Princeton HealthCare System Holding, Inc.

Consolidated Financial Statements and Supplemental Information
December 31, 2016 and 2015

Report of Independent Auditors

To the Board of Trustees
Princeton HealthCare System Holding, Inc.

We have audited the accompanying consolidated financial statements of Princeton HealthCare System Holding, Inc. ("PHCSH") which comprise the consolidated balance sheets as of December 31, 2016 and 2015 and the related consolidated statement of operations, changes in net assets and cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on the 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 our 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, we consider internal control relevant to PHCSH'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 PHCSH'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 Princeton HealthCare System Holding, Inc. at December 31, 2016 and December 31, 2015 and the results of its operations, changes in net assets, and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating supplemental schedules and other supplemental schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the consolidated financial statements. The consolidating and other supplemental 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 consolidating and other supplemental information is fairly stated, in all material respects, in relation to the consolidated financial statements taken as a whole. The consolidating and other supplemental information is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations and cash flows of the individual entities or business units and is not a required part of the consolidated financial statements. Accordingly, we do not express an opinion on the financial position, results of operations and cash flows of the individual entities or business units.

PricewaterhouseCoopers LLP

Philadelphia, Pennsylvania
April 21, 2017

Princeton HealthCare System Holding, Inc.
Consolidated Balance Sheets
December 31, 2016 and 2015

(dollars in thousands)

	2016	2015
Assets		
Current assets		
Cash and cash equivalents	$ 83,858	$ 58,594
Bond proceeds held by trustee	7,119	451
Patient accounts receivable, less allowance for doubtful accounts of $19,307 in 2016 and $14,003 in 2015	53,916	50,130
Investments	109,223	105,978
Pledges receivable, current	1,846	2,782
Other current assets	15,741	14,399
Land and building held for resale	7,552	10,555
Total current assets	279,255	242,889
Investments in other entities	2,601	3,533
Noncurrent investments	11,154	10,620
Property, plant, equipment and construction-in-progress, net	448,514	482,613
Pledges receivable, noncurrent	2,395	3,219
Other noncurrent assets	4,821	3,973
Total assets	$ 748,740	$ 746,847
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term debt	$ 5,418	$ 7,310
Accounts payable	30,260	28,743
Accrued expenses	25,089	29,456
Capital lease obligations	258	627
Accrued interest payable	4,788	2,345
Other current liabilities	6,718	6,267
Total current liabilities	72,531	74,748
Accrued benefit liability	40,342	46,350
Estimated third-party payable, net	4,295	4,792
Other noncurrent liabilities	14,897	13,073
Long-term debt, less current portion	297,342	296,312
Capital lease obligations, less current portion	-	258
Total liabilities	429,407	435,533
Net assets		
Unrestricted	300,790	291,613
Temporarily restricted	8,397	9,599
Permanently restricted	10,146	10,102
Total net assets	319,333	311,314
Total liabilities and net assets	$ 748,740	$ 746,847

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

Princeton HealthCare System Holding, Inc.
Consolidated Statements of Operations
Years Ended December 31, 2016 and 2015

(dollars in thousands)

	2016	2015
Unrestricted revenues, gains and other support		
Net patient service revenue before provision for bad debts	$ 463,546	$ 438,663
Less: provision for bad debts	13,812	12,135
Net patient service revenue after provision for bad debts	449,734	426,528
Other revenue	9,702	9,274
Net assets non capital released from restrictions	1,537	1,529
Total operating revenue	460,973	437,331
Expenses		
Salaries and wages	187,905	172,295
Contracted labor	10,808	11,463
Employee benefits	50,126	47,272
Supplies	72,631	66,804
Fees, utilities and other	86,805	87,206
Depreciation	40,437	40,919
Insurance	5,432	5,123
Interest	8,229	6,985
Total operating expenses	462,373	438,067
Operating loss before non recurring transactions	(1,400)	(736)
Loss on sale of assets	(415)	-
Operating loss	(1,815)	(736)
Loss on extinguishment of debt	(585)	-
Investment income and realized gain	2,891	3,316
Unrealized gain / (loss) on alternative investments	731	(24)
Excess of revenues over expenses	$ 1,222	$ 2,556

