above present fairly, in all material respects, the financial position of Spartanburg Regional Health Services District, Inc. as of September 30, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of Matter***

As discussed in Note 1 to the combined financial statements, during the year ended September 30, 2013, the District adopted new accounting guidance, Governmental Accounting Standards Board ("GASB") Section No. 63. Our opinion is not modified with respect to this matter.

***Other Matters******Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 11 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 audit 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.

*Dixon Hughes Goodman LLP*

Charlotte, North Carolina  
January 10, 2014

Spartanburg Regional Health Services District, Inc.

Management's Discussion and Analysis

Years Ended September 30, 2013 and 2012

This section of Spartanburg Regional Health Services District, Inc.'s (the "District") combined financial statements presents management's analysis of the District's financial performance during the fiscal year that ended on September 30, 2013. Please read it in conjunction with the combined financial statements, which follow this section.

**Financial Highlights**

Some highlights of the District's financial position in fiscal year 2013 include:

- Net patient service revenues increased from fiscal year 2012 to 2013 by approximately \$40 million or 5.6% primarily due to volume increases, new services, and resolution of prior year Medicare and Medicaid cost report settlements. Other revenues increased from fiscal year 2012 to 2013 by approximately \$10.4 million or 37.7% primarily due to the electronic health record incentive revenue recognized by the physician practice network, revenue recognized under promissory note agreements as well as a settlement agreement and revenue recognized by the newly acquired medical home network, Palmetto Physician Connections, LLC. Additionally, employee pharmacy drug sales increased over the prior year since fiscal year 2013 was its first full year of operations.
- Operating expenses increased from fiscal year 2012 to fiscal year 2013 by \$48.7 million or 6.7% primarily due to an increase in salaries and benefit expenses, supply expenses and other expenses. Salaries and benefit expenses increased approximately \$20.7 million primarily due to the addition of full time employees, wage merit increases, market adjustments, and increased health insurance expenses. Supplies increased approximately \$11.3 million primarily due to employee pharmacy costs (\$4.1 million) and changes in the administration of the 340B program (\$3.8 million) which resulted in net higher pharmaceutical costs in fiscal year 2013. Other expenses increased approximately \$16.8 million primarily due to an increase in fees and purchased services such as increased consulting cost related to expansion of cancer research program, contracted physicians services, and clinical equipment maintenance service costs.
- Net nonoperating revenues decreased by \$4.3 million or 307.8% from fiscal year 2012 to fiscal year 2013 primarily due to a decrease in net investment income. For the year ended September 30, 2013, the District recognized a net unrealized loss on investments and assets whose use is limited of approximately \$5.9 million. This is a change of approximately \$10 million less than the prior year. This decrease in net investment income is offset by an increase in other income. No unconditional promises to give were pledged in fiscal year 2013, and a gain on capital asset disposals was recognized in fiscal year 2013. This is a change of approximately \$5.9 million more than the prior year. Additionally, nonoperating revenues were not impacted in fiscal year 2013 by a loss on interest rate swap agreements since they were terminated during fiscal year 2012.

- The District's days cash on hand decreased in fiscal year 2013 to 154, a decrease of 24 under the prior year. This decrease was primarily attributable to significant capital asset purchases and the purchase of Palmetto Physician Connections, LLC. The District's day's cash in net patient accounts receivable of 48 days was comparable to the prior year. Volume increases over the prior year causing increases in patient accounts receivable helped to contribute to this increase.

### **Overview of the Combined Financial Statements**

The combined financial statements consist of two parts: Management's Discussion and Analysis and the Required Basic Combined Financial Statements. The required basic combined financial statements also include notes that explain in more detail some of the information in the combined financial statements.

### **Required Basic Combined Financial Statements**

The District uses accounting methods similar to those used by private sector companies. These combined financial statements offer short-term and long-term financial information about its activities. The combined Balance Sheets include all of the District's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to District creditors (liabilities). The assets and liabilities are presented in a classified format, which distinguishes between current and long-term assets and liabilities. These combined financial statements also provide the bases for computing rate of return, evaluating the capital structure of the District, and assessing the liquidity and financial flexibility of the District.

All of the current year's revenues and expenses are accounted for in the combined Statements of Revenues, Expenses, and Changes in Net Position. These combined statements measure the performance of the District's operations for the years ended September 30, 2013 and 2012.

The final required statements are the combined Statements of Cash Flows. The primary purpose of these combined statements is to provide information about the District's cash receipts and cash payments during the reporting period. The statements report cash receipts, cash payments, and net changes in cash resulting from operating, investing, noncapital financing, and capital and related financing activities and information concerning sources and uses of cash.

## Financial Analysis

**Table A-1**

*Condensed Combined Balance Sheets (In Thousands of Dollars)*

	Fiscal Year 2013	Fiscal Year 2012	Dollar Increase (Decrease)	Percentage Increase (Decrease)
Current assets	\$ 201,492	\$ 215,289	\$ (13,797)	(6.41)%
Capital assets, net	418,420	412,859	5,561	1.35%
Other long-term assets	268,103	255,231	12,872	5.04%
Total assets	<b>\$ 888,015</b>	<b>\$ 883,379</b>	<b>\$ 4,636</b>	<b>0.52%</b>
Current liabilities	\$ 106,082	\$ 109,535	\$ (3,424)	(3.13)%
Long-term liabilities	226,509	236,723	(10,214)	(4.31)%
Total liabilities	<b>332,591</b>	<b>346,258</b>	<b>(13,638)</b>	<b>(3.94)%</b>
Invested in capital assets, net	181,558	166,467	15,091	9.07%
Restricted	6,159	4,642	1,517	32.68%
Unrestricted	367,707	366,012	1,666	0.46%
Total net position	<b>555,424</b>	<b>537,121</b>	<b>18,274</b>	<b>3.40%</b>
Total liabilities & net position	<b>\$ 888,015</b>	<b>\$ 883,379</b>	<b>\$ 4,636</b>	<b>0.52%</b>

As can be seen in Table A-1, net position increased approximately \$18.3 million to approximately \$555.4 million in fiscal year 2013. Total assets increased by approximately \$4.6 million. Other long-term assets increased by approximately \$12.9 million primarily due to an increase in assets whose use is limited and goodwill, which increased approximately \$6.9 million and \$6.3 million, respectively, over the prior year. This was due to an increase in plant fund cash as well as an increase the amount held by the District's trustee for debt service. Goodwill increased over the prior year from zero as result of the District's purchase of a Medicaid medical home network, Palmetto Physician Connections, LLC. Current assets decreased approximately \$13.8 million primarily due to a decrease in cash and cash equivalents. Offsetting the decrease in cash and cash equivalents are increases in patient accounts receivable and other current assets. Patient accounts receivable has increased over the prior year by approximately \$8.9 million primarily due to increased volumes at Village Hospital, Gibbs Cancer Center and the new immediate care centers. Other current assets increased over the prior year approximately \$8.4 million primarily due to a Medicare cost report receivable, electronic health records incentive receivables and a Medicaid teaching supplement receivable outstanding at September 30, 2013. Net capital assets increased approximately \$5.6 million primarily due to the net activity of additions, deductions and depreciation. Total liabilities decreased by approximately \$13.7 million. Current liabilities decreased by approximately \$3.5 million over the prior year primarily

due to the decrease in estimated third-party payor settlements. Long-term liabilities decreased approximately \$10.2 million mainly due to the decrease in long-term debt of approximately \$7.7 million. Refer to Long-term Debt section below for more detail.

## **Financial Analysis**

**Table A-2**

*Condensed Combined Balance Sheets (In Thousands of Dollars)*

	<b>Fiscal Year 2012</b>	<b>Fiscal Year 2011</b>	<b>Dollar Increase (Decrease)</b>	<b>Percentage Increase (Decrease)</b>
Current assets	<b>\$ 215,289</b>	\$ 204,802	\$ 10,487	5.12%
Capital assets, net	<b>412,859</b>	427,291	(14,432)	(3.38)%
Other long-term assets	<b>255,231</b>	229,493	25,738	11.22%
Total assets	<b>\$ 883,379</b>	\$ 861,586	\$ 21,793	2.53%
Current liabilities	<b>\$ 109,535</b>	\$ 102,339	\$ 7,196	7.03%
Long-term liabilities	<b>236,723</b>	243,086	(6,363)	(2.62)%
Total liabilities	<b>346,258</b>	345,425	833	0.24%
Invested in capital assets, net	<b>166,467</b>	199,935	(33,468)	(16.74)%
Restricted	<b>4,642</b>	3,429	1,213	35.37%
Unrestricted	<b>366,012</b>	312,797	53,215	17.01%
Total net position	<b>537,121</b>	516,161	20,960	4.06%
Total liabilities and net position	<b>\$ 883,379</b>	\$ 861,586	\$ 21,793	2.53%

As can be seen in Table A-2, net position increased approximately \$20.9 million to approximately \$537.1 million in fiscal year 2012. Total assets increased by approximately \$21.8 million. Other long-term assets increased by approximately \$25.7 million primarily due to an increase in assets whose use is limited, which increased approximately \$32.4 million over the prior year. This was due to an increase in plant fund cash, an increase in the market value of long-term investments, and interest earned and collected on long-term investments. Current assets increased approximately \$10.5 million primarily due to an increase in patient accounts receivable and other current assets. Patient accounts receivable has increased over the prior year approximately \$6 million primarily due to increased volumes. Other current assets increased over the prior year approximately \$4.2 million primarily due to a Medicare cost report receivable outstanding at September 30, 2012.



