KPMG

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidated Financial Statements and Supplementary Information

June 30, 2018 and 2017

(With Independent Auditors' Report Thereon)

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

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KPMG LLP
750 East Pratt Street, 18th Floor
Baltimore, MD 21202

Independent Auditors' Report

The Board of Trustees
Sheppard and Enoch Pratt Foundation, Inc.:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Sheppard and Enoch Pratt Foundation, Inc. and its subsidiaries (the Company), which comprise the consolidated balance sheets as of June 30, 2018 and 2017, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sheppard and Enoch Pratt Foundation, Inc. and its subsidiaries as of June 30, 2018 and 2017, and the results of their operations, changes in net assets and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information in Schedules 1 through 3 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

October 17, 2018

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidated Balance Sheets

June 30, 2018 and 2017

Assets		**2018**	**2017**
Current assets:			
Cash and cash equivalents	$	57,539,767	76,277,561
Investments limited or restricted as to use		2,193,109	865,824
Accounts receivable, net		31,809,978	32,366,167
Prepaid expenses and other current assets		15,936,785	11,227,367
Total current assets		107,479,639	120,736,919
Investments limited or restricted as to use, less current portion		293,160,015	192,272,718
Notes receivable		1,745,868	1,877,631
Third-party payor settlements receivable		6,722,505	9,755,493
Property and equipment, net		233,229,587	215,912,516
Other assets		2,114,063	4,281,301
Total assets	$	644,451,677	544,836,578
Liabilities and Net Assets			
Current liabilities:			
Note payable	$	—	12,900,000
Current maturities of long-term debt		5,620,490	5,005,333
Current portion of obligations under capital leases		561,029	610,932
Accounts payable		9,324,925	7,055,763
Accrued salaries, wages and employee benefits		23,611,871	22,723,817
Self-insurance liabilities		4,353,612	3,950,703
Other accrued expenses		5,030,048	3,938,653
Total current liabilities		48,501,975	56,185,201
Long-term liabilities:			
Long-term debt, less current portion		187,664,834	92,893,443
Obligations under capitalized leases, less current portion		5,296,855	5,839,691
Self-insurance liabilities		7,535,696	7,386,614
Accrued pension liabilities		22,246,566	32,687,089
Other long-term liabilities		3,518,746	3,313,228
Total liabilities		274,764,672	198,305,266
Net assets:			
Unrestricted		342,239,494	325,785,684
Temporarily restricted		23,512,452	16,836,253
Permanently restricted		3,935,059	3,909,375
Total net assets		369,687,005	346,531,312
Total liabilities and net assets	$	644,451,677	544,836,578

See accompanying notes to consolidated financial statements.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidated Statements of Operations

Years ended June 30, 2018 and 2017

	2018	2017
Unrestricted revenues, gains, and other support:		
Patient service revenue (net of allowances and discounts)	$ 151,332,053	146,775,829
Residential and educational service revenue (net of allowances)	162,552,367	161,266,392
Total net service revenue	313,884,420	308,042,221
Less provision for bad debts	3,389,079	1,990,523
Net service revenue less provision for bad debts	310,495,341	306,051,698
Net assets released from restrictions used for operations	1,189,557	1,367,441
Other revenue	58,866,400	60,441,512
Total unrestricted revenues, gains, and other support	370,551,298	367,860,651
Expenses:		
Salaries and wages	222,689,158	216,823,012
Employee benefits	48,925,569	49,402,450
Expendable supplies	18,336,325	18,287,982
Purchased services	53,052,331	47,849,285
Interest	3,554,180	2,744,683
Repairs and minor alterations	10,518,490	9,297,754
Depreciation and amortization	18,978,249	18,726,251
Loss on disposal of assets, net	202,168	220,448
Total expenses	376,256,470	363,351,865
Operating (loss) income	(5,705,172)	4,508,786
Other income (expense):		
Investment income	2,114,843	1,717,523
Realized gain (loss) on investments, net	5,014,038	(1,637,695)
Change in unrealized gain on investments, net	3,563,005	20,383,687
Other	69,377	1,430,329
Total other income	10,761,263	21,893,844
Excess of revenues over expenses	5,056,091	26,402,630
Other changes in net assets:		
Net assets released from restrictions used for purchases of property and equipment	207,120	199,551
Pension liability adjustment	8,639,418	12,020,415
Capital grants	2,551,181	434,388
Increase in unrestricted net assets	$ 16,453,810	39,056,984

See accompanying notes to consolidated financial statements.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2018 and 2017

	2018	2017
Unrestricted net assets:		
Excess of revenues over expenses	$ 5,056,091	26,402,630
Other changes in net assets:		
Net assets released from restrictions used for purchases of property and equipment	207,120	199,551
Pension liability adjustment	8,639,418	12,020,415
Capital grants and other	2,551,181	434,388
Increase in unrestricted net assets	16,453,810	39,056,984
Temporarily restricted net assets:		
Gifts and grants	7,713,018	3,318,280
Investment income	83,504	65,326
Net realized gain (loss) on investments	160,731	(49,727)
Net unrealized gain on investments	115,623	616,318
Net assets released from restrictions for operations	(1,189,557)	(1,367,441)
Net assets released from restrictions for purchases of property and equipment	(207,120)	(199,551)
Reclassification of net assets	—	200,000
Increase in temporarily restricted net assets	6,676,199	2,583,205
Permanently restricted net assets:		
Gifts	17,576	11,600
Investment gain	8,108	13,315
Reclassification of net assets	—	(200,000)
Increase (decrease) in permanently restricted net assets	25,684	(175,085)
Increase in net assets	23,155,693	41,465,104
Net assets, beginning of year	346,531,312	305,066,208
Net assets, end of year	$ 369,687,005	346,531,312

See accompanying notes to consolidated financial statements.

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended June 30, 2018 and 2017

	2018	2017
Cash flows from operating activities:		
Increase in net assets	$ 23,155,693	41,465,104
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	18,978,249	18,726,251
Pension liability adjustment	(8,639,418)	(12,020,415)
Provision for doubtful accounts	3,389,079	1,990,523
Gifts and grants, net	(6,541,037)	(1,962,439)
Net realized (gain) loss on investments	(5,174,769)	1,687,422
Net unrealized gain on investments	(3,678,628)	(21,000,005)
Restricted investment income on restricted net assets	(91,612)	(78,641)
Capital grant and loss on disposal of assets	(2,349,013)	(213,940)
Increase in accounts receivable, net	(2,832,890)	(3,272,956)
Increase in prepaid expenses and other current assets	(3,191,694)	(398,843)
Decrease in third-party payor settlements receivable	3,032,988	1,114,026
Increase (decrease) in accounts payable, accrued expenses and other	3,099,941	(5,229,256)
Increase (decrease) in self-insurance liabilities	551,991	(604,326)
(Decrease) increase in accrued pension liability	(1,801,105)	717,541
Net cash provided by operating activities	17,907,775	20,920,046
Cash flows from investing activities:		
Purchases of property and equipment	(35,962,891)	(14,063,770)
Decrease (increase) in other assets	642,222	(219,463)
Proceeds from sale of property and equipment	86,016	273,204
Decrease in notes receivable	131,763	131,763
Purchases of alternative investments	(6,298,172)	(7,107,132)
Sales of alternative investments	5,532,388	2,804,231
Establishment of 2017 construction funds	(100,000,128)	—
Decrease (increase) in investments limited or restricted as to use, net	10,918,592	(7,557,735)
Net cash used in investing activities	(124,950,210)	(25,738,902)
Cash flows from financing activities:		
Proceeds from debt and other liabilities	178,748,000	17,025,341
Payment of note payable	(12,900,000)	—
Payment of long-term debt principal	(83,000,346)	(9,595,539)
Payment on capital lease obligations	(610,931)	(598,229)
Payment of deferred financing costs	(429,720)	(313,500)
Capital grants and advances	2,714,181	434,388
Gifts and grants, net	3,783,457	1,962,439
Net cash provided by financing activities	88,304,641	8,914,900
Net (decrease) increase in cash and cash equivalents	(18,737,794)	4,096,044
Cash and cash equivalents, beginning of year	76,277,561	72,181,517
Cash and cash equivalents, end of year	$ 57,539,767	76,277,561

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

(a) Organization

Sheppard and Enoch Pratt Foundation, Inc. (Foundation or the Company), a not-for-profit, nonstock Company, was organized on June 15, 1984 to engage in activities necessary to provide mental health services to the public through the planning and implementation of programs provided by its various subsidiaries. Subsidiary companies, controlled by Foundation, include Sheppard Pratt Health System, Inc. (Health System), Sheppard Pratt Physicians, P.A. (Physicians), Sheppard Pratt Investment, Inc. (Investment Company), Alliance, Inc. (Alliance), Mosaic Community Services, Inc. (Mosaic), Way Station, Inc. (Way Station), Family Services, Inc. (Family Services), and Sheppard Pratt Preferred Resources, Inc. (Resources).

On July 1, 2016, Mosaic became the sole member of Alliance. No consideration was exchanged in this transaction. The Company accounted for such transaction using the “as-if” pooling of interests method at carrying value since both entities are under common control.

Health System is a not-for-profit, nonstock company that operates two inpatient hospitals, day hospitals, residential and educational services for children and adolescents, and outpatient programs.

Physicians is a professional company of licensed medical professionals organized on July 1, 1985 exclusively to carry out the charitable, educational and scientific purposes of Foundation and its affiliates. The common stock of Physicians is held by several individuals who are employed by a member of Foundation, Health System, or Physicians and are subject to the terms of a stock agreement. Under the terms of the agreement, the stockholders are required to consult with Foundation regarding its views on any matter with respect to which the stockholder is entitled to vote, and the stockholders may not transfer shares (by sale or gift) without the permission of Foundation. The stock agreement does not allow for the stockholders to receive dividends or any other benefit for having held the stock. If the stockholders cease to be employed by Foundation, Health System, or Physicians, Physicians shall require the stockholders to sell and transfer all of the stock such stockholder owns to a person designated by Foundation. The purchase price for each share of stock of the Company is $1 per share.

Investment Company is a not-for-profit, nonstock company that manages the investments of certain subsidiaries.

On December 8, 2017, Foundation formed Sheppard Pratt Properties, LLC. The sole member of the company is Sheppard and Enoch Pratt Foundation, Inc., and its established purpose is to acquire, own, operate, lease and manage properties on behalf of Sheppard and Enoch Pratt Foundation, Inc. and its affiliates. During 2018, certain assets and rental activity relating to a warehouse rental property acquired in Elkridge, Maryland was transferred from the Investment Company to Sheppard Pratt Properties, LLC.

Mosaic, Way Station and Family Services (collectively, the Affiliates) are not-for-profit, nonstock Maryland companies that provide residential, rehabilitation, vocational, and outpatient mental health services across the state of Maryland.