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

Princeton HealthCare System Holding, Inc.
Consolidated Statements of Changes in Net Assets
Years Ended December 31, 2016 and 2015

(dollars in thousands)

	2016	2015
Unrestricted net assets		
Excess of revenues over expenses	$ 1,222	$ 2,556
Unrealized gain / (loss) on investments	1,952	(2,256)
Net assets released from restriction	2,631	2,117
Change in minimum pension liability	3,372	4,581
Increase in unrestricted net assets	9,177	6,998
Temporarily restricted net assets		
Contributions	2,336	2,810
Investment income, net of fees	355	574
Realized (loss) / gain on investments	(18)	288
Unrealized gain / (loss) on investments	374	(718)
Net assets released from restrictions	(4,249)	(3,612)
Decrease in temporarily restricted net assets	(1,202)	(658)
Permanently restricted net assets		
Contributions	44	181
Increase in permanently restricted net assets	44	181
Increase in net assets	8,019	6,521
Net assets		
Beginning of year	311,314	304,793
End of year	$ 319,333	$ 311,314

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

Princeton HealthCare System Holding, Inc.
Consolidated Statements of Cash Flows
Years Ended December 31, 2016 and 2015

(dollars in thousands)

	2016	2015
Cash flows from operating activities		
Increase in net assets	$ 8,019	$ 6,521
Adjustments to reconcile change in net assets to cash provided by operating activities		
Depreciation	40,437	40,919
Amortization of debt premium and cost of issuance	(2,087)	-
Donated securities received	(262)	(1,447)
Net realized and unrealized (gains) losses on investments	(2,825)	2,270
Provision for bad debts	13,812	12,135
Restricted contributions received	(4,009)	(4,269)
Proceeds from sale of unrestricted donated securities	2	13
Equity in earnings of other entities	(1,667)	(1,946)
Distributions from joint ventures	1,249	2,325
Change in pension liability	(3,372)	(4,581)
Loss on sale of land held for resale	771	-
Loss on extinguishment of debt	585	-
Gain on sale of interest in joint ventures	(356)	-
Note received from sale of joint ventures	1,420	-
(Increase) decrease in		
Accounts receivable	(17,598)	(10,879)
Other current assets	(1,342)	898
Pledges receivable	1,760	2,487
Other assets	(1,433)	(282)
Increase (decrease) in		
Accounts payable	1,516	6,158
Accrued expenses	(4,367)	1,420
Current liabilities	416	2,463
Other noncurrent liabilities	2,071	(409)
Accrued interest payable	2,443	(40)
Estimated third-party receivable / payable	(497)	(501)
Accrued benefit liability	(2,636)	(237)
Net cash provided by operating activities	32,050	53,018
Cash flows from investing activities		
Purchase of investments	(36,302)	(83,818)
Proceeds from sale of investments, net of fees	35,348	45,579
Acquisitions of property, plant and equipment	(7,886)	(12,397)
Proceeds from sale of land held for resale	3,780	-
Distributions from joint ventures	286	273
(Increase) in bond proceeds held by trustee	(6,668)	(446)
Net cash (used in) investing activities	(11,442)	(50,809)
Cash flows from financing activities		
Repayment of long-term debt	(301,123)	(7,035)
Proceeds from Series 2016 debt issuance	275,065	-
Proceeds from premium on Series 2016 debt issuance	28,720	-
Payment of cost of isssuance on Series 2016 debt	(3,038)	-
Proceeds from medical equipment loan	1,390	-
Payments under capital lease obligations	(627)	(685)
Restricted contributions received	4,009	4,269
Proceeds from sale of restricted donated securities	260	1,435
Net cash provided by / (used in) financing activities	4,656	(2,016)
Net change in cash and cash equivalents	25,264	193
Cash and cash equivalents		
Beginning of year	58,594	58,401
End of year	$ 83,858	$ 58,594
Supplemental information		
Cash paid for interest expense	$ 7,874	$ 7,118