Offsetting these increases in other long-term assets and current assets is a decrease in net capital assets of approximately \$14.4 million primarily due to the net activity of additions, deductions and depreciation. Total liabilities increased by approximately \$833,000. Current liabilities increased by approximately \$7.2 million over the prior year primarily due to the difference in timing of vendor payments compared to the prior fiscal year, increases in the current portion of long-term debt and capital lease obligations, and current liabilities amounting to \$2.2 million created as a result of two new unconditional promises to give. These current liability increases are offset by a decrease in estimated third-party payor settlements of approximately \$4.1 million due to prior year cost report settlements. Long-term liabilities decreased approximately \$6.4 million. Long-term debt increased approximately \$18.2 million. This increase is offset by a decrease in long-term liabilities of approximately \$25.7 million due to the termination of interest rate swap agreements.

**Table A-3**

*Condensed Combined Statements of Revenues, Expenses, and Changes in Net position (In Thousands of Dollars)*

	<b>Fiscal Year 2013</b>	<b>Fiscal Year 2012</b>	<b>Dollar Increase (Decrease)</b>	<b>Percentage Increase (Decrease)</b>
Net patient service revenues	\$ 759,552	\$ 719,525	\$ 40,027	5.56%
Other revenues	37,932	27,545	10,387	37.71%
Total operating revenues	797,484	747,070	50,414	6.75%
Salaries, temporary personnel, and benefit expenses	430,757	410,046	20,712	5.05%
Supply expenses	143,940	132,683	11,257	8.48%
Other expenses	201,548	184,794	16,782	9.08%
Total operating expenses	776,245	727,523	48,751	6.70%
Operating income	21,239	19,547	1,663	8.51%
Net nonoperating revenues (expenses)	(2,936)	1,413	(4,349)	(307.78)%
Increase in net position	18,303	20,960	(2,686)	(12.81)%
Beginning net position	537,121	516,161	20,960	4.06%
Ending net position	\$ 555,424	\$ 537,121	\$ 18,274	3.40%

Total operating revenues increased by approximately \$50.4 million primarily due to the increase of net patient service revenue of \$40 million and an increase in other revenues of \$10.4 million. This increase of net patient service revenue was primarily due to volume increases and resolution of prior year Medicare and Medicaid cost report settlements. The increase in other revenues was caused primarily by the electronic health record incentive revenue recognized by the physician practice network, revenue recognized under promissory note agreements as well as a settlement

agreement and revenue recognized by the newly acquired medical home network, Palmetto Physician Connections, LLC. Additionally, employee pharmacy drug sales increased over the prior year since fiscal year 2013 was its first full year of operations. The increase in total operating expenses of approximately \$48.7 million over the prior year was due to increases in salaries and benefit expenses, supply expenses and other expenses. Salaries and benefit expenses increased approximately \$20.7 million primarily due to the addition of full time employees, market adjustments, a two percent wage increase and increased health insurance expenses over the prior year. Supplies increased approximately \$11.3 million primarily due to employee pharmacy costs since fiscal year 2013 was its first full year of operations. Additionally, changes in the administration of the 340B program resulted in net higher pharmaceutical costs in fiscal year 2013. Other expenses increased approximately \$16.8 million primarily due to an increase in fees and purchased services such as increased consulting cost related to expansion of cancer research program, contracted physicians services, and clinical equipment maintenance costs.

Net nonoperating revenues decreased by \$4.3 million compared to the prior year primarily due to the decrease in net investment income. For the year ended September 30, 2013, the District recognized a net unrealized loss on investments and assets whose use is limited of approximately \$5.9 million. This is a change of approximately \$10 million less than the prior year. This decrease in net investment income is offset by an increase in other income. No unconditional promises to give were pledged in fiscal year 2013, and a gain on capital asset disposals was recognized in fiscal year 2013. This is a change of approximately \$5.9 million more than the prior year. Additionally, nonoperating revenues were not impacted in fiscal year 2013 by a loss on interest rate swap agreements since they were terminated during fiscal year 2012.

**Table A-4**

*Condensed Combined Statements of Revenues, Expenses, and Changes in Net position (In Thousands of Dollars)*

	<b>Fiscal Year 2012</b>	<b>Fiscal Year 2011</b>	<b>Dollar Increase (Decrease)</b>	<b>Percentage Increase (Decrease)</b>
Net patient service revenues	\$ 719,525	\$ 708,071	\$ 11,454	1.62%
Other revenues	27,545	18,541	9,004	48.56%
Total operating revenues	747,070	726,612	20,458	2.82%
Salaries, temporary personnel, and benefit expenses	410,046	411,384	(1,338)	(0.33)%
Supply expenses	132,683	127,015	5,668	4.46%
Other expenses	184,794	181,369	3,425	1.89%
Total operating expenses	727,523	719,768	7,755	1.08%

**SPARTANBURG REGIONAL HEALTH  
SERVICES DISTRICT, INC.**

**Management's Discussion and Analysis, continued**

Operating income	<b>19,547</b>	6,844	12,703	185.61%
Net nonoperating revenues (expenses)	<b>1,413</b>	3,042	(1,629)	(53.55)%
Capital grants and contributions	<b>0</b>	39	(39)	(100.00)%
Increase in net position	<b>20,960</b>	9,925	11,035	111.18%
Beginning net position	<b>516,161</b>	506,236	9,925	1.96%
Ending net position	<b>\$ 537,121</b>	\$ 516,161	\$ 20,960	4.06%

Total operating revenues increased by approximately \$20.5 million primarily due to the increase of net patient service revenue of \$11.5 million and an increase in other revenues of \$9 million. This increase of net patient service revenue was primarily due to volume increases. Additionally, a 3.7% aggregate payment increase from managed care contracts was implemented on October 1, 2011. The increase in other revenues was caused primarily by the recognition of revenue for incentives earned under the Medicare and Medicaid programs for compliance with the applicable electronic health record meaningful use requirements. Additionally, other revenues increased due to the new employee pharmacy drug sales. The increase in total operating expenses of approximately \$7.8 million over the prior year was primarily due to an increase in supplies of approximately \$5.7 million and an increase in other expenses of approximately \$3.4 million. The increase in supplies relates to increased pharmaceutical cost primarily due to the new employee pharmacy and increased orthopedic major medical supplies at Village Hospital. The increase in other expense relates to increased depreciation expense over the prior year.

**Capital Assets and Long-Term Debt**

**Capital Assets**

As of September 30, 2013, the District had approximately \$418.4 million invested in capital assets, as reflected in Table A-5, which represents a net increase (additions, deductions and depreciation) of approximately \$5.6 million or 1.35% from the end of last year.

**Table A-5**

*Capital Assets (In Thousands of Dollars)*

	<b>Fiscal Year 2013</b>	<b>Fiscal Year 2012</b>
Land and land improvements	\$ 57,163	\$ 54,995
Building and building fixtures	264,992	258,218
Equipment	571,315	547,253
Construction-in-progress	6,399	5,258
Equipment under capital lease obligations	17,607	15,314
Total capital assets	917,476	881,038
Less accumulated depreciation	499,056	468,179
Net capital assets	<u>\$ 418,420</u>	<u>\$ 412,859</u>

As of September 30, 2012, the District had approximately \$412.9 million invested in capital assets, as reflected in Table A-5, which represents a net decrease (additions, deductions and depreciation) of approximately \$14.4 million or 3.4% from the end of last year.

**Table A-6**

*Capital Assets (In Thousands of Dollars)*

	<b>Fiscal Year 2012</b>	<b>Fiscal Year 2011</b>
Land and land improvements	\$ 54,995	\$ 54,600
Building and building fixtures	258,218	256,387
Equipment	547,253	535,500
Construction-in-progress	5,258	6,850
Equipment under capital lease obligations	15,314	13,911
Total capital assets	881,038	867,248
Less accumulated depreciation	468,179	439,957
Net capital assets	<u>\$ 412,859</u>	<u>\$ 427,291</u>

### **Long-Term Debt**

As of September 30, 2013, the District had approximately \$229 million in outstanding long-term debt and as of September 30, 2012, the District had approximately \$237.7 million in outstanding long-term debt. This represents a net decrease of approximately \$8.7 million under the prior the fiscal year, primarily due to principal payments on long-term debt.

For more detailed information regarding the District's capital assets and long-term debt, refer to the accompanying notes to the combined financial statements.

### **Future Outlook**

The Board of Directors and management believe that the District is well positioned to improve its strong financial condition and continue to provide excellent health care services to its service area. Increases in volume are expected to continue as the District continues to add new services, expand existing services, and increase its market share. There is ongoing legislative action on both the federal and state level addressing health care reform and the national budget deficit that have the potential for impacting Medicare and South Carolina Medicaid payments to healthcare providers. These legislative actions include continuing implementation of the Affordable Care Act, South Carolina's response to Medicaid expansion, the sequestration of Medicare payments, and the American Taxpayer Relief Act. Due to the District's ownership of a diverse selection of physician practices (Medical Group of the Carolinas), advanced information technology, medical staff and employee leadership, development of a Medicaid managed care organization, growth of cancer research, and relationship with Regional Health Plus, LLC, management believes that the District is well positioned to address the challenges and opportunities of health care reform. The District's prudent use of financial resources, cost-control efforts, and increases in patient volume will ensure that the District will continue as the primary provider of health care service in the area.

### **Requests for Information**

This financial report is designed to provide a general overview of the District's finances for all those with an interest in the District's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the District.