Resources is a for-profit company that was formed for the purpose of providing employee assistance program services to other entities. Resources was inactive as an operating entity for the years ended June 30, 2018 and 2017.

(b) Basis of Presentation

The consolidated financial statements are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles. All majority-owned and affiliated member entities are consolidated. All entities where Foundation exercises significant influence but for which it does not have control are accounted for under the equity method. All other entities are accounted for under the cost method. All significant intercompany accounts and transactions have been eliminated.

Net assets, revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. The net assets of Foundation and changes therein are classified and reported as follows:

Unrestricted net assets – Net assets that are not subject to donor-imposed stipulations. Board-designated funds are included within this category of net assets.

Temporarily restricted net assets – Net assets whose use by Foundation has been limited by donors to a specific time or purpose.

Permanently restricted net assets – Net assets that have been restricted by donors to be maintained by the Foundation in perpetuity. Generally, the donors of these assets permit Foundation to use all or part of the income earned on related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Contributions with no donor-imposed restrictions are recognized as revenues in the period received as increases in unrestricted net assets.

Unconditional promises to give cash and other assets to Foundation with donor-imposed restrictions are reported as increases in temporarily or permanently restricted net assets at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. When the donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

(c) Charity Care

Foundation provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because Foundation does not pursue collection of amounts determined to qualify for charity care, such amounts are not reported as revenue.

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(d) Cash and Cash Equivalents

Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less that are not limited or restricted as to use.

(e) Allowance for Doubtful Accounts

Patient accounts receivable are reduced by allowances for bad debts. In evaluating the collectability of accounts receivable, Foundation analyzes historical collections and write-offs and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for bad debts and provision for uncollectible accounts. Management regularly reviews its estimate and evaluates the sufficiency of the allowance for bad debts. For patient accounts receivable associated with self-pay patients, which includes those patients without existing insurance coverage for a portion of the bill, Foundation records a significant provision for bad debts for patients that are unable or unwilling to pay for the portion of the bill representing their financial responsibility. Account balances are charged off against the allowance for doubtful accounts after all means of collection have been exhausted.

(f) Investments Limited or Restricted as to Use

Investments limited or restricted as to use, primarily recorded at fair value, represent assets that have been designated by the board of trustees for special purposes and self-insurance trust arrangements. The principal, income and capital appreciation of the Moses Sheppard and Enoch Pratt bequests are legally unrestricted but are classified, for financial reporting purposes, as board-designated and limited as to use. Assets designated by the board of trustees for particular purposes are controlled by the board of trustees, who at their discretion may subsequently use the assets for other purposes.

Investments of board-designated, temporarily restricted and permanently restricted funds are maintained in a combined investment pool or in a related investment account. Related income, and realized and unrealized gains and losses on sales of investments are apportioned on the basis of the shares held by each of the respective funds and in accordance with donor restrictions on the use of investment earnings.

Foundation classifies its investment portfolio as trading securities with unrealized gains and losses included in other income (expense), which is included in the excess of revenues over expenses. Investment income and realized gains and losses from all other investments are reported as other income (expense), unless the income is restricted by donors, which is reported as previously described above. The investment portfolio is classified as current or noncurrent assets based on management's intention as to use.

Alternative investments represent both subscriptions in private equity venture capital funds and subscriptions in funds-of-funds utilized to diversify the portfolio of Foundation. Annual audited financial statements for these funds are submitted to Foundation and reviewed by management. The funds' financial statements are presented at fair value as estimated in an unquoted market. Foundation's alternative investments are accounted for under the equity method of accounting. The investment balance is equal to Foundation's proportionate interest in the fund's net equity. Individual investment holdings within the investment portfolio may, in turn, include investments in both nonmarketable and market-traded securities. Valuations of these investments are primarily based on financial data supplied by the underlying investee funds. Values may be based on historical cost, appraisals, or other estimates that require varying degrees of judgment. Certain of these investments contain additional capital call requirements, based upon the provisions of the investment agreements.

Investment income from unrestricted cash equivalents and the self-insurance trust are reported as other operating revenue since such income is considered to be a part of Foundation's ongoing central operations of providing healthcare services.

(g) Pledges

Pledges, less an allowance for uncollectible amounts, are recorded as receivables in the year the pledge is made unless the pledge carries conditions that have not been met. Conditional pledges are recorded as contributions when the conditions of the pledge have been satisfied. Pledges receivable are recorded at net realizable value, which is calculated using a discount rate of 3% at June 30, 2018 and 2017.

(h) Property and Equipment

Property and equipment acquisitions are recorded at cost (except donated property and equipment that are recorded at their fair market value at the date of receipt). Depreciation is computed on the straight-line method and charged to operations over estimated useful lives ranging from 20 to 40 years for buildings and improvements and 3 to 10 years for furniture, equipment, information systems hardware and software and motor vehicles. Property and equipment under capital lease obligations are amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the property and equipment. Interest costs incurred on borrowed funds during the period of construction are capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings, or equipment are reported as other changes in unrestricted net assets, and are excluded from the excess of revenues over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(i) Costs of Borrowing

Deferred financing costs and debt premiums, which are a direct deduction to long term debt, are amortized using the effective-interest method and charged to operations as a component of interest expense over the term of the related debt.

(j) Estimated Self-Insurance Liability Claims

The estimated self-insured professional liability claims are reflected as a liability and include actuarially determined estimates of the ultimate costs for both reported claims and claims incurred but not reported. Costs under self-insurance programs for employee health benefits and workers' compensation include estimates for both reported claims and claims incurred but not reported, based on an evaluation of pending claims and past experience. These estimates are based on actuarial analysis of historical trends, claims asserted and reported incidents. Receivables for amounts in excess

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of self-insurance retention limits are recorded at their net realizable value and are due from highly rated commercial insurance companies.

(k) Pension Benefits

Pension benefits are recorded in accordance with Accounting Standards Codification (ASC) Subtopic 715-30, *Defined Benefit Plans – Pension*, which requires the recognition of the funded status of pension plans within the accompanying consolidated balance sheets.

(l) Patient Service Revenue

Foundation has agreements with third-party payors that provide for payments to Foundation at amounts different from its established rates. Payment arrangements include prospectively determined rates per day, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is 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 certain third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. Differences between the estimated amounts and final settlements are reported in operations in the year of settlement.

Foundation's revenues may be subject to adjustment as a result of examination by government agencies or contractors, and as a result of differing interpretation of government regulations, medical diagnosis, charge coding, medical necessity, or other contract terms. The resolution of these matters, if any, often is not finalized until subsequent to the period during which the services were rendered (note 15).

(m) Residential and Educational Service Revenue

Foundation provides educational services to special needs children under arrangements with the Maryland State Department of Education (MSDE). On an annual basis, a prospective rate per student is set with MSDE based upon an approved operating budget. Subsequently, as services are provided, invoices are submitted to each student's local school district for payment on a monthly basis.

Foundation also operates two residential treatment centers for adolescents. Substantially all of the RTC services are reimbursed by the State of Maryland Medicaid Program on a cost basis subject to annual ceilings. Foundation receives an interim per diem rate during the year and ultimately settles final payment based upon an audited cost report filing.

(n) Other Operating Revenue

Other operating revenue is primarily comprised of grant revenue which is recognized when funds are released to cover qualified expenses, and business service revenue which is recognized when earned.

(o) Impairment of Long-Lived Assets

Management regularly evaluates whether events or changes in circumstances have occurred that could indicate an impairment in the value of long-lived assets. In accordance with the provisions of ASC Subtopic 360-10, *Property, Plant, and Equipment – Overall*, if there is an indication that the

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carrying amount of an asset is not recoverable, Foundation estimates the projected undiscounted cash flows, excluding interest, to determine if an impairment loss should be recognized. The amount of impairment loss is determined by comparing the historical carrying value of the asset to its estimated fair value. Estimated fair value is determined through an evaluation of recent and projected financial performance using standard industry valuation techniques.

In addition to consideration of impairment upon the events or changes in circumstances described above, management regularly evaluates the remaining lives of its long-lived assets. If estimates are changed, the carrying value of affected assets is allocated over the remaining lives.

In estimating the future cash flows for determining whether an asset is impaired and if expected future cash flows used in measuring assets are impaired, Foundation groups its assets at the lowest level for which there are identifiable cash flows independent of other groups of assets. No impairment charges were recorded during the years ended June 30, 2018 and 2017.

(p) Rental Income

Foundation has agreements with various organizations and individual clinicians to rent office space and land. Foundation recognizes the rent under the leases, using the straight-line method, net of an allowance for doubtful accounts, where necessary, in other income (expense).

(q) Excess of Revenues over Expenses

The consolidated statements of operations include a performance indicator, the excess of revenues over expenses. Changes in unrestricted net assets that are excluded from excess of revenues over expenses, consistent with industry practice, include changes in pension liability adjustments, contributions of long-lived assets (including assets acquired using contributions that by donor restriction were to be used for the purposes of acquiring such assets) and grants for capital purposes.

(r) Income Taxes

Foundation and its subsidiaries, except for Resources, have been recognized as tax-exempt organizations under Section 501(a) as organizations described in Section 501(c)(3) of the Internal Revenue Code and are not subject to income taxes on related income pursuant to Section 501(a) of the Internal Revenue Code. The operations of Resources, a for-profit company, are not significant to the consolidated financial statements. Foundation has cumulative net operating losses of $3 million for unrelated business activities, which expire at various dates through 2038. The Foundation’s deferred tax assets, including the asset related to its net operating losses, are fully reserved as they are not deemed to have realizable value nor are they expected to be utilized. Foundation accounts for income taxes under ASC Topic 740, *Income Taxes*.

On December 22, 2017, the President signed into law H.R. 1, originally known as the Tax Cuts and Jobs Act. The new law includes several provisions that result in substantial changes to the tax treatment of tax-exempt organizations and their donors. Foundation has reviewed these provisions and the potential impact and concluded the enactment of H.R. 1 will not have a material effect on the operations of the organization.

(s) Leases

Lease arrangements, including assets under construction, are capitalized when such leases convey substantially all the risks and benefits incidental to ownership. Capital leases are amortized over either the lease term or the life of the related assets, depending upon available purchase options and lease renewal features. Amortization related to capital leases is included in the statements of operations within depreciation or amortization expense.

(t) Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates

(u) New Accounting Pronouncements

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This ASU establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Particularly, that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 is effective for fiscal year 2019. The Company expects to record a decrease in net patient service revenue related to self-pay patients and a corresponding decrease in bad debt expense upon the adoption of the standard.

The FASB issued ASU No. 2016-02, *Leases*, which will require lessees to recognize most leases on-balance sheet, increasing their reported assets and liabilities – sometimes very significantly. This update was developed to provide financial statement users with more information about an entity's leasing activities, and will require changes in processes and internal controls. The adoption of ASU 2016-02 is effective fiscal year 2020, and will require application of the new guidance at the beginning of the earliest comparable period presented. The Company is currently assessing the impact of the adoption of ASU No. 2016-02, which is expected to have a material impact on its financial position.