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

(dollars in thousands)

1. Nature of Operations

Organization: Princeton HealthCare System Holding, Inc. ("PHCSH"), and its not-for-profit and for-profit members provide healthcare services primarily to residents of the greater Princeton area including Mercer, Middlesex, and Somerset counties in central New Jersey.

Basis of Presentation: The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates include contractual allowance, allowance for doubtful accounts, estimated third-party adjustments, self-insurance and accrued employee benefits. Actual results could differ from those estimates.

Principles of Consolidation: The consolidated financial statements include the accounts of PHCSH, a not-for-profit holding corporation, its controlled member not-for-profit subsidiaries, Princeton HealthCare System (the "System"), Princeton HealthCare System Foundation, Inc. (the "Foundation"), Princeton Medical Properties, Inc. ("PMP"), Princeton Caregivers ("PCG"), its wholly owned for-profit subsidiaries Princeton Health, Inc. ("PHI") and Princeton HealthCare Affiliated Physicians d/b/a Princeton Medicine.

All significant intercompany balances and transactions have been eliminated in consolidation. Although these entities have been consolidated for financial statement presentation, there may be limitations, due to the charitable nature of some of the consolidated entities or other factors, on the use of the consolidated entity's net assets by another member of the affiliated group.

The System is comprised of three divisions. The University Medical Center of Princeton at Plainsboro ("UMCPP") is an acute care facility licensed for 319 acute care beds (including 14 special care nursery bassinets and 17 physical rehabilitation beds). Princeton House Behavioral Health is a 110-bed psychiatric and behavioral health facility. Princeton HomeCare Services provides home nursing care, home rehabilitation, homemaker services, and operates a hospice program.

The Foundation supports and maintains programs, services, and facilities through the solicitation, receipt, administration and distribution of philanthropic gifts for the sole benefit of PHCSH.

PMP was formed for the purpose of acquiring, constructing, financing and holding property for the benefit of PHCSH.

PCG's primary business activity is providing private duty home care services.

PHI is the sole shareholder of Princeton HealthCare Management Services, Inc. ("PMS"). PMS provides management and administrative support to physician practices owned by the System and to private physician practices. PHI is also a partner in joint ventures with Princeton Fitness & Wellness Center, Princeton Endoscopy Center, LLC and Princeton Fitness & Wellness Center at Plainsboro.

(dollars in thousands)

Princeton Medicine is a Captive PC and is structured as a professional corporation pursuant to the provisions of the Professional Services Corporation Act of New Jersey. Princeton Medicine is incorporated outside of PHCSH. Because the System retains reserve power of control and authority, and because Princeton Medicine is financially dependent on the System for its operations and funding it is consolidated for financial reporting purposes. Princeton Medicine's purpose is to provide physician services to further the charitable and health care purposes of the System.

In the Other Supplemental Schedules, financial information of Princeton HealthCare System Obligated Group is included. The Obligated Group consists of the System and the Foundation and is the guarantor of PHCSH's long-term debt.

2. Summary of Significant Accounting Policies

The following is a summary of PHCSH's significant accounting policies:

Cash and Cash Equivalents: Cash and cash equivalents include highly liquid short term investments purchased with original maturities of three months or less. PHCSH maintained cash balances in bank accounts that exceed insured limits set by the Federal Deposit Insurance Corporation (FDIC). PHCSH has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on its cash and cash equivalents.