# SPARTANBURG REGIONAL HEALTH SERVICES DISTRICT, INC.

## Combined Balance Sheets

	September 30,	
	2013	2012
	<i>(In Thousands)</i>	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 41,501	\$ 78,110
Short term investments	27,174	22,128
Patient accounts receivable, net of allowance for uncollectible accounts of approximately \$78,836 (2013) and \$92,596 (2012)	99,161	90,293
Drugs and supplies	7,054	6,604
Other current assets	26,602	18,154
Total current assets	<u>201,492</u>	<u>215,289</u>
Assets whose use is limited:		
Board designated cash and investments	242,132	236,594
Board designated other assets	951	1,095
Funds held by trustee	6,159	4,642
Total assets whose use is limited	<u>249,242</u>	<u>242,331</u>
Capital assets, net	418,420	412,859
Other assets	18,861	12,900
Total assets	<u>\$ 888,015</u>	<u>\$ 883,379</u>

# SPARTANBURG REGIONAL HEALTH SERVICES DISTRICT, INC.

## Combined Balance Sheets (continued)

	September 30,	
	2013	2012
	<i>(In Thousands)</i>	
<b>Liabilities and Net Position</b>		
Current liabilities:		
Accounts payable	\$ 43,568	\$ 33,312
Accrued expenses	46,029	51,341
Estimated third-party payor settlements	3,047	10,241
Current portion of obligations under capital leases	3,632	3,016
Current portion of unconditional promises to give	1,400	2,200
Current portion of long-term debt	8,406	9,425
Total current liabilities	<u>106,082</u>	<u>109,535</u>
Long-term debt, less current portion	220,621	228,317
Long-term obligations under capital leases,		
less current portion	4,203	5,634
Long-term unconditional promises to give,		
less current portion	1,685	2,772
Total liabilities	<u>332,591</u>	<u>346,258</u>
Net position:		
Unrestricted	367,707	366,012
Restricted:		
Expendable for debt service	6,159	4,642
Invested in capital assets, net of related debt	181,558	166,467
Total net position	<u>555,424</u>	<u>537,121</u>
Total liabilities and net position	<u>\$ 888,015</u>	<u>\$ 883,379</u>

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

# SPARTANBURG REGIONAL HEALTH SERVICES DISTRICT, INC.

## Combined Statements of Revenues, Expenses, and Changes in Net Position

	Year Ended September 30,	
	2013	2012
	<i>(In Thousands)</i>	
Operating revenues:		
Net patient service revenues, net of provision for bad debts of approximately \$61,853 (2013) and \$68,359 (2012)	759,552	719,525
Other operating revenues	37,932	27,545
Total operating revenues	<u>797,484</u>	<u>747,070</u>
Operating expenses:		
Salaries	342,026	327,116
Benefits	88,731	82,929
Supplies	143,940	132,683
Fees and purchased services	83,523	72,549
Depreciation	49,259	46,770
Other	68,766	65,476
Total operating expenses	<u>776,245</u>	<u>727,523</u>
Operating income	21,239	19,547
Nonoperating revenues (expenses):		
Interest expense	(11,717)	(10,495)
Net investment income (loss)	(1,309)	9,474
Noncapital grants and contributions	9,446	10,301
Other income (loss)	644	(7,867)
Total nonoperating revenues (expenses)	<u>(2,936)</u>	<u>1,413</u>
Excess of revenues over expenses	<u>18,303</u>	<u>20,960</u>
Increase in net position	18,303	20,960
Net position at beginning of year	537,121	516,161
Net position at end of year	<u>\$ 555,424</u>	<u>\$ 537,121</u>

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



# SPARTANBURG REGIONAL HEALTH SERVICES DISTRICT, INC.

## Combined Statements of Cash Flows

	<b>Year Ended September 30,</b>	
	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Cash flows from operating activities:		
Receipts from patients	\$ 743,490	\$ 709,481
Payments to vendors	(293,910)	(267,235)
Claims and self-insurance payments	(39,615)	(42,504)
Payments for salaries and benefits	(389,092)	(365,031)
Other receipts for operations	27,402	23,940
Net cash provided by operating activities	<u>48,275</u>	<u>58,651</u>
Cash flows from noncapital financing activities:		
Noncapital grants and contributions	9,446	10,301
Unconditional pledges to give	–	5,600
Payment of unconditional pledges to give	(2,000)	(200)
Other	644	(4,682)
Net cash provided by noncapital financing activities	<u>8,090</u>	<u>11,019</u>
Cash flows from capital and related financing activities:		
Payment of debt issue costs	–	(1,733)
Purchase and construction of capital assets	(49,818)	(29,491)
Proceeds from issuance on long-term debt	–	161,022
Principal payments on long-term debt, net	(9,375)	(137,811)
Interest payments on long-term debt	(11,604)	(10,311)
Termination of interest rate swap agreements	–	(28,747)
Principal payments on capital lease obligations	(3,108)	(2,853)
Net cash used in capital and related financing activities	<u>(73,905)</u>	<u>(49,924)</u>
Cash flows from investing activities:		
Net change in investments	(5,046)	1
Net change in assets whose use is limited	(11,152)	4,402
Net investment income (loss)	(1,309)	9,474
Proceeds from sale of capital assets	85	130
Purchase of Palmetto Physician Connections, LLC	(6,000)	–
Net change in investments in joint ventures	112	506
Net cash provided by (used in) investing activities	<u>(23,310)</u>	<u>14,513</u>
Net increase (decrease) in cash and cash equivalents	<u>(40,850)</u>	34,259
Cash and cash equivalents at beginning of year	<u>152,529</u>	118,270
Cash and cash equivalents at end of year	<u><u>\$ 111,679</u></u>	<u><u>\$ 152,529</u></u>

(continued)

# SPARTANBURG REGIONAL HEALTH SERVICES DISTRICT, INC.

## Combined Statements of Cash Flows (continued)

	Year Ended September 30,	
	2013	2012
	<i>(In Thousands)</i>	
Reconciliation of cash and cash equivalents:		
Cash and cash equivalents on the balance sheet	\$ 41,501	\$ 78,110
Cash and cash equivalents in assets whose use is limited	70,178	74,419
Total cash and cash equivalents	<u>\$ 111,679</u>	<u>\$ 152,529</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 21,239	\$ 19,547
Adjustments to reconcile operating income to net cash provided by operating activities:		
Amortization of bond discount and bond premium	660	102
Amortization of debt issue costs	215	270
Provision for bad debts	61,853	68,359
Depreciation	49,259	46,777
Loss on sale of capital assets	125	1,505
Changes in operating assets and liabilities:		
Patient accounts receivable	(70,721)	(74,320)
Drugs and supplies	(450)	1,135
Other current assets	(8,448)	(4,196)
Accounts payable	7,049	683
Estimated third-party payor settlements	(7,194)	(4,083)
Accrued expenses	(5,312)	2,872
Net cash provided by operating activities	<u>\$ 48,275</u>	<u>\$ 58,651</u>
Supplemental non-cash information:		
Capital assets acquired under capital lease obligations	\$ 2,293	\$ 1,403
Capital assets included in accounts payable	<u>\$ 2,919</u>	<u>\$ 3,086</u>

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

1. **Description of Reporting Entity and Summary of Significant Accounting Policies**

**Reporting Entity** - Spartanburg Regional Health Services District, Inc. (the “District”) is a statutory public hospital corporation and a political subdivision of the state of South Carolina, and, as such, is exempt from federal and state income tax. The District is governed by an eleven member Board of Directors (the “Board”) appointed by the Spartanburg County Council, the primary government.

The District operates a health care system in Spartanburg County consisting of Spartanburg Medical Center (“SMC”), Spartanburg Hospital for Restorative Care (“SHRC”), Village Hospital (“VH”) and the Home Office, which provides common services for the District. The District also owns and operates the Medical Group of the Carolinas, a network of physician practices. In addition, the District owns SMC Ventures, LLC and Greer Group, LLC, which are organized as limited liability companies under South Carolina limited liability company statutes. The District also owns NC Network, Inc., which is organized as a North Carolina corporation. During the year ended September 30, 2013, the District purchased a Medicaid Medical Home Network, Palmetto Physician Connections, LLC, with the intention to convert to a Medicaid Management Care Organization. These affiliated entities are reported as blended component units of the District. SMC Ventures, LLC and Greer Group, LLC operate on a calendar year end. All intercompany transactions have been eliminated in the combined financial statements.

SMC Ventures, LLC holds investments in joint ventures as further described in this note under “Investments in Joint Ventures.”

**Accounting Standards and Methods** - The District follows the provisions of the American Institute of Certified Public Accountants Audit and Accounting Guide, *Health Care Organizations* (the “Guide”). Under the provisions of the Guide, the District qualifies as a governmental organization and is subject to the pronouncements of the Governmental Accounting Standards Board (“GASB”). The District is reported as an enterprise fund under GASB pronouncements. The proprietary fund method of accounting is used whereby revenues and expenses are recognized on the accrual basis.

During the year ended September 30, 2013, the District adopted GASB Statement No. 61, *Financial Reporting Entity: Omnibus*. This Statement modifies the criteria for including component units as part of the financial reporting entity and the conditions under which a component unit may be reported as blended. Adoption of this Statement did not have a material impact on the District’s basic combined financial statements.

During the year September 30, 2013, the District adopted GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which supersedes GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*. This Statement is intended to resolve conflicting accounting and financial reporting guidance that could diminish the consistency in financial reporting. Adoption of this Statement did not have a material impact on the District's basic combined financial statements.

In the year ended September 30, 2013, the Medical Center adopted GASB Statement No. 63, *Financial reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which modifies current financial reporting of those elements. The most significant change was the replacement of the Statements of Revenues, Expenses, and Changes in Net Assets with the Statements of Revenues, Expenses, and Changes in Net Position

**Use of Estimates** - The preparation of combined 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 combined financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Cash and Cash Equivalents** - Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less when purchased.

At various times throughout the year, the District maintains deposits at financial institutions in excess of amounts covered by the Federal Deposit Insurance Corporation ("FDIC") limits. Management believes the credit risk associated with these deposits is minimal.

**Patient Accounts Receivable** - Patient accounts receivable are carried at the original charge less an estimate for bad debts. The allowance is based upon a review of the outstanding balances aged by financial class. Management uses collection percentages based upon historical collection experience to determine collectability. Management also reviews troubled, aged accounts to determine collection potential. Patient accounts receivable are written off when deemed uncollectible. Recoveries of accounts previously written off are recorded as a reduction to provision for bad debts when received. Interest is not charged on patient accounts receivable.