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

- Reduces the number of net asset classes presented from three to two: with donor restrictions and without donor restrictions;
- Requires all NFPs to present expenses by their functional and their natural classifications in one location in the financial statements;
- Requires NFPs to provide quantitative and qualitative information about management of liquid resources and availability of financial assets to meet cash needs within one year of the balance sheet date; and

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

The FASB issued ASU No. 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. The amendments in this ASU require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost as defined in paragraphs 715-30-35-4 and 715-60-35-9 are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. The amendments also allow only the service cost component to be eligible for capitalization when applicable (for example, as a cost of internally manufactured inventory of a self-constructed asset). ASU No. 2017-07 is effective for fiscal year 2020. This ASU requires retrospective application to all prior periods presented. The Company does not anticipate that the adoption of this ASU will have a material impact on its financial position and results of operations.

(v) Recently Adopted Pronouncements

The FASB issued ASU 2015-07, *Fair Value Measurement (Topic 820) Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share*. This ASU removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value (NAV) per share practical expedient. The amendments also remove the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using that practical expedient. The Company implemented this ASU in 2018.

(w) Management's Assessment and Plans

Accounting Standards Update (ASU) 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern,* requires management to evaluate an entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued, when applicable). Management determined that there were no conditions or events that raise substantial doubt about the Company's ability to continue as a going concern and the Company will continue to meet its obligations through October 18, 2019.

(x) Reclassifications

Certain prior year amounts have been reclassified to conform to current year presentation.

(2) Charity Care and Community Services

Foundation maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy and equivalent service statistics. The estimated cost of charity care provided during the years ended June 30, 2018 and 2017 was $3,784,810 and $4,374,354, respectively.

Foundation provides the community with other healthcare services and programs, including teaching of psychiatric residents, providing programs and facilities for teaching other medical health professionals, providing behavioral health educational programs for the general public, and conducting research to improve treatment of behavioral health problems.

(3) Investments Limited or Restricted as to Use

Investments limited or restricted as to use, stated at fair value, except for the real estate investment, which is recorded at cost and investments in partnerships and alternative investments, which are recorded under the equity method, include the following at June 30:

		2018	2017
Board-designated, unrestricted:			
Portion of pooled investments	$	162,975,810	155,681,432
Other investments		11,415,951	23,821,720
Held by trustees:			
Construction Funds		100,664,801	—
Under self-insurance trusts		4,754,820	4,541,304
Security Deposit		631,669	—
Donor-restricted:			
Temporarily restricted portion of pooled investments		3,020,595	2,559,934
Other temporarily restricted investments		7,954,419	2,624,777
Permanently restricted portion of pooled investments		3,367,985	3,350,408
Other permanently restricted investments		567,074	558,967
Total investments limited or restricted as to use		295,353,124	193,138,542
Current portion		2,193,109	865,824
Investments limited or restricted as to use, less current portion	$	293,160,015	192,272,718

Foundation manages a significant component of its investments limited or restricted as to use in a combined investment pool. The combined investment pool has been allocated based on donor restrictions, where applicable, as follows at June 30:

		2018	2017
Board-designated unrestricted	$	162,975,810	155,681,432
Temporarily restricted		3,020,595	2,559,934
Permanently restricted		3,367,984	3,350,408
Total	$	169,364,389	161,591,774

The combined investment pool is comprised of the following at June 30:

		2018	2017
Cash and cash equivalents	$	5,724,924	3,013,198
Corporate bonds		12,881,359	12,715,999
Marketable equity securities		5,933	4,417
Mutual and common trust funds		93,593,425	92,739,623
Other (primarily alternative investments under equity method)		57,158,748	53,118,537
Total	$	169,364,389	161,591,774

Other board-designated investments consist of the following at June 30:

		2018	2017
Cash and cash equivalents	$	4,362,151	3,596,363
Mutual funds		3,375,384	3,124,313
Real estate held for future development, at cost		3,084,139	15,908,001
Other		594,277	1,193,043
	$	11,415,951	23,821,720

The funds held by trustees under self-insurance trusts are comprised of the following at June 30:

		2018	2017
Cash and cash equivalents	$	587,265	358,406
Fixed income investments		4,167,555	4,182,898
	$	4,754,820	4,541,304

A Foundation trustee serves as an investment manager for a portion of the investments limited or restricted as to use totaling approximately $13,101,000 and $13,100,000 as of June 30, 2018 and 2017, respectively.

The total investment return, net of investment fees, including the return from the combined investment pool, is summarized as follows for the years ended June 30:

		2018	2017
Investment income:			
Unrestricted	$	2,114,843	1,717,523
Temporarily restricted		83,504	65,326
Permanently restricted		8,108	13,315
		2,206,455	1,796,164
Net realized gains (losses) on sales of investments:			
Unrestricted		5,014,038	(1,637,695)
Temporarily restricted		160,731	(49,727)
		5,174,769	(1,687,422)
Net unrealized gains on investments:			
Unrestricted		3,563,005	20,383,687
Temporarily restricted		115,623	616,318
Total unrealized gains		3,678,628	21,000,005
Total investment gain income		11,059,852	21,108,747
Investment income on other unrestricted investments and cash and cash equivalents		968,334	922,751
Investment income on self-insurance trust assets		6,852	1,876
Total investment income	$	12,035,038	22,033,374

(4) Disclosures about Fair Value of Financial Instruments

Foundation accounts for its financial assets and liabilities, in accordance with ASC Subtopic 820-10 as discussed in note 1. ASC Subtopic 820-10 defines fair value, establishes a framework for measuring fair value in accordance with U.S. generally accepted accounting principles, and expands disclosures about fair value measurements. Specifically, the guidance provides for the following:

- Defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establishes a framework for measuring fair value;
- Establishes a three-level hierarchy for fair value measurement;
- Requires consideration of Foundation’s nonperformance risk when valuing liabilities; and
- Expands disclosures about instruments measured at fair value.

The three-level valuation hierarchy for fair value measurements is based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect Foundation's market assumptions. The three-level valuation hierarchy is defined as follows:

- Level 1 – Quoted prices for identical instruments in active markets;
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar investments in markets that are not active; and model-derived valuations whose significant inputs are observable; and
- Level 3 – Instruments whose significant inputs are unobservable.

The table below presents Foundation's investable assets and liabilities as of June 30, 2018, aggregated by the three-level valuation hierarchy:

	Level 1	Level 2	Level 3	Total
Assets:				
Cash and cash equivalents	$ 115,513,147	—	—	115,513,147
Equities:				
Common stocks	10,140,939	—	—	10,140,939
Mutual funds	81,245,116	—	—	81,245,116
Other	1,806,983	4,572,667	—	6,379,650
Fixed income:				
Collateralized mortgage obligations	—	574,709	—	574,709
Corporate bonds	—	9,064,222	—	9,064,222
Government issued bonds	—	7,409,983	—	7,409,983
Other financial instruments	—	4,424	—	4,424
Total assets	$ 208,706,185	21,626,005	—	230,332,190
Liabilities:				
Interest rate swap	$ —	129,649	—	129,649

The table below presents Foundation's investable assets and liabilities as of June 30, 2017, aggregated by the three-level valuation hierarchy:

		Level 1	Level 2	Level 3	Total
Assets:					
Cash and cash equivalents	$	9,607,512	—	—	9,607,512
Equities:					
Common stocks		9,055,320	—	—	9,055,320
Mutual funds		80,886,263	—	—	80,886,263
Other		1,864,728	4,207,680	—	6,072,408
Fixed income:					
Collateralized mortgage obligations		—	802,659	—	802,659
Corporate bonds		—	8,340,084	—	8,340,084
Government issued bonds		—	7,756,154	—	7,756,154
Other financial instruments		—	804	—	804
Total assets	$	101,413,823	21,107,381	—	122,521,204
Liabilities:					
Interest rate swap	$	—	67,452	—	67,452

Foundation did not have transfers between Levels, or Level 3 measurements, thus, no additional disclosures were necessary.

Foundation's Level 1 securities primarily consist of common stock, exchange-traded mutual funds, and cash. Foundation determines the estimated fair value for its Level 1 securities using quoted (unadjusted) prices for identical assets or liabilities in active markets.

Foundation's Level 2 securities consist of collateralized mortgage obligations, corporate bonds, government issued bonds, mutual funds, and derivative instruments, which are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active or model-derived valuations whose significant inputs are observable. Valuation models require a variety of inputs, including contractual terms, market fixed prices, inputs from forward price yield curves, notional quantities, measures of volatility, and correlations of such inputs.

Investments classified within Level 3 have significant unobservable inputs, as they trade infrequently or not at all. The classification of a financial instrument within Level 3 is based upon the significance of the unobservable inputs to the overall fair value measurement.

The carrying amount of cash and cash equivalents, accounts receivable, third-party payor settlements receivable or payable, other current assets, accounts payable and accrued expenses approximates fair value because of the short-term maturity of these instruments. The fair value of Foundation's long-term debt, except for the Series A portion of the 2012 Bonds, is estimated to approximate the carrying amount because interest rates are variable and determined frequently based on prevailing market conditions. The estimated fair value of the Series 2017 Bond at June 30, 2018 and the Series A portion of the 2012 Bonds at June 30, 2017 was approximately $177,329,000 and $32,039,000, respectively. During FY18, Series A and Series B portion of the 2012 Bond were refinanced with the issuance of the Series 2017 Bond. Due to the subjective nature of the terms of the Foundation's notes receivable and capital lease obligations, their fair values cannot be estimated.

(5) Temporarily Restricted Assets

Temporarily restricted assets consist of the following at June 30:

	2018	2017
Pledges receivable, net of unamortized discount of $146,000 at June 30, 2018 and $17,000 at June 30, 2017	$ 3,125,332	278,752
Less allowance for uncollectible pledges	98,000	9,000
Net pledges receivable	3,027,332	269,752
Other investments (primarily property)	12,537,438	11,651,542
Portion of pooled investments (note 3)	3,020,595	2,559,934
Restricted cash and investments	4,927,087	2,355,025
	$ 23,512,452	16,836,253

The net realizable value of the unconditional pledges receivable at June 30, 2018 was calculated using an average discount rate of 3%. The net present value of pledges receivable and the expected collection period at June 30, 2018 are as follows:

2019	$ 1,476,589
2020	1,610,756
2021	37,241
2022	554
2023	192
	$ 3,125,332

(6) Note Receivable

In conjunction with the land lease described in note 7, Investment Company provided a loan and a line of credit to the Maryland Economic Development Company (MEDCO) to help finance the development of university student housing located on the campus of Foundation. The unsecured term loan of $3.75 million is payable in equal quarterly installments between the initial repayment date (January 2004) and June 30, 2031. MEDCO repaid approximately $132,000 during each of the years ended June 30, 2018 and 2017, which resulted in an outstanding balance of $1,745,867 and $1,877,631 June 30, 2018 and 2017, respectively. The loan bears interest at the rate of 12% per annum. Foundation has included approximately $218,000 and $234,000 of interest income from the loan in investment income during the fiscal years ended June 30, 2018 and 2017, respectively.