Bond Proceeds Held by Trustee: The balances of these funds represent deposits with the trustee for principal and interest payments on the 2016 Series A Debt on the Consolidated Balance Sheets. The Bank of New York Mellon serves as the Master Trustee of the bond offering and manages the short term investment and disbursement of funds to the bondholders. The proceeds are invested in a fixed income mutual fund.

Temporarily and Permanently Restricted Net Assets: PHCSH accounts for and reports restricted and unrestricted assets separately. Restricted assets are assets whose use is limited by the gift agreement. Assets arising from the results of operations or assets set aside for board-designated purposes are not considered to be restricted. Restricted assets, or the income on those assets, are generally available to support healthcare services. Cumulative losses to individual funds in excess of restricted amounts are classified as unrestricted net assets.

Temporarily restricted net assets are those whose use by PHCSH has been limited by contributions for a specific time period and/or purpose. PHCSH's policy is to exclude from operating income, net assets released from capital restrictions. Net assets released from restrictions for noncapital purposes are included within other operating revenue.

Permanently restricted net assets have been restricted by gift agreements to be maintained by PHCSH in perpetuity.

Property, Plant and Equipment: Property, plant and equipment are stated at cost. Depreciation is provided on a straight-line basis over the estimated useful lives as follows:

Building and improvements	10–40 years
Fixed equipment	5–20 years
Moveable equipment	4–20 years
Information technology related	3–7 years

(dollars in thousands)

Capitalized leases are recorded at their present value of future cash flows at the inception of the lease. Equipment under capital leases is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation in the financial statements. Gains and losses resulting from the retirement of property, plant and equipment are included in the results of operations.

Gifts of long-lived assets such as property, plant and equipment are determined at the fair value at the date of the gift and reported as an increase to unrestricted net assets 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.

Land and Building Held for Resale: As of December 31, 2015 the System owned certain properties contiguous to its hospital campus for which it had numerous contracts to sell for certain healthcare related services (child care, adult day care, assisted living and independent living) to unrelated third parties with a book value of $10,555. During 2016, the child care, adult day care, and assisted living properties were sold and closed. These properties had a book value of $4,551. The independent living property is anticipated to close in 2017. The Foundation owns the land and building that houses the Foundation's offices in West Windsor, NJ. As of December 31, 2016, the Foundation has a signed contract to sell the property with a net book value $1,548 to an unrelated third party. The cost of these properties has been reclassified to a current asset.

Impairment of Long-Lived Assets: Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the sum for the expected future undiscounted cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between the fair value and carrying value of the asset. No impairment losses were recorded for the years ended December 31, 2016 and 2015.

Deferred Financing Costs: Deferred financing costs are being amortized over the period the applicable obligation is outstanding using the effective interest method in 2016. Deferred financing costs were amortized using the straight-line method in 2015, which was not materially different than the effective interest method. Amortization expenses related to deferred financing costs were $190 and $30 for years ended December 31, 2016 and 2015, respectively.

Investments in Other Entities: Investments in other entities in which the System and PHI have an ownership interest less than or equal to 50% are accounted for by the equity method. Under such method, the System's and PHI's share of net earnings (or losses) is included in the consolidated statements of operations.

Net Patient Service Revenue and Patient Accounts Receivable: Net patient service revenue is accounted for on the accrual basis in the period in which the service is provided. The System, Caregivers and Princeton Medicine are reimbursed from third party payers under various methodologies based on the level of care provided. Net revenues received are subject to audit and retroactive adjustments for which estimates are made and reserves are established.

(dollars in thousands)

A summary of the payment arrangements with major third-party payers is as follows:

- Medicare – Inpatient services and outpatient services rendered to Medicare program beneficiaries are paid prospectively at set rates. Inpatient rates only vary according to a patient classification system that is based on clinical, diagnostic and other factors. The System is reimbursed for certain items such as graduate medical education costs which are subject to base year limits at a tentative rate with final settlement determined after submission of the annual cost report and audits thereof by the Medicare fiscal intermediary. Services billed to the Medicare program are subject to external review for both medical necessity and billing compliance. Medicare cost reports for all years up to 2013 have been audited and final settled as of December 31, 2016.