**Drugs and Supplies** - Drugs and supplies are stated at the lower of cost, determined using the first-in, first-out method, or market.

**Investments** - Short term and long term investments consist principally of certificates of deposit, debt securities, and equity securities. Investments in debt and equity securities are reported at fair value. Interest, dividends and gains and losses, both realized and unrealized, on investments in debt and equity securities are included in nonoperating revenues when earned. Alternative investments are recorded at cost since the District does not have the ability to exert influence over the portfolio. Investments recorded at cost are evaluated for impairment on a monthly basis. At September 30, 2013 no impairment charges were recorded for cost-based alternative investments.

**Assets Whose Use is Limited** - Assets whose use is limited primarily includes assets designated by the Board for future capital improvements, over which the Board retains control and may at its discretion subsequently use for other purposes, and amounts held by Bond Trustees in accordance with indenture agreements.

**Capital Assets** - Capital assets are stated at cost, except for contributed property, which is recorded at its fair value at date of donation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as determined by industry standards. Routine maintenance, repairs, and replacements are charged to expense. The District capitalizes all assets purchased individually that have a useful life of three or more years and a cost of \$2,500. Items purchased as a group are capitalized if the purchase is for the same item, the individual item cost is equal to or exceeds \$500, the total cost of the group purchase is equal to or exceeds \$25,000, and the purchase occurs at one time.

The amortization of assets under capital leases is included in depreciation expense.

When properties are retired or otherwise disposed of, the cost of the assets and related allowances for depreciation are removed from the accounts, and any resulting gain or loss is recognized as an operating activity in the combined Statements of Revenues, Expenses and Changes in Net Position.

Interest costs incurred during the period of construction of qualifying capital assets are capitalized as a component of the cost of these assets and amortized over the life of the asset.

**Investments in Joint Ventures** - Regional HealthPlus, LLC (“RHP”) is a limited liability company formed to organize a collaborative network of health care providers and execute and manage various contracts with third-party payors. RHP is owned 50% by SMC Ventures, LLC and 50% by area physicians. The District accounts for the investment in RHP using the equity method.

Upstate Linen Services, LLC is a limited liability company formed to offer a collaborative linen supplier service. Upstate Linen Services, LLC is owned 33% by SMC Ventures, LLC and 67% by other area hospitals. The District accounts for the investment in Upstate Linen Services, LLC using the equity method.

The Ambulatory Surgery Center of Spartanburg, LLC (“ASCS, LLC”) is a limited liability company formed to assist the District in serving the ambulatory surgical needs of Spartanburg County residents. ASCS, LLC is owned 50% by SMC Ventures, LLC and 50% by area physicians. The District accounts for the investment in ASCS, LLC using the equity method.

The Ambulatory Surgery Center of Pelham, LLC (“ASC Pelham, LLC”) is a limited liability company formed to assist the District in serving the ambulatory surgical needs of Spartanburg County residents. ASC Pelham, LLC is owned 50% by SMC Ventures, LLC and 50% by area physicians. The District accounts for the investment in ASC Pelham, LLC using the equity method.

The District’s investments in joint ventures included in other assets are as follows:

	<b>September 30</b>	
	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Regional HealthPlus, LLC	\$ 3,853	\$ 3,569
Upstate Linen Services, LLC	1,609	1,718
Ambulatory Surgery Center of Spartanburg, LLC	2,311	2,444
Ambulatory Surgery Center of Pelham, LLC	1,477	1,631
	<u>\$ 9,250</u>	<u>\$ 9,362</u>

**Debt Issue Costs** - Debt issue costs are amortized over the life of the related bonds utilizing a straight-line method, which approximates the effective interest method. Accumulated amortization was approximately \$1.3 million and \$2.1 million at September 30, 2013 and 2012, respectively.

**Derivative Instruments** - The District entered into derivatives, exclusively interest rate swap agreements, to manage interest rate exposures on variable rate Hospital Revenue Bonds. Interest rate swaps allow the District to swap variable interest rates on a stated notional amount for fixed rates. The gain or loss for the period associated with the fair market value of the agreements is included in nonoperating revenues and expenses. These interest rate swap agreements were terminated in 2012 in conjunction with the 2012 bond refundings.

**Net Position** - Pursuant to Governmental Accounting Standards No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, which amends Governmental Accounting Standards No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, the District has renamed net assets to “net position.”

Net position of the District classified as invested in capital assets, net of related debt consist of capital assets, net of accumulated depreciation reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets.

Restricted components of net position include amounts deposited with trustees as required by revenue bond indentures. Unrestricted components of net position are remaining net position that do not meet the definition of invested in capital assets net of related debt or restricted.

**Net Patient Service Revenues** - Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Third-party contractual revenue adjustments are accrued on an estimated basis in the period the related services are rendered. Such amounts are subject to audit by governmental agencies. Adjustments, if any, are included in contractual revenue adjustments in the year of determination. In compliance with governmental accounting standards, net patient service revenues have been reduced by the amount of bad debt expense incurred by the District.

The District's policy does not require collateral or other security for patient accounts receivable. The District routinely accepts assignment of, or is otherwise entitled to receive, patient benefits payable under health insurance programs, plans or policies such as those related to Medicare, Medicaid, Blue Cross, health maintenance organizations and commercial insurance carriers.

**Charity Care** - The District accepts all patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain established policies of the District. Essentially, these policies define charity services as those services for which no payment is anticipated. In assessing a patient's inability to pay, the District utilizes the generally recognized poverty income levels of South Carolina, and also includes certain cases where incurred charges are significant when compared to the patient's income. Patients that qualify for the state Medically Indigent Act Program are a component of charity care. The District receives no reimbursement for services provided to these patients. Charity care is not reflected in net patient service revenues. The gross amount of charges written off to charity care under these policies for the year ended September 30, 2013 and 2012 were approximately \$80.7 million and \$81.6 million, respectively. The net cost of charity care provided was approximately \$26.5 million in 2013 and \$27.6 million in 2012. The District uses the cost to charge ratio to estimate the cost of charity care.

**Operating Revenues and Expenses** - The District's combined statements of revenues, expenses, and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the District's principal activity. Nonexchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs. Investment income on proceeds of borrowings that are held by a trustee, to the extent not capitalized, is reported as other revenues.

**Grants and Contributions** - From time to time, the District receives grants from Spartanburg County, the State of SC, and the Federal Government as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

**Income Taxes** - The District is a political subdivision of the State of South Carolina and also has been granted exemption from income taxes as an organization described in Section 115 of the Internal Revenue Code. SMC Ventures LLC is a nonexempt affiliate that files informational tax returns with appropriate federal and state taxing authorities in compliance with Internal Revenue Service and state provisions, are current on all tax payments. Greer Group, LLC and the NC Network Inc. are reported within SMC Ventures, LLC. The District has determined that it does not have any material unrecognized tax benefits or obligations as of September 30, 2013. Fiscal years ending on or after September 30, 2010 remain subject to examination by federal and state tax authorities.

**Risk Management** - The District 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; and, natural disasters; medical malpractice claims and judgments; and employee health, dental and accident benefits. Insurance coverage is purchased to cover the majority of claims arising from such matters. The District is self-insured for amounts up to a specified level for health and medical coverages for its employees and medical malpractice claims. The estimated liability is the total estimated amount to be paid for all known claims or incidents and a reserve for incurred but not reported claims. As of September 30, 2013 and 2012, the District included a liability of \$2.5 million included in accounts payable related to an ongoing U.S. Department of Justice investigation.



**Future Accounting and Reporting Requirements** - In 2012, the GASB issued GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. This Statement specifically requires certain balances currently being reported as assets and liabilities to be reported as deferred outflows of resources and deferred inflows of resources on the Combined Balance Sheet. Further, the pronouncement also requires certain items currently reported as assets and liabilities on the Combined Balance Sheet to be reported as outflows of resources and inflows of resources on the Combined Statement of Revenues, Expenses, and Changes in Net Position. This Statement must be adopted no later than the year ending September 30, 2014. The District has not yet determined the impact of this Statement on the basic combined financial statements.

In 2012, the GASB issued GASB Statement No. 66, *Technical Corrections – 2012*, which amends GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*. This amendment, along with GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which was adopted in the year ended September 30, 2013 by the District, is intended to resolve conflicting accounting and financial reporting guidance that could diminish the consistency in financial reporting for: a) governmental fund type usage for risk financing activities, b) operating lease payments that vary from a straight-line basis, c) differences between the initial investment and the principal amount of purchased loans, and d) servicing fees related to certain mortgage loan sales. The provisions of GASB Statement No. 66 must be adopted no later than the year ending September 30, 2014. The adoption of this Statement is not expected to have a material impact on the basic combined financial statements of the District.

In 2012, the GASB issued GASB Statement No. 67, *Financial Reporting for Pension Plans*, and GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which require enhanced note disclosure and required supplementary information for both defined benefit and defined contribution pension plans as well as provide standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expenses for pension plans. GASB Statement No. 67 must be adopted for pension plans no later than the year ending September 30, 2014, while GASB Statement No. 68 must be adopted not later than the year ending September 30, 2015. The District has not yet determined the impact of these Statements on the basic combined financial statements.

In 2013, the GASB issued GASB Statement No. 69, *Government Combinations and Disposals of Government Operations*, which establishes accounting and financial reporting standards related to government combinations and disposals of government operations. The provisions of this Statement must be adopted no later than the year ending September 30, 2014. The District has not yet determined the impact of this Statement on the basic combined financial statements.

**Reclassification** – Certain 2012 combined financial statement amounts have been reclassified to conform to the 2013 combined financial statement presentation.