(7) Property and Equipment

Property and equipment at June 30 are summarized as follows:

	2018	2017
Land	$ 24,682,726	22,339,800
Land improvements	14,761,963	12,118,225
Buildings and building improvements	337,649,336	321,026,595
Furniture and equipment	71,011,568	66,687,458
Vehicles	8,341,644	8,269,913
Construction in progress	19,864,813	12,241,843
	476,312,050	442,683,834
Less accumulated depreciation	243,082,463	226,771,318
	$ 233,229,587	215,912,516

Assets under capital lease at June 30, 2018 and 2017 of $9,639,233 and $9,621,041, respectively, were included in buildings and building improvements and furniture and equipment in the table above. Accumulated depreciation of assets under capital leases totaled $5,481,545 and $4,559,995 at June 30, 2018 and 2017, respectively.

Certain land, buildings, improvements, and equipment are pledged as collateral for the debt described in note 9.

Depreciation expense for the years ended June 30, 2018 and 2017 was $18,917,376 and $18,691,954, respectively.

In June 2001, the Health System entered into a 40-year ground lease with MEDCO, whereby MEDCO leases certain parcels of land from Foundation. The base year rental income, included in other revenue in the accompanying consolidated statements of operations is $885,500 and increases by 3.00% per annum over the life of the lease. MEDCO has constructed student housing on the leased parcels of land (the MEDCO lease). Unpaid accrued rent bears interest at 12.65% per annum.

The payment of ground rent is subordinate to the payment of debt on the MEDCO loan. Based on current cash flow projections, it is anticipated that the full amount of rent accruing will not be paid. Foundation has recorded an allowance for a portion of the unpaid accrued rent, and the related interest on the unpaid rents for fiscal years 2014 through 2018. Partial ground rent payments of approximately $2,130,000 and $2,640,000 were accrued as a receivable at June 30, 2018 and 2017. As of June 30, 2018 and 2017, Foundation has recorded total ground rent receivable in the accompanying consolidated balance sheets of $7,708,194 and $7,537,246, respectively, with a related reserve of $5,578,630 and $4,901,111, respectively.

On September 20, 2016 the State Health Planning and Development Agency approved Foundation's application to build a new hospital in Elkridge, Maryland. The new hospital will replace Sheppard Pratt at Ellicott City which is currently housed in a leased facility in Ellicott City, Maryland. The project is expected to span multiple years with a cumulative investment of approximately $96,530,000.

(8) Other Assets

The other assets balance is composed of the following at June 30:

		2018	2017
Workers' compensation excess insurance receivable	$	275,395	376,638
Intangible assets		1,307,000	1,307,000
Cash surrender value of life insurance and other		1,071,843	3,105,163
		2,654,238	4,788,801
Less accumulated amortization		(540,175)	(507,500)
	$	2,114,063	4,281,301

(9) Long-Term Debt and Note Payable

Long-term debt consists of the following at June 30:

		2018	2017
Maryland Health and Higher Educational Facilities Authority (MHHEFA) Revenue Bonds, Series 2017	$	177,329,000	—
Maryland Health and Higher Educational Facilities Authority (MHHEFA) Revenue Bonds, Series 2012		—	80,420,179
MHHEFA Revenue Bond – 2013		5,046,052	5,480,650
MHHEFA Revenue Bond – 2014		3,672,748	3,799,748
MHHEFA Revenue Bond – 2016		3,446,000	3,820,000
Bank notes		1,524,017	1,707,562
Mortgages on real estate		3,251,727	3,354,042
Other debt		126,497	124,399
		17,067,041	98,706,580
Less deferred financing costs		(1,110,717)	(807,804)
Less current portion		(5,620,490)	(5,005,333)
	$	187,664,834	92,893,443

In December 2017, Health System, Physicians, Foundation and Investment (Obligated Group) acquired new financing to fund a portion of the construction costs of a new hospital in Elkridge, Maryland and other capital improvements and equipment, to refinance certain outstanding indebtedness including 2012 Series A and Series B bonds, and to fund transaction related costs. The 2017 Series bond was issued by the Maryland Health and Higher Educational Facilities Authority (MHHEFA) and purchased by a bank in a direct placement loan arrangement.

The 2017 Series bond is a tax- exempt fixed rate bond with an original principal amount of $178,748,000 bearing an initial fixed interest rate of 2.48%. Effective January 1, 2018, the interest rate was increased to 3.014% in conjunction with financing agreement provisions tied to the “Tax Cuts and Jobs Act of 2017”. The initial term of the credit facility provided by the direct placement loan arrangement is 15 years, and the final scheduled maturity of the bonds is June 1, 2048. The Series 2017 bonds are secured by a trust indenture and Obligated Group has granted the bank and MHHEFA a security interest in its revenues. The Series 2017 Bonds require Obligated Group to satisfy certain measures of financial performance as long as the bonds are outstanding.

The Series 2012 A bonds were fixed rate bonds with an original principal amount of $34,032,000 bearing interest at a fixed rate of 2.84%. The initial term of the credit facility provided by the direct placement loan arrangement was 15 years, and the final scheduled maturity of the bonds was July 1, 2036. The Series 2012 B bonds were variable rate bonds with an original principal amount of $62,182,000 bearing interest at 77% of the sum of one-month London Interbank Offered Rate (LIBOR) plus 1.1%. The initial term of the credit facility provided by the direct placement loan arrangement was 10 years and the final scheduled maturity of the bonds was July 1, 2035.

The Series 2012 bonds were secured by a trust indenture and Obligated Group has granted the bank and MHHEFA a security interest in its revenues. The Series 2012 Bonds required Obligated Group to satisfy certain measures of financial performance as long as the Series 2012 Bonds were outstanding.

On September 28, 2016, Mosaic borrowed $4,066,000 variable rate debt through MHHEFA via a tax-exempt nonbank qualified direct purchase (MHHEFA Revenue Bond – 2016). The loan was issued for the purposes of advance refunding a 2006 MHHEFA Series D pooled loan program revenue bonds along with three existing mortgages. The refinance occurred via a taxable nonbank qualified direct purchase by a commercial bank. The bonds accrue interest at a variable rate based on 83% of LIBOR plus 1.42% which was 3.08% and 2.00% at June 30, 2018 and 2017, respectively, and are being amortized over ten years. The loan has principal payments that began November 2016 and will terminate October 2026. The loan is secured by collateral including, but not limited to, gross revenues, cash accounts and certain fixed assets. The loan requires Mosaic to satisfy certain measures of financial performance as long as the loan is outstanding. In conjunction with the refinance, Mosaic entered into a 10-year interest rate swap agreement with a third party under which the Company will make monthly payments at a fixed rate of 0.92% in exchange for payments based on LIBOR. The liability of $129,649 and $67,452 as of June 30, 2018 and 2017, respectively, is included in other long-term liabilities.

On May 2, 2013, MHHEFA issued $7,200,000 bank-qualified tax-exempt revenue bonds (MHHEFA Revenue Bond – 2013) for the purpose of reimbursing Way Station for certain capital expenditures associated with the acquisition and development of two properties in Frederick, Maryland, a property in Hagerstown, Maryland, and a property in Columbia, Maryland. The bonds were purchased by a bank and

Way Station is required to make payments over 15 years with a fixed interest rate of 2.645%. However, the lowering of the corporate tax rate in the Tax Cuts and Jobs Act of 2017 has triggered an adjustment to the interest rate. The new rate with the bank is 3.11%. The Company owed $5,046,051 and $5,480,651 as of June 30, 2018 and 2017. As part of the same transaction, the same bank loaned Way Station $1,700,000 in a taxable term loan payable over 15 years, at a fixed interest rate of 3.305%. The taxable loan was paid off in February 2017. The tax-exempt loan is secured by a deed of trust covering six of the Company's properties in Frederick, Hagerstown, and Columbia, Maryland. This loan requires Way Station to satisfy certain measures of financial performance as long as the loan is outstanding. The Company is limited in additional borrowings, which cannot occur without the bank's consent.

On March 4, 2014, MHHEFA issued a $4,430,000 bank-qualified tax-exempt revenue bond (MHHEFA Revenue Bond – 2014) for the purpose of refinancing Family Services existing mortgage debt. The bond was purchased by a bank, and Family Services is required to make payments over 25 years at varying interest rates. As part of the same transaction, the same bank loaned Family Services $1,683,000 in a taxable term loan that is amortized over 25 years; however, it is due in 10 years, at fixed interest rates that vary from 4.25% in year one to 5.25% in subsequent years. The tax-exempt and taxable term loans are secured by a deed in trust covering the Company's properties, and these loans require Family Services to satisfy certain measures of financial performance as long as the loans are outstanding.

The Affiliates have mortgages on multiple properties with a total outstanding balance of $3,251,727 as of June 30, 2018 and $3,354,042 as of June 30, 2017. The interest rates and years of maturity range from 0% to 7.45%, and 2019 to 2037, respectively.

The Affiliates have other nonmortgage debt, consisting primarily of auto and renovation loans, with a total outstanding balance of $126,497 as of June 30, 2018 and $124,399 as of June 30, 2017. The interest rates range from 0% to 5.9%.

The affiliates have combined variable rate lines of credit the amount of $5,000,000. As of June 30, 2018 and 2017, there were no outstanding balances on the lines of credit.

Repayment of long-term debt, including mandatory sinking fund redemptions, in each of the next five fiscal years is as follows:

2019	$ 5,620,490
2020	5,342,869
2021	5,462,362
2022	5,585,285
2023	5,733,532
2024 and thereafter	166,651,503
	$ 194,396,041

Interest payments were $4,143,587 and $2,410,257 in 2018 and 2017, respectively.

In December 2016, the Health System obtained a short term note which was used to fund working capital for the purchase of certain land and improvements. The note was a 364 day nonrevolving term loan of up to $15,000,000, with an outstanding balance of $0 and $12,900,000 as of June 30, 2018 and 2017, respectively. Maturity was 364 days from closing (May 2018) with interest only payable prior to maturity. The rate was the sum of the one month LIBOR, plus 100 basis points. Collateral was a double negative pledge on the property. This note was paid off in full in December of 2017 prior to the issuance of the 2017 bond.