2. **Cash, Investments, and Assets Whose Use is Limited**

At September 30, 2013 and 2012, the District had cash on hand and deposits as follows:

	<b>September 30</b>	
	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Insured (FDIC) or collateralized with securities held by the District	\$ 2,673	\$ 2,176
Collateralized by securities held by the pledging financial institution's trust department, but not in the District's name	38,828	75,934
Total	<u><u>\$ 41,501</u></u>	<u><u>\$ 78,110</u></u>

The types of securities which are permitted investments for District funds are established by the District's Investment Policy in accordance with South Carolina Statutes. As of September 30, 2013, the District's funds are permitted to be invested in certain principal protected investment vehicles. The District's investments maintain a target allocation of one-third corporate bonds, one-third U.S. Intermediate Term Treasuries, and one-third Treasury Inflation Protected Securities as established by the District's Investment Policy.

**Custodial Credit Risk** - The District's deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized or are collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name. The District's investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the District, and are held by either the counterparty or the counterparty's trust department or agent but not in the District's name. The deposit risk is that, in the event of the failure of a depository financial institution, the District will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

**Concentration of Credit Risk** - This is the risk associated with the amount of investments the District has with any one issuer that exceeds 5% or more of its total investments and assets whose use is limited. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement. The District's investment policy states that not more than 10% of a manager's portfolio may be invested in the securities of any one issuer, with the exception of the U.S. Government or its agencies and other sovereign government issuers.

Credit Risk - This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The District's investment policy provides guidelines for its fund managers and lists specific allowable investments. The policy provides for the utilization of varying styles of managers so that portfolio diversification is maximized and total portfolio efficiency is enhanced.

The credit risk profile of the District's investments and assets whose use is limited as of September 30, 2013 and 2012 is as follows:

Investment Type	September 30, 2013 <i>(In Thousands)</i>	Rating	
		A-AAA	N/A
Cash and cash equivalents	\$ 70,178	\$ -	\$ 70,178
Corporate obligations	48,401	48,401	-
Foreign obligations	16,090	16,090	-
U.S. Treasury obligations	109,339	-	109,339
Certificates of Deposit	2,000	-	2,000
U.S. Agency obligations	30,032	-	30,032
Municipal	240	240	-
Alternative investments	136	-	136
<b>Total</b>	<b>\$ 276,416</b>	<b>\$ 64,731</b>	<b>\$ 211,685</b>

Investment Type	September 30, 2012 <i>(In Thousands)</i>	Rating	
		A-AAA	N/A
Cash and cash equivalents	\$ 74,419	\$ -	\$ 74,419
Corporate obligations	42,852	42,852	-
Foreign obligations	10,142	10,142	-
U.S. Treasury obligations	124,837	-	124,837
Certificates of Deposit	2,000	-	2,000
U.S. Agency obligations	10,018	-	10,018
Alternative investments	191	-	191
<b>Total</b>	<b>\$ 264,459</b>	<b>\$ 52,994</b>	<b>\$ 211,465</b>

Interest Rate Risk – This is the risk that changes in interest rates will adversely affect the fair value of an investment. The District's investment policy authorizes a strategic asset allocation that is designed to provide an optimal return over the District's investment horizon and within the District's risk tolerance and cash requirements.

**SPARTANBURG REGIONAL HEALTH  
SERVICES DISTRICT, INC.**

**Notes to the Combined Financial Statements, continued**

The distribution of the District's investments and assets whose use is limited by maturity as of September 30, 2013 and 2012 are as follows (in thousands):

Investment Type	September 30, 2013	Remaining Maturity (In Months)				N/A
		12 Months or Less	13 Months to 24 Months	25 Months to 60 Months	Greater than 60 Months	
<i>(In Thousands)</i>						
Cash and cash equivalents	\$ 70,178	\$ 70,178	\$ -	\$ -	\$ -	\$ -
Corporate obligations	48,401	1,921	7,212	17,882	21,386	-
Foreign obligations	16,090	1,276	1,072	7,326	6,416	-
U.S. Treasury obligations	109,339	14,481	15,330	48,666	30,862	-
Certificates of Deposit	2,000	2,000	-	-	-	-
U.S. Agency obligations	30,032	456	4,283	8,921	16,372	-
Municipal	240	-	101	139	-	-
Alternative investments	136	-	-	-	-	136
Total	\$ 276,416	\$ 90,313	\$ 27,998	\$ 82,934	\$ 75,036	\$ 136

Investment Type	September 30, 2012	Remaining Maturity (In Months)				N/A
		12 Months or Less	13 Months to 24 Months	25 Months to 60 Months	Greater than 60 Months	
<i>(In Thousands)</i>						
Cash and cash equivalents	\$ 74,419	\$ 74,419	\$ -	\$ -	\$ -	\$ -
Corporate obligations	42,852	3,281	3,069	14,282	22,220	-
Foreign obligations	10,142	679	1,079	4,941	3,443	-
U.S. Treasury obligations	124,837	15,138	17,431	52,201	40,067	-
Certificates of Deposit	2,000	2,000	-	-	-	-
U.S. Agency obligations	10,018	694	2,467	6,462	395	-
Alternative investments	191	-	-	-	-	191
Total	\$ 264,459	\$ 96,211	\$ 24,046	\$ 77,886	\$ 66,125	\$ 191

The carrying amount of investments and assets whose use is limited are included in the District's combined balance sheets as follows:

	September 30	
	2013	2012
<i>(In Thousands)</i>		
Short term investments	\$ 27,174	\$ 22,128
Assets whose use is limited	249,242	242,331
Other long term investments	-	-
	<b>\$ 276,416</b>	<b>\$ 264,459</b>

For the years ended September 30, 2013 and 2012, net investment income (loss) is comprised of the following:

	<b>September 30</b>	
	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Interest and dividends, net of fees	\$ 3,712	\$ 4,334
Net unrealized gain (loss)	(5,866)	4,093
Net realized gain	845	1,047
	<u>\$ (1,309)</u>	<u>\$ 9,474</u>

**3. Accounts Receivable and Payable**

Patient accounts receivable and accounts payable (including accrued expenses) reported as current assets and liabilities by the District at September 30, 2013 and 2012 consisted of these amounts:

*Patient Accounts Receivable*

	<b>September 30</b>	
	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Receivable from patients and their insurance carriers	\$ 125,854	\$ 137,285
Receivable from Medicare	37,512	36,176
Receivable from Medicaid	14,631	9,428
Total patient accounts receivable	177,997	182,889
Less allowance for uncollectible amounts	(78,836)	(92,596)
Patient accounts receivable, net	<u>\$ 99,161</u>	<u>\$ 90,293</u>

*Accounts Payable and Accrued Expenses*

	<b>September 30</b>	
	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Payable to employees (including payroll taxes)	\$ 40,130	\$ 42,666
Payable to suppliers	20,486	15,217
Other	28,891	26,770
Total accounts payable and accrued expenses	<u>\$ 89,597</u>	<u>\$ 84,653</u>

**4. Capital Assets**

A summary of capital assets and the related accumulated depreciation for 2013 and 2012 is as follows:

	<b>Balance September 30, 2012</b>	<b>Additions</b>	<b>Transfers</b>	<b>Disposals</b>	<b>Balance September 30, 2013</b>
	<i>(In Thousands)</i>				
Land and land improvements	\$ 54,995	\$ 831	\$ 1,812	\$ (475)	\$ 57,163
Buildings and building fixtures	258,218	347	6,553	(126)	264,992
Fixed equipment	276,359	54	8,716	(871)	284,258
Major movable equipment	270,894	26,104	7,179	(17,120)	287,057
Equipment under capital lease obligations	15,314	2,293	-	-	17,607
Construction-in-progress	5,258	25,401	(24,260)	-	6,399
	<b>881,038</b>	<b>55,030</b>	<b>-</b>	<b>(18,592)</b>	<b>917,476</b>
Less accumulated depreciation	<b>(468,179)</b>	<b>(49,259)</b>	<b>-</b>	<b>18,382</b>	<b>(499,056)</b>
Capital assets, net	<b>\$ 412,859</b>	<b>\$ 5,771</b>	<b>\$ -</b>	<b>\$ (210)</b>	<b>\$ 418,420</b>

	<b>Balance September 30, 2011</b>	<b>Additions</b>	<b>Transfers</b>	<b>Disposals</b>	<b>Balance September 30, 2012</b>
	<i>(In Thousands)</i>				
Land and land improvements	\$ 54,600	\$ 25	\$ 370	\$ -	\$ 54,995
Buildings and building fixtures	256,387	83	1,748	-	258,218
Fixed equipment	268,508	4,459	4,318	(926)	276,359
Major movable equipment	266,992	15,858	7,308	(19,264)	270,894
Equipment under capital lease obligations	13,911	1,403	-	-	15,314
Construction-in-progress	6,850	12,152	(13,744)	-	5,258
	<b>867,248</b>	<b>33,980</b>	<b>-</b>	<b>(20,190)</b>	<b>881,038</b>
Less accumulated depreciation	<b>(439,957)</b>	<b>(46,777)</b>	<b>-</b>	<b>18,555</b>	<b>(468,179)</b>
Capital assets, net	<b>\$ 427,291</b>	<b>\$ (12,797)</b>	<b>\$ -</b>	<b>\$ (1,635)</b>	<b>\$ 412,859</b>

The District had outstanding commitments of approximately \$1.9 million at September 30, 2013, for completion of construction-in-progress and for the purchase of equipment. The projects are expected to be completed in May 2014.