(10) Other Financial Instruments

During the year ended June 30, 2006, Foundation received a gift annuity from donors. Under the terms of such agreement, Foundation agreed to pay 6% annually of the contributed amount (approximately $1 million) on a quarterly basis over the remaining lives of the donors. Accordingly, as of June 30, 2018 and 2017, the net present value of the estimated remaining payments of approximately $369,661 and $401,493, respectively, have been recorded as an other long-term liability.

(11) Pension Plan, Employees' Thrift Plan and Life, Accident and Health Plan

Foundation has a noncontributory defined benefit pension plan that covers eligible employees of Health System and Physicians. The benefits are based on the employees' credited service and average compensation during the five consecutive years, taken from the last 10 years of service before retirement, which produces the highest result. The funding policy is to contribute annually amounts actuarially determined to provide for benefits attributed to service to date and benefits expected to be earned in the future. Prior service cost is being amortized on a straight-line basis over the estimated term of employment of current employees.

ASC Subtopic 715-30, *Defined Benefit Plans-Pension*, requires Foundation to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of its pension plan in the accompanying consolidated balance sheets, with a corresponding adjustment to unrestricted net assets. The pension liability adjustment to unrestricted net assets represents the change in net unrecognized actuarial losses and unrecognized prior service costs that have not yet been recognized as part of excess of revenues over expenses. Those amounts will be subsequently recognized as a component of net periodic pension cost pursuant to Foundation's historical accounting policy for amortizing such amounts.

The following are deferred pension costs that have not yet been recognized in periodic pension expense but instead are included as a component of unrestricted net assets, as of June 30, 2018 and 2017. Unrecognized actuarial losses represent unexpected changes in the projected benefit obligation and plan assets over time, primarily due to changes in assumed discount rates and investment experience. Unrecognized prior service cost is the impact of changes in plan benefits applied retrospectively to employee service previously rendered. Deferred pension costs are amortized into annual pension expense over the average remaining assumed service period for active employees.

		Amounts in unrestricted net assets to be recognized during the next fiscal year	Amounts recognized in unrestricted net assets at June 30, 2018	Amounts recognized in unrestricted net assets at June 30, 2017
Net prior service cost	$	3,992	3,992	33,129
Net actuarial loss		3,118,309	41,938,086	50,548,367
Total	$	3,122,301	41,942,078	50,581,496

During 2013, the Plan was amended to permanently allow certain vested terminated participants to take a lump sum payment of Plan benefits not previously available as a lump sum in lieu of a deferred monthly benefit. This offer is available to terminating participants with a vested benefit value of less than $25,000. In FY18, the Plan was amended to temporarily allow a one-time opportunity to elect a lump sum distribution of vested benefit in lieu of monthly payments for vested benefit payouts not to exceed $250,000. As a result of these changes, Foundation made lump sum payments of approximately $7,979,319 and $147,807 in 2018 and 2017, respectively.

Foundation previously adopted the new RP-2014 Mortality Table with generational improvements using projection scale MP-2014. The Foundation updated its mortality table assumptions to the projection scale MP-2016 and MP-2015 in 2018 and 2017, respectively.

The Plan's change in benefit obligations, the change in plan assets, current funded status and the components of net periodic pension cost as of and for the years ended June 30 are as follows:

		2018	2017
Accumulated benefit obligation at the end of the year	$	204,466,414	217,317,683
Changes in benefit obligations:			
Projected benefit obligation at the beginning of the year	$	234,679,327	232,328,224
Service cost		4,675,073	5,125,827
Interest cost		8,081,882	7,392,919
Actuarial loss		(10,843,582)	(2,410,313)
Benefits paid		(16,159,982)	(7,757,330)
Projected benefit obligation at the end of the year		220,432,718	234,679,327
Changes in plan assets:			
Fair value of plan assets at beginning of the year		201,992,238	188,338,261
Actual return on plan assets		7,353,896	16,411,307
Contributions to the plan		5,000,000	5,000,000
Benefits paid		(16,159,982)	(7,757,330)
Fair value of plan assets at end of the year		198,186,152	201,992,238
Funded status	$	(22,246,566)	(32,687,089)

Net periodic pension expense includes the following components for the years ended June 30:

		2018	2017
Service cost	$	4,675,073	5,125,827
Interest cost		8,081,882	7,392,919
Expected return on plan assets		(13,592,310)	(12,685,992)
Amortization of prior service cost		29,137	29,137
Amortization of net loss		4,005,113	5,855,650
Net pension expense	$	3,198,895	5,717,541

The following table presents the weighted average assumptions used to determine benefit obligations and net periodic benefit expense for the Plan:

	2018	2017
Discount rates (benefit obligation)	4.35 %	4.02 %
Discount rates (benefit expense)	4.02	3.93
Rate of compensation increase	Age Graded	Age Graded
Expected long-term return on plan assets	6.80	6.80

(a) Determination of Expected Long-Term Rate of Return

In developing the expected long-term rate of return on assets assumption, Foundation considered the current level of expected returns on risk free investments (primarily government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested, and the expectations for future returns of each asset class. The expected return for each asset class was then weighted based on the target allocation to develop the expected long-term rate of return on assets assumption for the portfolio.

(b) Investment Policy and Objectives

The investment policy and objectives are established by the trustees of Foundation. The plan objectives include achieving and maintaining fully funded status and minimizing volatility with reasonable and prudent levels of risk. The investment policy is based on a long-term perspective. An investment advisory firm engaged by Foundation trustees selects investment managers, makes investment decisions in keeping with the Pension Investment Policy Statement developed by the trustees, and reviews fund performance and funding status routinely. The percentage allocation to each asset class may vary depending upon the funded status of the Plan.

Foundation monitors the investment managers' performance and ensures adequate diversification by asset class to further mitigate the risks associated with the investment program. Management believes that its assets are invested in accordance with its overall investment policies at June 30, 2018 and 2017.

(Continued)

(c) Plan Assets

Foundation's pension plan weighted average asset allocations at the measurement dates of June 30, 2018 and 2017 by asset category are as follows:

	Target allocation	2018	2017
Equity securities	44 %	45 %	46 %
Debt securities	56	53	53
Cash and cash equivalents	—	2	1
	100 %	100 %	100 %

In accordance with ASC Subtopic 715-20, *Defined Benefit Plans-General-Disclosures*, nonpublic entities are required to report the fair value of each major category of pension plan asset within the fair value hierarchy. ASC Subtopic 820-10, *Fair Value Measurements-Overall*, provides guidance for the fair value hierarchy, which is a valuation technique that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs. Refer to note 3 for descriptions of each of the three levels within the valuation hierarchy.

The table below presents Foundation's pension plan investable assets as of June 30, 2018 aggregated by the three level valuation hierarchy:

	Level 1	Level 2	Level 3	Total	Reported at NAV[1]
Assets:					
Cash and cash equivalents	$ 3,099,198	—	—	3,099,198	—
Collective trusts – equity	—	88,863,733		88,863,733	—
Collective trusts – fixed income	—	105,173,272	—	105,173,272	—
Private equity and real estate funds	—	—	—	—	1,049,949
Total assets	$ 3,099,198	194,037,005	—	197,136,203	1,049,949

[1] Investments reported at NAV as the practical expedient

The table below presents Foundation's pension plan investable assets as of June 30, 2017 aggregated by the three level valuation hierarchy:

	Level 1	Level 2	Level 3	Total	Reported at NAV[1]
Assets:					
Cash and cash equivalents	$ 2,558,921	—	—	2,558,921	—
Collective trusts – equity	—	92,423,415	—	92,423,415	—
Collective trusts – fixed income	—	105,582,511	—	105,582,511	—
Private equity and real estate funds	—	—	—	—	1,427,391
Total assets	$ 2,558,921	198,005,926	—	200,564,847	1,427,391

[1] Investments reported at NAV as the practical expedient

In conjunction with the adoption of FASB ASU 2015-07 discussed in note 1(v), Foundation reclassified $1,049,949 and $1,427,391 of private equity and real estate funds from Level 3 to Reported at NAV as of June 30, 2018 and 2017, respectively.

The majority of the investments held by the plan are Level 2 securities. There were no significant transfers between levels during the years ended June 30, 2018 and 2017. Foundation has the ability to liquidate the collective trusts on a daily basis.

Foundation's pension plan invests in six alternative investments, which are primarily hedge funds of funds and private equity funds. Such investments are carried at their estimated fair value. Foundation uses the practical expedient to report the net asset values of these funds as an estimate of fair value. Most of the funds have not had changes in the redemption policies during the year ended June 30, 2018, and the policies range primarily from 30 to 90 days. Determination of fair value is performed on a quarterly basis by the General Partner(s) of the funds. Because of the inherent uncertainty of valuation, the determined values may differ significantly from the values that would have been used had a ready market for these investments existed.

(d) Contributions

The Foundation expects to contribute $5 million to its pension plan during the fiscal year ending June 30, 2019.

(e) Estimated Future Benefit Payments

The following benefit payments, which reflect expected future employee service, as appropriate, are expected to be paid from the plan in each of the fiscal years as follows:

2019	$	10,524,000
2020		10,548,000
2021		11,249,000
2022		11,758,000
2023		12,299,000
2024–2028		67,587,000

The expected benefits to be paid are based on the same assumptions used to measure Foundation's benefit obligation at June 30, 2018.

Effective July 1, 2006, Foundation elected to not allow employees hired on or after July 1, 2006 to participate in either the defined benefit pension plan or the current employees' thrift plan. Instead, such employees participate in a new employees' thrift plan. The new employee's thrift plan expense was $4,158,573 and $4,336,557 in 2018 and 2017, respectively. The retirement benefits for employees hired on or prior to June 30, 2006 under the defined benefit plan and employees' thrift plan remain unchanged.

Foundation sponsors an employees' thrift plan for certain employees of Health System and Physicians. Foundation may provide a discretionary contribution to the employees' thrift plan. There were no discretionary contributions to the thrift plan in 2018 and 2017.

Foundation maintains a self-insured life, accident and health plan for employees of Health System and Physicians, which provides for monthly contributions in amounts sufficient to cover the costs of basic hospital, surgical and diagnostic benefits and administrative expenses. The life, accident, and health plan expense was $14,403,841 in 2018 and $12,224,546 in 2017.

Certain of the subsidiaries maintain various tax sheltered annuity accounts, defined contribution plans or other retirement benefit plans. These subsidiaries have the option to issue discretionary matching contributions to the plans. During the years ended June 30, 2018 and 2017, these subsidiaries contributed $557,117 and $361,026, respectively, to the plans.

(12) Leases

Foundation leases office space under long-term operating leases, which expire at various dates through 2035, some of which require increasing monthly payments expiring over the next several years. The

(Continued)

following is a schedule of the future minimum lease payments under operating leases as of June 30, 2018 that have initial or remaining lease terms in excess of one year for each of the years ending June 30:

2019	$	4,256,817
2020		3,529,015
2021		2,180,098
2022		1,331,328
2023		629,491
Thereafter		1,330,001
Total minimum lease payments	$	13,256,750

Rent expense was approximately $7,302,294 and $7,325,771 in 2018 and 2017, respectively. Foundation also leases various equipment under short-term leases.