5. **Long-Term Debt and Capital Lease Obligations**

*Series 2012A*

Hospital Revenue and Refunding bonds, Series 2012A were issued on July 19, 2012 in the amount of \$132.5 million consisting of: (i) \$27.8 million of serial bonds with interest rates ranging from 2.0% to 5.0% maturing in 2027; (ii) \$55.9 million of term bonds with an interest rate of 5.0% due in 2032; and (iii) \$48.8 million of term bonds with an interest rate of 5.0% due in 2037. Interest is payable semi-annually on October 15 and April 15. The bonds are secured by a pledge of the revenues of the District. The term bonds maturing in 2032 are subject to mandatory sinking fund redemption from 2028 to 2032 ranging in amounts from approximately \$8.3 million to \$12.7 million. The term bonds maturing in 2037 are subject to mandatory sinking fund redemption from 2033 to 2037 ranging in amounts from approximately \$8.9 million to \$10.7 million.

The Series 2012A Bonds were issued with a premium of approximately \$8.5 million of which approximately \$8.1 million remains unamortized at September 30, 2013.

The advance refunding of the Series 2008B and Series 2002 bonds from the issuance of Series 2012A Bonds resulted in losses on refunding of approximately \$4.5 million and \$0.9 million, respectively. This difference, reported in the accompanying combined financial statements as a reduction of long-term debt, is being charged as a component of interest expense through the years 2022 and 2032 using the straight line method, which approximates the effective interest method. At September 30, 2013, the total unamortized loss on refunding is approximately \$4.8 million.

*Series 2012B*

Hospital Revenue and Refunding bonds, Series 2012B were issued on July 19, 2012 in the amount of \$20.0 million. Interest is payable monthly at an annual fixed rate of 1.93%, commencing on August 15, 2012. Principal is paid annually on April 15, commencing on April 15, 2013. The bonds are secured by a pledge of the revenues of the District. The Series 2012B bonds mature on April 15, 2023.

The advance refunding of the Series 2008C from the issuance of the Series 2012B Bonds resulted in a loss on refunding of approximately \$0.4 million. This difference, reported in the accompanying combined financial statements as a reduction of long-term debt, is being charged as a component of interest expense through the year 2023 using the straight line method, which approximates the effective interest method. At September 30, 2013, the unamortized loss on refunding is approximately \$0.3 million.

*Series 2009*

Hospital Revenue bonds, Series 2009 were issued on May 21, 2009 in the amount of \$15.0 million. The Series 2009 bonds are term bonds bearing interest at an annual rate of 4.11%. Principal and interest installments are payable semi-annually on October 15 and April 15, commencing October 15, 2009. The bonds are secured by a pledge of the revenues of the District. The Series 2009 bonds mature on April 15, 2019.

*Series 2008A*

Hospital Revenue and Refunding bonds, Series 2008A were issued on June 25, 2008 in the amount of \$49.5 million consisting of: (i) \$23.3 million of serial bonds with interest rates ranging from 4.0% to 5.25% maturing in 2022; (ii) \$10.3 million of term bonds with an interest rate of 5.25% due in 2025; and (iii) \$15.9 million of term bonds with an interest rate of 4.5% due in 2027. Interest is payable semi-annually on October 15 and April 15. The bonds are secured by a pledge of the revenues of the District. The term bonds maturing in 2025 are subject to mandatory sinking fund redemption from 2023 to 2025 ranging in amounts from approximately \$1.1 million to \$4.7 million. The term bonds maturing in 2027 are subject to mandatory sinking fund redemption for 2026 and 2027 in the amount of approximately \$7.8 million and \$8.1 million, respectively.

The Series 2008A Bonds were issued with a premium of approximately \$0.7 million of which approximately \$0.5 million remains unamortized at September 30, 2013.

*Series 2008B*

Hospital Revenue and Refunding bonds, Series 2008B were issued on June 25, 2008 in the amount of \$90.8 million. The Series 2008B are variable rate bonds initially bearing interest determined weekly by the remarketing agent under prevailing market conditions. In accordance with the Series 2008B bond indenture, the District converted the weekly interest rate to a long-term variable interest rate as defined by the bond indenture and interest is payable semi-annually on October 15 and April 15. The bonds are secured by a pledge of the revenues of the District and are subject to mandatory sinking fund redemption annually from 2010 to 2037 ranging in amounts from approximately \$0.1 million to \$8.9 million. The Series 2008B Bonds were refunded with the issuance of the Series 2012A Bonds.

A portion of the proceeds from the issuance of the Series 2008A and 2008B bonds was deposited in an irrevocable trust with an escrow agent to fully refund the Series 1997A bonds and refund approximately \$31.4 million of the Series 1997B bonds. The refunding of the Series 1997A&B bonds resulted in a loss on refunding of approximately \$6.2 million. This difference, reported in the accompanying combined financial statements as a deduction from long-term debt, is being charged as a component of interest expense through the year 2022 using the straight line method, which approximates the effective interest method. At September 30, 2013, the unamortized loss on refunding is approximately \$3.3 million.



A portion of the proceeds from the issuance of the Series 2008B bonds refunded in advance of their maturity approximately \$18.9 million of the Series 2002 bonds. The partial advance refunding of the Series 2002 bonds resulted in a loss on refunding of approximately \$0.2 million. This difference, reported in the accompanying combined financial statements as a reduction of long-term debt, is being charged as a component of interest expense through the year 2032 using the straight line method, which approximates the effective interest method. At September 30, 2013, the unamortized loss on refunding is approximately \$0.1 million.

*Series 2008C*

Hospital Revenue and Refunding bonds, Series 2008C were issued in the amount of \$20.0 million on June 25, 2008. The Series 2008C are variable rate bonds initially bearing interest determined weekly by the remarketing agent under prevailing market conditions. In accordance with the Series 2008C bond indenture, the District converted the weekly interest rate to a long-term variable interest rate as defined by the bond indenture and interest is payable semi-annually on October 15 and April 15. The bonds are secured by a pledge of the revenues of the District and are subject to mandatory sinking fund redemption annually from 2009 to 2023 ranging in amounts from approximately \$0.6 million to \$4.8 million. The Series 2008C Bonds were refunded with the issuance of the Series 2012B Bonds.

A portion of the proceeds of the Series 2008C bonds was deposited in an irrevocable trust with an escrow agent to provide future debt service payments on the Series 1998 bonds. The advance refunding of the Series 1998 bonds resulted in a loss on refunding of approximately \$0.4 million. This difference, reported in the accompanying combined financial statements as a deduction from long-term debt, is being charged as a component of interest expense through the year 2023 using the straight-line method, which approximates the effective interest method. At September 30, 2013, the unamortized loss on refunding is approximately \$0.3 million.

*Series 2008D*

Hospital Revenue and Refunding bonds, Series 2008D in the amount of \$32.6 million were issued on July 30, 2008 consisting of: (i) \$16.4 million of serial bonds with interest rates ranging from 4.0% to 5.0% maturing in 2018; (ii) \$4.0 million of term bonds with an interest rate of 5.25% due in 2020; (iii) \$4.5 million of term bonds with an interest rate of 5.25% due in 2022; and (iv) \$7.7 million of term bonds with an interest rate of 4.5% due in 2025. Interest is payable semi-annually on October 15 and April 15. The bonds are secured by a pledge of the revenues of the District. The term bonds maturing in 2020 are subject to mandatory sinking fund redemption for 2019 and 2020 in the amount of \$2.0 million and \$2.2 million, respectively. The term bonds maturing in 2022 are subject to mandatory sinking fund redemption for 2021 and 2022 in the amount of approximately \$2.2 million and \$2.3 million, respectively.

A portion of the proceeds of the Series 2008D bonds was deposited in an irrevocable trust with an escrow agent to provide future debt service payments on the Series 1995 bonds. The refunding of the Series 1995 bonds resulted in a loss on refunding of approximately \$1.4 million. This difference, reported in the accompanying combined financial statements as a deduction from long-term debt, is being charged as a component of interest expense through the year 2025 using the straight line method, which approximates the effective interest method. At September 30, 2013, the unamortized loss on refunding is approximately \$1.0 million.

The Series 2008D bonds were issued with a premium of approximately \$0.4 million of which approximately \$0.3 million remains unamortized at September 30, 2013.

*Series 2002*

Hospital Revenue and Refunding Bonds, Series 2002 in the amount of \$49.5 million were issued on May 15, 2002, consisting of: (i) \$19.8 million of serial bonds with interest rates ranging from 3.5% to 5.5% maturing in 2022; (ii) \$2.2 million of term bonds with an interest rate of 5.25% due in 2027; and (iii) \$27.5 million of term bonds with an interest rate of 5.25% due in 2032. Interest is payable semi-annually on October 15 and April 15. The Series 2002 are secured by a pledge of revenues of the District. The Series 2002 Bonds were refunded with the issuance of the Series 2012A Bonds.

Trust agreements for Series 2012 A and B; Series 2009; and Series 2008 A and D contain certain restrictive covenants which, among other matters, require the District to maintain its rates, fees and charges to the extent necessary in order for the District to maintain certain earnings levels as defined. In addition, the Trust agreements name banks as Trustees to receive, transfer and disburse all monies.

*Interest Rate Swap Agreements*

On June 25, 2008, the District entered into an interest rate swap agreement on the notional amount of \$90.8 million relating to the variable rate Hospital Revenue and Refunding Bond Series 2008B. The District is the fixed rate payer and the swap agreement fixes the interest rate on the Series 2008B bonds at 3.50% through April 2037. This swap was terminated on July 19, 2012 as part of the Series 2008B advance refunding by the Series 2012A bonds.

On June 25, 2008, the District entered in an interest rate swap agreement on the notional amount of \$20.0 million relating to the variable rate Hospital Revenue and Refunding Bonds Series 2008C. The District is the fixed rate payer and the swap agreement fixes the interest rate on the Series 2008C bonds at 3.28% through April 2023. This swap was terminated on July 19, 2012 as part of the Series 2008C advance refunding by the Series 2012B bonds.