Foundation has various capital leases for buildings and software the majority of which are related to its electronic medical records system and the long-term rental for one of its school locations.

The following is a schedule of future minimum lease payments under capital leases as of June 30, 2018:

2019	$	846,792
2020		938,528
2021		972,661
2022		1,008,056
2023		1,044,762
Thereafter		2,384,363
Total minimum lease payments		7,195,162
Less amount representing interest		1,337,278
Present value of net minimum lease payments		5,857,884
Less obligations under capital leases, current portion		561,029
Obligations under capital leases, less current portion	$	5,296,855

(13) Self-Insurance Programs and Litigation

Foundation is from time to time subject to claims and suits arising in the ordinary course of business. In the opinion of management, the ultimate resolution of pending legal proceedings will not have a material effect on the consolidated financial statements. In this regard, Foundation maintains a self-insurance program for professional liability claims, and a related trust fund has been established for the purpose of setting aside assets based on actuarial funding recommendations. Under the trust agreement, the assets can only be used for the payment of professional and general liability claims, related expenses, and the cost of administering the trust. Certain claims-made based professional and occurrence-based general liability insurance coverages have been purchased to provide protection for claims in excess of the self-insured amounts. The assets of the trust are classified as investments limited as to use in the accompanying consolidated balance sheets in the amount of approximately $587,000 and $358,000 at June 30, 2018 and 2017, respectively. The related claims liabilities of approximately $3,730,000 and $4,080,000 as of June 30, 2018 and 2017, respectively, are recorded on an undiscounted basis and represent estimates for asserted claims and unasserted claims arising from reported incidents and unreported incidents. Management believes that the provision for loss is adequate at June 30, 2018 and 2017; however, the ultimate liability may differ significantly. Management is aware of certain asserted and unasserted legal claims, none of which, in the opinion of management, are expected to result in losses in excess of insurance limits.

Health System and Physicians are also self-insured for unemployment claims and have established a letter of credit arrangement of approximately $1,458,000 in 2018 and $1,365,000 in 2017 in accordance with the requirements of the Maryland Department of Employment and Training.

Also, Foundation is self-insured for workers' compensation claims up to $550,000 for both 2018 and 2017. Investments of approximately $4,200,000 at June 30, 2018 and 2017 are being held in an account at a financial institution to secure the payment of claims. These investments are included in the balance of investments limited or restricted as to use. The related liabilities of approximately $5,880,000 and $5,370,000 as of June 30, 2018 and 2017, respectively, are recorded in the accompanying consolidated balance sheets. Foundation records outstanding losses and loss expenses for workers' compensation liability claims based on the estimates of the amount of reported losses together with a provision for losses incurred but not reported, the recommendations of an independent actuary, and management's judgment using its past experience and industry experience.

Foundation offers employees a self-insured health plan. Foundation maintains an accrual for claims that have been incurred but not reported to the plan administrator. The accrued liability for claims incurred but not reported is based on the historical claim lag period and current payment trends of health insurance claims. The accrued liability for health claims is approximately $2,270,000 and $1,890,000, respectively, as of June 30, 2018 and 2017.

While management believes that the provision for claims on unemployment, workers' compensation, and employee health benefits is adequate, at June 30, 2018 and 2017, the ultimate liability may be significantly different from the estimates.

(14) Net Assets

Net assets at June 30 are summarized as follows:

	2018	2017
Unrestricted:		
Undesignated	$ 207,920,052	195,144,404
Board-designated:		
Moses Sheppard bequest	53,288,821	49,972,310
Enoch Pratt bequest	33,985,570	31,870,384
Other	47,045,051	48,798,586
Total board-designated	134,319,442	130,641,280
Total unrestricted	$ 342,239,494	325,785,684

Temporarily restricted net assets are available for the purposes of providing indigent care, health and educational programs and the purchase of property and equipment. Permanently restricted net assets are restricted in perpetuity, the income from which is expendable to provide health and educational programs.

(15) Rate Setting Matters and Business and Credit Concentrations

Foundation provides healthcare services through its inpatient and outpatient care facilities located throughout Maryland. Foundation grants credit to patients and generally does not require collateral or other security in extending credit; however, it routinely obtains assignment of (or is otherwise entitled to receive) patients' benefits receivable under their health insurance programs, plans or policies (e.g., Medicare, Medicaid, Blue Cross/Blue Shield, health maintenance organizations (HMOs), and commercial insurance policies).

Net patient, residential and educational service revenue, by payor class, consisted of the following for the years ended June 30:

	2018	2017
Medicare	8 %	8 %
Medicaid	44	43
Commercial insurers and HMOs	13	13
Local government	16	19
Blue Cross/Blue Shield	10	10
Self-pay and other	9	7
	100 %	100 %

(Continued)

Foundation accepts all patients covered by the Medicare and Medicaid programs. These programs reimburse Foundation at amounts less than charges. The difference between the charges for healthcare services and the related reimbursement amounts for these and other third-party payors is as follows for the years ended June 30:

		2018	2017
Medicare	$	9,491,310	8,357,308
Medicaid		8,358,532	7,603,675
Other third-party payors		6,018,604	5,987,169
	$	23,868,446	21,948,152

Patient charges of the Health System (other than Medicare and Medicaid) are recorded at rates established by the State of Maryland Health Services Cost Review Commission (HSCRC), reviewed on an annual basis and adjusted prospectively giving effect to, among other things, the anticipated impact of inflation on operating expenses, variances between actual volume of patient services and the volume budgeted for such services, and variances between actual unit rates and approved unit rates during the previous rate year. Such rate adjustments are reflected in revenue of Health System in the subsequent rate year, which coincides with Health System's fiscal year.

The Foundation is reimbursed for certain services to their Medicare and Medicaid program beneficiaries based upon cost reimbursement methodologies. The Maryland Medicaid program's inpatient reimbursement methodology is a prospective payment system, which is set at 94% of HSCRC rates. Medicaid outpatient services continue to be reimbursed on a cost report basis. Effective July 1, 2005, the Medicare program changed its reimbursement methodology to a prospective payment system. Health System has received either the final settlement or the notice of final settlement on Medicare cost reports through June 30, 2016 and on Medicaid cost reports for all programs through June 30, 2015. As of June 30, 2018 and 2017, the Company has recorded third-party payor settlements receivable of $6,722,504 and $9,755,493 respectively.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount. Management periodically reviews recorded amounts receivable from or payable to third-party payors and may adjust these balances as new information becomes available. In addition, revenue received under certain third-party agreements are subject to audit.

During 2018 and 2017, some of Foundation's prior year third-party cost reports were audited and settled, or tentatively settled, by third-party payors. Adjustments resulting from such audits and management reviews of unaudited years and open claims are reflected as adjustments to revenue in the year the adjustment becomes known. The effect of these adjustments was to increase net patient service revenue by approximately $252,515 and $700,291 during the years ended June 30, 2018 and 2017, respectively. Although certain other prior year cost reports submitted to third-party payors remain subject to audit and retroactive adjustment, management does not expect any material adverse settlements.

Patient accounts receivable are as follows at June 30:

		2018	2017
Patient accounts receivable, net of contractuals	$	21,804,584	20,635,931
Residential and educational accounts receivable, net of contractuals		16,246,606	18,292,451
Less allowance for doubtful accounts		(6,241,212)	(6,562,215)
Patient accounts receivable, net	$	31,809,978	32,366,167

The activity in the allowance for bad debts is summarized as follows for the years ended June 30:

		2018	2017
Beginning Balance July 1	$	6,562,215	7,030,044
Provisions for bad debts		3,389,079	1,990,523
Less writeoffs		(3,710,082)	(2,458,352)
Ending Balance as of June 30	$	6,241,212	6,562,215

(16) Functional Expenses

Members of Foundation provide healthcare and educational services to the patients, which they serve. Expenses related to providing these services, based on management's estimates of expense allocations, are as follows:

		2018	2017
Healthcare and educational services	$	306,427,753	297,627,962
General and administrative		69,828,717	65,723,903
	$	376,256,470	363,351,865

(17) Certain Significant Risks and Uncertainties

Foundation provides psychiatric healthcare services in the State of Maryland. Foundation and other healthcare providers are subject to certain inherent risks, including the following:

- Dependence on revenues derived from reimbursement by the Federal Medicare and state Medicaid programs
- Regulation of hospital rates by the State of Maryland Health Services Cost Review Commission
- Government regulation, government budgetary constraints and proposed legislative and regulatory changes

- Lawsuits alleging malpractice or other claims

Such inherent risks require the use of certain management estimates in the preparation of Foundation's consolidated financial statements and it is reasonably possible that a change in such estimates may occur.

The Medicare and state Medicaid reimbursement programs represent a substantial portion of Foundation's revenues and Foundation's operations are subject to a variety of other federal, state, and local regulatory requirements. Failure to maintain required regulatory approvals and licenses and/or changes in such regulatory requirements could have a significant adverse effect on Foundation.

Changes in federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on Foundation.

The healthcare industry is subject to numerous laws and regulations from federal, state, and local governments, and the government has aggressively increased enforcement of Medicare and Medicaid anti-fraud and abuse laws. Foundation's compliance with these laws and regulations is subject to periodic governmental review, which could result in enforcement actions unknown or unasserted at this time. The federal government and many states have aggressively increased enforcement under Medicare and Medicaid anti-fraud and abuse laws and physician self-referral laws (STARK law and regulation). Recent federal initiatives have prompted a national review of federally funded healthcare programs. In addition, the federal government and many states have implemented programs to audit and recover potential overpayments to providers from the Medicare and Medicaid programs.

As a result of recently enacted and pending federal healthcare reform legislation, substantial changes are anticipated in the U.S. healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers and the legal obligations of health insurers, providers, and employers. These provisions are currently slated to take effect at specified times over the next decade.