In accordance with the provisions of GASB No. 53, *Accounting and Financial Reporting for Derivative Instruments*, since these interest rate swap agreements were evaluated by the District as ineffective in the first reporting period of the interest rate swap agreements, fiscal 2008, the District has recorded the change in fair market value of the interest rate swaps as a component of nonoperating revenues and expenses in the combined statements of revenues, expenses, and changes in net position. As of the year ended September 31, 2012, the combined statements of revenues and expenses include a loss of approximately \$3.0 million related to the change in fair value of the interest rate swap agreements.

*Loan Agreements*

On December 29, 2008, the District entered into a promissory note agreement with G.B. Hodge, MD for \$0.4 million with a fixed interest rate of 6.00%. The note is unsecured. The proceeds of the note were used to purchase the Hodge building and related land. The note is being repaid over six years in annual installments of interest and principal, commencing December 29, 2009, and will mature on December 29, 2014. Approximately \$0.1 million of the principal balance remained outstanding at September 30, 2013.

On August 23, 2005, the District entered into a loan agreement with a financial institution that provided \$5,000,000 with a fixed interest rate of 5.25%. The loan is unsecured. The proceeds of the loan were used to purchase a medical office and condo suite at VH. The loan is being repaid over ten years in monthly installments of interest and principal and will mature in 2015. Approximately \$1.2 million of the principal balance remained outstanding at September 30, 2013.

Future principal and interest payments, excluding the unamortized losses on advance refundings of the Series 1992A&B, 1995, 1997A&B, 1998, 2002, 2008B&C, the unamortized bond discount and the unamortized bond premium, under the District's long-term debt agreements are:

<b>Year Ending September 30,</b>	<b>Principal Payments</b>	<b>Interest Payments</b>	<b>Total Debt Service</b>
	<i>(In Thousands)</i>		
2014	8,406	10,529	18,935
2015	8,602	10,219	18,821
2016	8,312	9,892	18,204
2017	8,630	9,579	18,209
2018	8,948	9,260	18,208
2019 – 2023	43,149	40,403	83,552
2024 – 2028	50,570	30,940	81,510
2029 – 2033	53,660	21,168	74,828
2034 – 2037	39,955	5,113	45,068
	<u>\$ 230,232</u>	<u>\$ 147,403</u>	<u>\$ 377,335</u>

Activity related to long-term debt excluding capital lease obligations for the years ended September 30, 2013 and 2012, is summarized as follows (in thousands):

	<b>2012</b>	<b>Additions</b>	<b>Reductions</b>	<b>2013</b>	<b>Amounts Due Within 1 Year</b>
	<i>(In Thousands)</i>				
Hospital Revenue and Refunding Bonds, Series 2012A	\$ 132,520	\$ -	\$ (2,710)	\$ 129,810	\$ 1,445
Hospital Revenue and Refunding Bonds, Series 2012B	19,977	-	(1,158)	18,819	1,218
Hospital Revenue Bonds, Series 2009	11,081	-	(1,396)	9,685	1,454
Hospital Revenue and Refunding Bonds, Series 2008A	47,610	-	(1,950)	45,660	1,985
Hospital Revenue and Refunding Bonds, Series 2008D	26,520	-	(1,555)	24,965	1,615
Notes Payable	1,899	-	(606)	1,293	689
Add: Unamortized bond premium	9,330	-	(427)	8,903	-
Less: Unamortized refunding loss	11,108	-	(1,078)	10,030	-
Unamortized bond discount	87	-	(9)	78	-
<b>Total</b>	<b>\$ 237,742</b>	<b>\$ -</b>	<b>\$ ( 8,715)</b>	<b>\$ 229,027</b>	<b>\$ 8,406</b>

**SPARTANBURG REGIONAL HEALTH  
SERVICES DISTRICT, INC.**

**Notes to the Combined Financial Statements, continued**

	<b>2011</b>	<b>Additions</b>	<b>Reductions</b>	<b>2012</b>	<b>Amounts Due Within 1 Year</b>
	<i>(In Thousands)</i>				
Hospital Revenue and Refunding Bonds, Series 2012A	\$ -	\$ 132,520	\$ -	\$ 132,520	\$ 2,710
Hospital Revenue and Refunding Bonds, Series 2012B	-	19,977	-	19,977	1,158
Hospital Revenue Bonds, Series 2009	12,422	-	(1,341)	11,081	1,396
Hospital Revenue and Refunding Bonds, Series 2008A	49,530	-	(1,920)	47,610	1,950
Hospital Revenue and Refunding Bonds, Series 2008B	90,520	-	(90,520)	-	-
Hospital Revenue and Refunding Bonds, Series 2008C	18,105	-	(18,105)	-	-
Hospital Revenue and Refunding Bonds, Series 2008D	28,035	-	(1,515)	26,520	1,555
Hospital Revenue and Refunding Bonds, Series 2002	23,790	-	(23,790)	-	-
Notes Payable	2,519	-	(620)	1,899	656
Add : Unamortized bond premium	929	8,525	(124)	9,330	-
Less: Unamortized refunding loss	8,281	3,648	(821)	11,108	-
Unamortized bond discount	313	-	(226)	87	-
Total	<u>\$ 217,256</u>	<u>\$ 157,374</u>	<u>\$ ( 136,888)</u>	<u>\$ 237,742</u>	<u>\$ 9,425</u>

*Capital Lease Obligations*

Equipment under capital lease obligations is included in major movable equipment and accumulated depreciation. The carrying value and related accumulated depreciation at September 30, 2013 are approximately \$12.4 million and \$7.3 million, respectively, and at September 30, 2012 are approximately \$8.4 million and \$5.8 million, respectively. The assets recorded under capital leases are pledged as collateral for the capital lease obligations.

Activity related to capital lease obligations for the years ended September 30, 2013 and 2012, is summarized as follows (in thousands):

	<b>2012</b>	<b>Additions</b>	<b>Reductions</b>	<b>2013</b>	<b>Amounts Due Within 1 Year</b>
	<i>(In Thousands)</i>				
Capital lease obligations	\$ <u>8,650</u>	\$ <u>2,293</u>	\$ <u>(3,108)</u>	\$ <u>7,835</u>	\$ <u>3,632</u>
	<b>2011</b>	<b>Additions</b>	<b>Reductions</b>	<b>2012</b>	<b>Amounts Due Within 1 Year</b>
	<i>(In Thousands)</i>				
Capital lease obligations	\$ <u>10,100</u>	\$ <u>1,403</u>	\$ <u>(2,853)</u>	\$ <u>8,650</u>	\$ <u>3,016</u>

The District leases certain equipment used in its operations under capital leases with interest rates varying from 4.62% to 7.19% that have noncancellable terms in excess of one year. Future minimum capital lease payments as of September 30, 2013 are as follows:

<b>Fiscal Year</b>	<b>Capital Leases</b>
	<i>(In Thousands)</i>
2014	\$ 3,928
2015	2,886
2016	694
2017	456
2018	338
Thereafter	57
Total minimum lease payments	8,359
Less amounts representing interest	(524)
Present value of minimum lease payments	7,835
Less current portion	(3,632)
	<u>\$ 4,203</u>

6. **Net Patient Service Revenues**

Net patient service revenues for the years ended September 30, 2013 and 2012 consisted of the following:

	<b>2013</b>	<b>2012</b>
	<i>(In Thousands)</i>	
Gross patient charges at established rates, including charges foregone for charity care	<b>\$ 2,251,651</b>	\$ 2,069,330
Deductions:		
Contractual adjustments	<b>(1,349,575)</b>	(1,199,817)
Charity care provided at established billing rates	<b>(80,671)</b>	(81,629)
Provision for bad debts	<b>(61,853)</b>	(68,359)
Net patient service revenues	<b><u>\$ 759,552</u></b>	<u>\$ 719,525</u>

The District has agreements with third-party payors for health care services that provide for payments at amounts different from established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. A summary of the payment arrangements with major third-party payors follows:

- **Medicare:** Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Outpatient services are reimbursed under a prospective payment system called the Ambulatory Payment Classification System (“APCs”). Inpatient non-acute services and defined capital and medical education costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The District is reimbursed for cost-reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the District and audits thereof by the Medicare fiscal intermediary. SMC’s Medicare cost reports have been audited by the Medicare fiscal intermediary through 2011; however, final settlements have only been determined through 2009. The Medicare cost reports for SHRC and VH have been audited and final settlements have been determined through 2011 and 2009, respectively. Approximately 39% of the District’s net patient service revenues for both the years ended September 30, 2013 and 2012 were derived from Medicare.
- **Medicaid:** Inpatient reimbursement is based upon prospectively determined rates per discharge. Outpatient services rendered to Medicaid program beneficiaries are reimbursed under various reimbursement methodologies. The District is reimbursed for outpatient services at tentative rates with final settlement determined after submission of annual cost reports by the District and audits thereof by the fiscal intermediary. The Medicaid cost reports for SMC and VH have been audited by the Medicaid fiscal intermediary through 2010. The Medicaid cost reports for SHRC have been audited by the Medicaid fiscal intermediary through 2006. Approximately 7% and 8% of the

District's net patient service revenues for the years ended September 30, 2013 and 2012, respectively, were derived from Medicaid.

The District receives payments for serving a disproportionately high volume of Medicaid patients. The District received approximately \$20.7 million related to the Medicaid disproportionate share program for the year ended September 30, 2013. There was no related receivable related to the Medicaid disproportionate share program for the year ended September 30, 2013. The District received approximately \$23.1 million and had a receivable included in other current assets of approximately \$0.2 million related to the Medicaid disproportionate share program for the year ended September 30, 2012. These amounts have been included in net patient service revenues. South Carolina requires that the District pay a Hospital Tax that is used as matching funds for the Medicaid disproportionate share program. The amount of Hospital Tax paid by the District was approximately \$14.7 million and \$14.6 million for the years ended September 30, 2013 and 2012, respectively. The Hospital Tax is included as a fiscal and administrative expense.