(18) Endowment Net Assets

Foundation's endowments consist of both individual donor-restricted funds established for a variety of purposes and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

(a) Interpretation of Relevant Law

Foundation has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Foundation classifies its permanently restricted net assets as (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for

(Continued)

expenditure by the organization in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

(1) The duration and preservation of the fund

(2) The purposes of Foundation and the donor-restricted endowment fund

(3) General economic conditions

(4) The possible effect of inflation and deflation

(5) The expected total return from income and the appreciation of investments

(6) Other resources of Foundation

(7) The investment policies of Foundation

(b) Net Asset Classification by Type of Endowment as of June 30, 2018

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$	—	—	3,935,059	3,935,059
Board-designated endowment funds		134,319,442	—	—	134,319,442
	$	134,319,442	—	3,935,059	138,254,501

Changes in endowment net assets for the year ended June 30, 2018:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets beginning of year	$ 130,641,280	—	3,909,375	134,550,655
Investment return:				
Investment income	1,595,504	—	—	1,595,504
Net appreciation (realized and unrealized gains and losses)	6,456,226	—	8,108	6,464,334
Total investment return	8,051,730	—	8,108	8,059,838
Contributions	—	—	17,576	17,576
Appropriation of endowment assets for expenditure	(4,373,568)	—	—	(4,373,568)
	$ 134,319,442	—	3,935,059	138,254,501

(c) Net Asset Classification by Type of Endowment as of June 30, 2017

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$ —	—	3,909,375	3,909,375
Board-designated endowment funds	130,641,280	—	—	130,641,280
	$ 130,641,280	—	3,909,375	134,550,655

Changes in endowment net assets for the year ended June 30, 2017:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets beginning of year	$ 118,875,924	—	4,084,460	122,960,384
Investment return:				
Investment income	1,435,054	—	3,016	1,438,070
Net appreciation (realized and unrealized gains and losses)	14,533,926	—	10,299	14,544,225
Total investment return	15,968,980	—	13,315	15,982,295
Contributions	—	—	11,600	11,600
Appropriation of endowment assets for expenditure	(4,203,624)	—	(200,000)	(4,403,624)
	$ 130,641,280	—	3,909,375	134,550,655

(d) Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or SPMIFA requires Foundation to retain as a fund of perpetual duration as a result of unfavorable market fluctuations. During the years ended June 30, 2018 and 2017, the fair value did not fall below the specified amounts.

(e) Investment Strategies

Foundation has adopted policies for corporate investments, including endowment assets that seek to maximize risk-adjusted returns with preservation of principal. Endowment assets include those assets of donor-restricted funds that Foundation must hold in perpetuity or for a donor-specified period(s). The endowment assets are invested in a manner that is intended to hold a mix of investment assets designed to meet the objectives of the account. Foundation expects its endowment funds, over time, to provide an average rate of return that generates earnings to achieve the endowment purpose.

To satisfy its long-term rate-of-return objectives, Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). Foundation employs a diversified asset allocation structure to achieve its long-term return objectives within prudent risk constraints.

Foundation monitors the endowment funds returns and appropriates average returns for use. In establishing this practice, Foundation considered the long-term expected return on its endowment. This is consistent with Foundation's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

(19) Subsequent Events

Foundation has evaluated all events and transactions from the balance sheet date through October 17, 2018, the date at which the consolidated financial statements were issued, and determined there are no other items to be recognized or disclosed.

SUPPLEMENTARY INFORMATION

Schedule 1

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidating Balance Sheet Information

June 30, 2018

Assets	Sheppard and Enoch Pratt Foundation, Inc.	Sheppard Pratt Health System, Inc.	Sheppard Pratt Investment, Inc.	Sheppard Pratt Physicians, P.A.	Obligated group combining eliminations	Combined obligated group subtotal	Sheppard Pratt Properties, LLC	Eliminations	Subtotal
Current assets:									
Cash and cash equivalents	$ 375,608	39,252,412	—	287,365	—	39,915,385	—	—	39,915,385
Investments limited or restricted as to use	1,520,940	—	—	—	—	1,520,940	—	—	1,520,940
Accounts receivable, net	—	24,692,649	—	1,012,856	—	25,705,505	—	—	25,705,505
Due from affiliates	5,000	846,728	2,947,929	37,435	(3,129,714)	707,378	—	(139,904)	567,474
Prepaid expenses and other current assets	—	9,058,369	—	233,915	—	9,292,284	—	—	9,292,284
Total current assets	1,901,548	73,850,158	2,947,929	1,571,571	(3,129,714)	77,141,492	—	(139,904)	77,001,588
Investments limited or restricted as to use, less current portion	14,896,976	151,283,337	135,738,666	—	—	301,918,979	—	(12,637,742)	289,281,237
Interest in net assets of Foundation	—	13,828,924	—	—	(13,828,924)	—	—	—	—
Notes receivable	—	296,478	1,745,867	—	—	2,042,345	—	—	2,042,345
Third-party payor settlements receivable	—	6,722,505	—	—	—	6,722,505	—	—	6,722,505
Property and equipment, net	—	168,755,936	—	—	—	168,755,936	12,415,774	—	181,171,710
Other assets	—	480,203	399,625	—	—	879,828	—	—	879,828
Total assets	$ 16,798,524	415,217,541	140,832,087	1,571,571	(16,958,638)	557,461,085	12,415,774	(12,777,646)	557,099,213
Liabilities and Net Assets									
Current liabilities:									
Current maturities of long-term debt	$ —	3,964,000	—	—	—	3,964,000	—	—	3,964,000
Current portion of obligations under capital leases	—	561,029	—	—	—	561,029	—	—	561,029
Accounts payable	—	6,040,794	—	89,764	—	6,130,558	—	—	6,130,558
Accrued salaries, wages and employee benefits	—	13,886,648	—	2,398,980	—	16,285,628	—	—	16,285,628
Due to affiliates	378,128	2,641,716	6,214,705	107,774	(3,129,714)	6,212,609	139,904	(139,904)	6,212,609
Self-insurance liabilities	—	3,724,138	—	269,526	—	3,993,664	—	—	3,993,664
Other accrued expenses	—	2,398,705	297,940	194,994	—	2,891,639	38,502	—	2,930,141
Total current liabilities	378,128	33,217,030	6,512,645	3,061,038	(3,129,714)	40,039,127	178,406	(139,904)	40,077,629
Long-term liabilities:									
Long-term debt, less current portion	—	172,885,901	—	—	—	172,885,901	—	—	172,885,901
Obligations under capitalized leases, less current portion	—	5,296,855	—	—	—	5,296,855	—	—	5,296,855
Self-insurance liabilities	—	6,603,522	—	—	—	6,603,522	—	—	6,603,522
Accrued pension liabilities	—	14,151,723	—	8,094,843	—	22,246,566	—	—	22,246,566
Other long-term liabilities	369,661	—	—	—	—	369,661	—	—	369,661
Total liabilities	747,789	232,155,031	6,512,645	11,155,881	(3,129,714)	247,441,632	178,406	(139,904)	247,480,134
Net assets (deficit):									
Unrestricted	1,905,349	169,109,341	134,319,442	(9,584,310)	—	295,749,822	12,237,368	(12,637,742)	295,349,448
Temporarily restricted	10,460,940	13,953,169	—	—	(13,828,924)	10,585,185	—	—	10,585,185
Permanently restricted	3,684,446	—	—	—	—	3,684,446	—	—	3,684,446
Total net assets (deficit)	16,050,735	183,062,510	134,319,442	(9,584,310)	(13,828,924)	310,019,453	12,237,368	(12,637,742)	309,619,079
Total liabilities and net assets	$ 16,798,524	415,217,541	140,832,087	1,571,571	(16,958,638)	557,461,085	12,415,774	(12,777,646)	557,099,213

(Continued)

Schedule 1

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidating Balance Sheet Information

June 30, 2018

Assets	Family Services Inc.	Mosaic Community Services, Inc.	Way Station, Inc.	Consolidating eliminations	Consolidated totals
Current assets:					
Cash and cash equivalents	$ 1,982,531	6,892,788	8,749,063	—	57,539,767
Investments limited or restricted as to use	151,493	109,263	411,413	—	2,193,109
Accounts receivable, net	2,340,947	1,994,617	1,768,909	—	31,809,978
Due from affiliates	1,738	1,249	333	(570,794)	—
Prepaid expenses and other current assets	184,820	4,212,486	2,247,195	—	15,936,785
Total current assets	4,661,529	13,210,403	13,176,913	(570,794)	107,479,639
Investments limited or restricted as to use, less current portion	—	3,878,778	6,209,290	(6,209,290)	293,160,015
Interest in net assets of Foundation	—	—	—	—	—
Notes receivable	—	—	—	(296,477)	1,745,868
Third-party payor settlements receivable	—	—	—	—	6,722,505
Property and equipment, net	9,471,083	20,428,055	22,158,739	—	233,229,587
Other assets	63,900	731,981	438,354	—	2,114,063
Total assets	$ 14,196,512	38,249,217	41,983,296	(7,076,561)	644,451,677
Liabilities and Net Assets					
Current liabilities:					
Current maturities of long-term debt	$ 215,328	983,409	457,753	—	5,620,490
Current portion of obligations under capital leases	—	—	—	—	561,029
Accounts payable	838,097	1,923,293	432,977	—	9,324,925
Accrued salaries, wages and employee benefits	1,468,233	3,890,263	1,967,747	—	23,611,871
Due to affiliates	223,952	245,040	98,482	(6,780,083)	—
Self-insurance liabilities	—	150,870	209,078	—	4,353,612
Other accrued expenses	605,107	789,507	705,293	—	5,030,048
Total current liabilities	3,350,717	7,982,382	3,871,330	(6,780,083)	48,501,975
Long-term liabilities:					
Long-term debt, less current portion	5,442,616	4,879,947	4,456,370	—	187,664,834
Obligations under capitalized leases, less current portion	—	—	—	—	5,296,855
Self-insurance liabilities	—	346,109	586,065	—	7,535,696
Accrued pension liabilities	—	—	—	—	22,246,566
Other long-term liabilities	304,651	822,025	2,318,887	(296,478)	3,518,746
Total liabilities	9,097,984	14,030,463	11,232,652	(7,076,561)	274,764,672
Net assets:					
Unrestricted	3,724,556	19,800,987	23,364,503	—	342,239,494
Temporarily restricted	1,373,972	4,167,154	7,386,141	—	23,512,452
Permanently restricted	—	250,613	—	—	3,935,059
Total net assets	5,098,528	24,218,754	30,750,644	—	369,687,005
Total liabilities and net assets	$ 14,196,512	38,249,217	41,983,296	(7,076,561)	644,451,677

See accompanying independent auditors' report.