- Other: The District has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The bases for payments to the District under these agreements include prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. The District believes that it is in compliance with all applicable laws and regulations. Compliance with such laws and regulations can be subject to further government review and interpretation as well as significant regulatory action including fines, penalties and exclusion from the Medicare and Medicaid programs. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The net patient service revenue increased by approximately \$6.9 million and \$7.9 million for the years ended September 30, 2013 and 2012, respectively, due to changes in allowances for prior years' cost reports.

**HITECH Funding for Meaningful Use of Electronic Health Records ("EHR")** - The District recognizes revenue for incentives earned under the Medicare and Medicaid programs in the period in which it is reasonably assured that it will comply with the applicable EHR meaningful use requirements. Incentive revenues are recognized ratably over the applicable meaningful use demonstration period. Incentive payments received under the Medicare program include a discharge-related portion, which is calculated by the Centers for Medicare & Medicaid Services ("CMS") based on the District's most recently filed cost report. Such amounts are subject to adjustment at the time of settling the 12-month cost report for the District's fiscal year that begins after the beginning of the payment year. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.



The District achieved compliance with meaningful use requirements under the Medicare program during fiscal years 2013 and 2012 and, accordingly, recognized other operating revenues of approximately \$2,698,000 and \$3,597,000 in the accompanying combined statement of revenues, expenses, and changes in net position for the years ended September 30, 2013 and 2012, respectively. The District achieved compliance with meaningful use requirements under the Medicaid program during fiscal years 2013 and 2012 and, accordingly, recognized other operating revenues of approximately \$1,104,000 and \$1,380,000 in the accompanying combined statement of revenues, expenses, and changes in net position for the years ended September 30, 2013 and 2012, respectively.

**7. Retirement Plans**

*Retirement System*

The District contributes to the South Carolina Retirement System (“SCRS”). SCRS is a cost-sharing multiple-employer defined benefit pension plan administered by South Carolina Retirement Systems, a Division of the State Budget and Control Board. The gross wages for all District employees was approximately \$337.7 million and \$322.0 million, respectively, for the years ended September 30, 2013 and 2012. The gross wages for District employees covered by the SCRS for the years ended September 30, 2013 and 2012 was approximately \$273.8 million and \$271.0 million, respectively or approximately 81% and 84%, respectively, of total District payroll in 2013 and 2012. The contribution from the District for the years ended September 30, 2013 and 2012 was approximately \$28.6 million and \$26.2 million, respectively. The District’s 2013 contributions represented approximately 1.8% of total contributions to SCRS.

Under SCRS, employees who retire at or after age sixty-five (65) or have twenty eight (28) years of service are entitled to an annual retirement benefit, payable monthly for life equal to 1.82% of their final compensation times years of credited service. Benefits are fully vested on reaching five (5) years of earned service. Employees who retire at or after age sixty-five (65) or whose age plus years of service total at least ninety (90) years are also entitled to an annual retirement benefit, payable monthly for life equal to 1.82% of their final compensation times years of credited service. Benefits are fully vested on reaching eight (8) years of earned service. Vested employees may retire at or after age fifty-five (55) with at least twenty-five (25) years of service and receive reduced retirement benefits. Vested employees may also retire at or after age sixty (60) and receive reduced retirement benefits. SCRS also provides death and disability benefits. Benefits are established by state statute. A Comprehensive Annual Financial Report containing financial statements and required supplementary information of SCRS is issued and publicly available by writing the South Carolina Retirement System, P.O. Box 11960, Columbia, SC 29211-1960 or at [www.retirementsc.gov](http://www.retirementsc.gov).

The employee and employer contribution rates are actuarially determined for SCRS. Covered employees are required by state statute to contribute 7.0% of their total earnings. The District is required to contribute 10.45% of earnable compensation.

The accrued liability is a standardized disclosure measure of the actuarial present value of the projected benefits of each individual allocated on a level basis over the earnings or service of the individual between entry age and assumed exit age(s). The measure is intended to help users assess SCRS's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems. SCRS does not make separate measurements of assets and benefits payable for individual employers. The unfunded accrued liability at July 1, 2012, the most recent valuation date for retired and active members, determined through an actuarial valuation performed as of that date, was approximately \$13.9 billion. Ten-year historical trend information showing SCRS's progress in accumulating sufficient assets to pay benefits when due is presented in the June 30, 2013 Component Unit Comprehensive Annual Financial Report issued by the SCRS.

*Alternative Retirement Plans*

Employees who are not members of the SCRS are eligible for alternative retirement plans, which include a 401(k) plan and a 457(b) plan. These plans are provided through the South Carolina Deferred Compensation Program. Employees can contribute as much as the maximum allowed by the Internal Revenue Service ("IRS") and employees age 50 or older can contribute an additional amount per year under the "catch-up" provisions provided by the IRS. There is no District match associated with the 401(k) plan. Upon joining the 457(b) plan, employees receive an automatic membership payment of 1 percent of their base pay, which vests upon completion of the first year of plan membership. The District will match 100% of the first 3% of the pay that each employee places in the plan. Vesting of the 3 percent District match occurs after three full years of participation in the plan. Employee contributions are always 100 percent vested.

**8. Commitments and Contingencies**

**Operating Leases**

The District leases certain equipment and facilities used in its operations under operating leases that have noncancellable terms in excess of one year. Future minimum lease payments as of September 30, 2013 under leases classified as operating leases are as follows:

<u>Fiscal Year</u>	<u>Operating Leases</u> (In Thousands)
2014	\$ 2,860
2015	1,583
2016	1,113
2017	380
2018	260
2019 – 2023	483
Total minimum lease payments	<u>\$ 6,679</u>

Lease expense relating to operating leases was approximately \$4.1 million and \$6.1 million in 2013 and 2012, respectively.

### **Litigation**

The District is involved in litigation arising in the course of business. After consultation with legal counsel, management estimates that any potential exposure related to these matters is adequately funded by the District and will be resolved without material adverse effect on the District's combined financial position.

### **Professional Malpractice Liability Insurance**

The District is self-insured for professional and general liability insurance coverage. The self-insurance program is responsible for payment of all claims and costs not to exceed \$600,000 on an individual case basis. A liability of \$12.8 million has been established for payment of all claims reported as of September 30, 2013 including an accrual of estimated incurred but not reported claims. Stop-loss or excess liability insurance is in effect for any single claim in excess of \$600,000 or in the aggregate of \$10,000,000.

At September 30, 2013, management is aware of no claims that might lead to significant amounts not adequately funded by the District or covered by insurance that would have a material adverse effect on the combined financial position of the District.

### **Self-Insurance Plan**

The District's health insurance plan (Plan) is a self-insured plan that provides certain benefits for covered employees. The employee pays a monthly premium and the Plan will pay for certain medical expenses, as defined in the Plan document. The District has an accrual of approximately \$3.6 million for estimated incurred but not reported claims as of September 30, 2013.

### **Workers' Compensation**

The District participates in a workers' compensation self-insurance pool operating as Palmetto Hospital Trust (PHT). Beginning in January 2008, the District elected to accept legal and financial responsibility for a per claim deductible of \$500,000 in exchange for a deductible credit against its deposit premium. In order to facilitate the efficient administration of the program and the payment of claims and expenses, PHT from time to time will advance funds on behalf of the District equal to the deductible obligation of the District.

**Industry**

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, governmental health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Management believes the District is in compliance with fraud and abuse as well as other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

**9. Related Party Transactions**

The amounts due from Regional HealthPlus, LLC ("RHP") are approximately \$2.1 million and \$2.4 million as of September 30, 2013 and 2012, respectively, included in other current assets on the combined balance sheets. The amounts due to Regional HealthPlus, LLC ("RHP") are approximately \$1.2 million and \$1.1 million as of September 30, 2013 and 2012, respectively, included in accounts payable on the combined balance sheets. The District pays operating expenses for RHP for which RHP reimburses the District.

The District pays substantially all the operating expenses on behalf of Spartanburg Regional Healthcare System Foundation (the "Foundation"). The District paid approximately \$1,200,000 and \$1,402,000 in 2013 and 2012, respectively, on behalf of the Foundation. The Foundation issues grants to the District with approximately \$498,000 and \$1,565,000 granted during 2013 and 2012, respectively. The grant revenue is included in nonoperating revenues.

The District has entered into an agreement to lease medical office space to the Ambulatory Surgery Center of Pelham, LLC with monthly payments of approximately \$55,000. Future lease revenue will be approximately \$658,000 per year through September 30, 2015, when the lease expires.

**10. Fair Value of Financial Instruments**

The fair value of the Series 2008A, 2008D, 2009, 2012A, and 2012B bonds were estimated using discounted cash flows based on market yield on comparable bonds for a similar type of borrowing arrangement. The carrying amount approximates fair value for the other long-term notes payable. The carrying values of the District's long-term debt at September 30, 2013 and 2012 are approximately \$229.0 million and \$237.7 million, respectively. The fair values are approximately \$234.0 million and \$256.0 million, respectively.

11. **Unconditional Promises to Give**

During 2012, the District signed agreements for unconditional promises to give totaling \$5.6 million. As of September 30, 2013, \$2.2 million was paid by the District. The unamortized discount on the pledges as of September 30, 2013 was approximately \$0.4 million. Future payments, not including unamortized discount, as of September 30, 2013 are as follows:

<b>Fiscal Year</b>	<b>Promises to Give</b>
	<i>(In Thousands)</i>
2014	\$ 1,400
2015	1,000
2016	1,000
Total	<u>\$ 3,400</u>

12. **Subsequent Events**

Subsequent events have been evaluated through January 10, 2014, which is the date the combined financial statements were available to be issued.