Schedule 2

**SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES**

Consolidating Statement of Operations Information

Year ended June 30, 2018

	Sheppard and Enoch Pratt Foundation, Inc.	Sheppard Pratt Health System, Inc.	Sheppard Pratt Investment, Inc.	Sheppard Pratt Physicians, P.A.	Obligated group combining eliminations	Combined obligated group subtotal	Sheppard Pratt Properties, LLC	Eliminations	Subtotal
Unrestricted revenues, gains, and other support:									
Patient service revenue (net of allowances and discounts)	$ —	137,557,107	—	13,774,946	—	151,332,053	—	—	151,332,053
Residential and educational service revenue (net of allowances)	—	86,536,071	—	—	—	86,536,071	—	—	86,536,071
Total net service revenue	—	224,093,178	—	13,774,946	—	237,868,124	—	—	237,868,124
Less provision for bad debts	—	1,326,838	—	312,302	—	1,639,140	—	—	1,639,140
Net service revenue less provision for bad debts	—	222,766,340	—	13,462,644	—	236,228,984	—	—	236,228,984
Net assets released from restrictions used for operations	7,535	963,204	—	—	—	970,739	—	—	970,739
Other revenue	—	12,890,610	—	14,262,653	(15,674,773)	11,478,490	—	—	11,478,490
Total unrestricted revenues, gains, and other support	7,535	236,620,154	—	27,725,297	(15,674,773)	248,678,213	—	—	248,678,213
Expenses:									
Salaries and wages	—	123,743,320	—	26,525,357	—	150,268,677	—	—	150,268,677
Employee benefits	—	30,585,925	—	4,150,601	—	34,736,526	—	—	34,736,526
Expendable supplies	—	12,407,524	—	—	—	12,407,524	28,756	—	12,436,280
Purchased services	6,346	42,102,768	—	6,481,367	(15,860,398)	32,730,083	89,255	—	32,819,338
Interest	—	2,880,240	—	—	—	2,880,240	—	—	2,880,240
Repairs and minor alterations	—	7,592,136	—	—	—	7,592,136	43,964	—	7,636,100
Depreciation and amortization	—	14,631,614	—	—	—	14,631,614	238,399	—	14,870,013
Loss on disposal of assets, net	—	189,092	—	—	—	189,092	—	—	189,092
Total expenses	6,346	234,132,619	—	37,157,325	(15,860,398)	255,435,892	400,374	—	255,836,266
Operating income (loss)	1,189	2,487,535	—	(9,432,028)	185,625	(6,757,679)	(400,374)	—	(7,158,053)
Other income (expense):									
Investment income	—	449,955	1,595,502	—	(185,625)	1,859,832	—	—	1,859,832
Realized gain on investments, net	—	926,214	3,934,885	—	—	4,861,099	—	—	4,861,099
Change in unrealized gain on investments, net	—	668,410	2,830,587	—	—	3,498,997	—	—	3,498,997
Other	—	440,821	(309,246)	—	—	131,575	—	—	131,575
Total other income (expense)	—	2,485,400	8,051,728	—	(185,625)	10,351,503	—	—	10,351,503
Excess (deficiency) of revenues over expenses	1,189	4,972,935	8,051,728	(9,432,028)	—	3,593,824	(400,374)	—	3,193,450
Other changes in net assets:									
Net assets released from restrictions used for purchases of property and equipment	—	75,109	—	—	—	75,109	—	—	75,109
Transfer from (to) affiliates	—	(3,716,432)	(4,373,568)	8,090,000	—	—	12,637,742	(12,637,742)	—
Pension liability adjustment	—	8,639,418	—	—	—	8,639,418	—	—	8,639,418
Capital grants	—	2,500,000	—	—	—	2,500,000	—	—	2,500,000
Increase (decrease) in unrestricted net assets	$ 1,189	12,471,030	3,678,160	(1,342,028)	—	14,808,351	12,237,368	(12,637,742)	14,407,977

(Continued)

Schedule 2

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidating Statement of Operations Information

Year ended June 30, 2018

	Family Services Inc.	Mosaic Community Services, Inc.	Way Station, Inc.	Consolidating eliminations	Consolidated totals
Unrestricted revenues, gains, and other support:					
Patient service revenue (net of allowances and discounts)	$ —	—	—	—	151,332,053
Residential and educational service revenue (net of allowances)	13,101,859	36,991,390	25,923,047	—	162,552,367
Total net service revenue	13,101,859	36,991,390	25,923,047	—	313,884,420
Less provision for bad debts	1,215,629	373,226	161,084	—	3,389,079
Net service revenue less provision for bad debts	11,886,230	36,618,164	25,761,963	—	310,495,341
Net assets released from restrictions used for operations	89,507	16,083	113,228	—	1,189,557
Other revenue	11,587,532	26,488,662	10,104,427	(792,711)	58,866,400
Total unrestricted revenues, gains, and other support	23,563,269	63,122,909	35,979,618	(792,711)	370,551,298
Expenses:					
Salaries and wages	14,011,390	34,981,114	23,427,977	—	222,689,158
Employee benefits	2,549,131	7,033,265	4,606,647	—	48,925,569
Expendable supplies	1,388,837	2,838,700	1,672,508	—	18,336,325
Purchased services	4,414,824	13,190,933	3,419,947	(792,711)	53,052,331
Interest	244,502	271,621	157,817	—	3,554,180
Repairs and minor alterations	411,538	1,680,651	790,201	—	10,518,490
Depreciation and amortization	713,557	2,234,421	1,160,258	—	18,978,249
Loss (gain) on disposal of assets, net	3,589	(10,196)	19,683	—	202,168
Total expenses	23,737,368	62,220,509	35,255,038	(792,711)	376,256,470
Operating income (loss)	(174,099)	902,400	724,580	—	(5,705,172)
Other income (expense):					
Investment income	—	144,933	110,078	—	2,114,843
Realized gain on investments, net	—	—	152,939	—	5,014,038
Change in unrealized gain on investments, net	—	10,511	53,497	—	3,563,005
Other	—	(62,198)	—	—	69,377
Total other income	—	93,246	316,514	—	10,761,263
Excess (deficiency) of revenues over expenses	(174,099)	995,646	1,041,094	—	5,056,091
Other changes in net assets:					
Net assets released from restrictions used for purchases of property and equipment	—	—	132,011	—	207,120
Transfer from (to) affiliates	—	—	—	—	—
Pension liability adjustment	—	—	—	—	8,639,418
Capital grants	—	41,181	10,000	—	2,551,181
Increase (decrease) in unrestricted net assets	$ (174,099)	1,036,827	1,183,105	—	16,453,810

See accompanying independent auditors' report.

Schedule 3

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidating Statement of Changes in Net Assets Information

Year ended June 30, 2018

	Sheppard and Enoch Pratt Foundation, Inc.	Sheppard Pratt Health System, Inc.	Sheppard Pratt Investment, Inc.	Sheppard Pratt Physicians, P.A.	Obligated group combining eliminations	Combined obligated group subtotal	Sheppard Pratt Properties, LLC	Eliminations	Subtotal
Unrestricted net assets:									
Excess (deficiency) of revenues over expenses	$ 1,189	4,972,935	8,051,728	(9,432,028)	—	3,593,824	(400,374)	—	3,193,450
Other changes in net assets:									
Net assets released from restrictions used for purchases of property and equipment	—	75,109	—	—	—	75,109	—	—	75,109
Transfer from (to) affiliates	—	(3,716,432)	(4,373,568)	8,090,000	—	—	12,637,742	(12,637,742)	—
Pension liability adjustment	—	8,639,418	—	—	—	8,639,418	—	—	8,639,418
Capital grants and other	—	2,500,000	—	—	—	2,500,000	—	—	2,500,000
Increase (decrease) in unrestricted net assets	1,189	12,471,030	3,678,160	(1,342,028)	—	14,808,351	12,237,368	(12,637,742)	14,407,977
Temporarily restricted net assets:									
Gifts and grants	6,824,864	—	—	—	—	6,824,864	—	—	6,824,864
Investment income	75,365	—	—	—	—	75,365	—	—	75,365
Net realized gain on investments	160,731	—	—	—	—	160,731	—	—	160,731
Net unrealized gain on investments	115,623	—	—	—	—	115,623	—	—	115,623
Interest in net assets of Foundation	—	6,125,813	—	—	(6,125,813)	—	—	—	—
Transfer to affiliates	(22,498)	—	—	—	—	(22,498)	—	—	(22,498)
Net assets released from restrictions for operations	(7,535)	(963,204)	—	—	—	(970,739)	—	—	(970,739)
Net assets released from restrictions for purchases of property and equipment	—	(75,109)	—	—	—	(75,109)	—	—	(75,109)
Reclassification of net assets	(1,038,313)	1,038,313	—	—	—	—	—	—	—
Increase (decrease) in temporarily restricted net assets	6,108,237	6,125,813	—	—	(6,125,813)	6,108,237	—	—	6,108,237
Permanently restricted net assets:									
Gifts	17,576	—	—	—	—	17,576	—	—	17,576
Investment gain	8,108	—	—	—	—	8,108	—	—	8,108
Increase in permanently restricted net assets	25,684	—	—	—	—	25,684	—	—	25,684
Increase (decrease) in net assets	6,135,110	18,596,843	3,678,160	(1,342,028)	(6,125,813)	20,942,272	12,237,368	(12,637,742)	20,541,898
Net assets (deficit), beginning of year	9,915,625	164,465,668	130,641,281	(8,242,282)	(7,703,111)	289,077,181	—	—	289,077,181
Net assets (deficit), end of year	$ 16,050,735	183,062,511	134,319,441	(9,584,310)	(13,828,924)	310,019,453	12,237,368	(12,637,742)	309,619,079

(Continued)

Schedule 3

SHEPPARD AND ENOCH PRATT FOUNDATION, INC.
AND SUBSIDIARIES

Consolidating Statement of Changes in Net Assets Information

Year ended June 30, 2018

	Family Services Inc.	Mosaic Community Services, Inc.	Way Station, Inc.	Consolidating eliminations	Consolidated totals
Unrestricted net assets:					
Excess (deficiency) of revenues over expenses	$ (174,099)	995,646	1,041,094	—	5,056,091
Other changes in net assets:					
Net assets released from restrictions used for purchases of property and equipment	—	—	132,011	—	207,120
Transfer from (to) affiliates	—	—	—	—	—
Pension liability adjustment	—	—	—	—	8,639,418
Capital grants and other	—	41,181	10,000	—	2,551,181
Increase (decrease) in unrestricted net assets	(174,099)	1,036,827	1,183,105	—	16,453,810
Temporarily restricted net assets:					
Gifts and grants	631,857	(108,391)	364,688	—	7,713,018
Investment income	—	8,139	—	—	83,504
Net realized gain on investments	—	—	—	—	160,731
Net unrealized gain on investments	—	—	—	—	115,623
Interest in net assets of Foundation	—	—	—	—	—
Transfer from affiliates	18,000	4,498	—	—	—
Net assets released from restrictions for operations	(89,507)	(16,083)	(113,228)	—	(1,189,557)
Net assets released from restrictions for purchases of property and equipment	—	—	(132,011)	—	(207,120)
Reclassification of net assets	—	—	—	—	—
Increase (decrease) in temporarily restricted net assets	560,350	(111,837)	119,449	—	6,676,199
Permanently restricted net assets:					
Gifts	—	—	—	—	17,576
Investment gain	—	—	—	—	8,108
Increase in permanently restricted net assets	—	—	—	—	25,684
Increase in net assets	386,251	924,990	1,302,554	—	23,155,693
Net assets, beginning of year	4,712,277	23,293,764	29,448,090	—	346,531,312
Net assets, end of year	$ 5,098,528	24,218,754	30,750,644	—	369,687,005

See accompanying independent auditors' report.