- Medicaid – Inpatient acute care services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Non-acute services such as rehabilitation and behavioral health services are paid based on a base year cost per case inflated forward. Most outpatient services are paid based upon a cost reimbursement methodology and certain services, such as outpatient behavioral health services, are paid based on a Medicaid fee schedule. The System is paid for reimbursable costs at a tentative rate with final settlement determined after submission of the annual cost report and audit thereof by the New Jersey Division of Medical Assistance and Health Services. Medicaid cost reports for all years up to 2014 have been final settled as of December 31, 2016.

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

Supplies: Supplies are carried at the lower of cost or market using the average cost method.

Other Current Assets: Other current assets are comprised primarily of prepaid expenses, inventory, and non-patient accounts receivable.

Other Noncurrent Assets: Other noncurrent assets are comprised primarily of estimated insurance recoverables.

Accrued Expenses: Accrued expenses include employee wage and benefit expenses as well as accruals for goods and services received but not yet invoiced.

Other Noncurrent Liabilities: Other noncurrent liabilities are comprised primarily of deferred revenues and estimated professional liability reserves. The deferred revenues relate to a 70-year ground lease for the Medical Arts Pavilion and a 60-year prepaid rent agreement with the Princeton Fitness & Wellness Center at Plainsboro.

Investments and Fair Value Measurement: Investments are measured at fair value at the balance sheet date. The investments are governed by the Board of Trustees and the Board's Investment Committee. The investment portfolio serves both as collateral for the outstanding bank debt of the Obligated Group and a general liquidity vehicle.

(dollars in thousands)

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheet. Fair value is generally determined by sales prices or bid-and-asked quotations that are available on a securities exchange registered with the Securities and Exchange Commission or in the over-the-counter market. For investments in mutual funds, the fair value per share, or unit, is the value that is determined and published and the basis for current transactions. Realized gains and losses on investments, interest and dividends, are included in "Investment income" on the statement of operations and "Unrealized gains and losses on investments, net" are included on the statement of changes in net assets, unless the income or loss is restricted by the gift agreement or law.

Noncurrent investments are investments restricted by the gift agreement.

The FASB issued a standard on fair value that provides a framework for measuring fair value and expands disclosures required for fair value measurements. The standard emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participant would use in pricing the asset or liability. As a basis for considering market participation assumptions in fair value measurements, the standard establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumption about market participation assumptions (unobservable inputs classified within Level 3 of the hierarchy).

The standard classifies the inputs used to measure the fair value into the following hierarchy:

Level 1 Level 1 valuations are based on unadjusted quoted market based prices for identical assets, exchange traded securities, mutual funds and actual transactions in an active market. Mutual funds are valued daily with net asset values retrievable with pricing sources such as Bloomberg.

Level 2 Level 2 valuations include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3 Level 3 valuations relate to unobservable inputs derived from extrapolation or interpolation that cannot be substantiated by market data including other investment manager specific inputs such as projected cash flows. These investments are valued by the fund manager, based on the pro-rata interest in the net assets of the underlying investments, which approximates fair value, and by financial information provided by the manager.

Categorization within the hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

(dollars in thousands)

Effective January 1, 2016, the System elected to adopt the standard on Fair Value Measurement Disclosure for Investments in Certain Entities That Calculate Net Asset Value per Share (or its Equivalent). Under the new guidance, investments measured at net asset value (NAV), as a practical expedient for fair value are excluded from the fair value hierarchy. In addition, when the NAV as practical expedient is not applied to eligible investments, certain other disclosures regarding nature and risks of investments are no longer required. The effects of adopting this amendment are addressed in Notes 3 and 11. Both the December 31, 2016 and 2015 amounts have been updated to conform with this presentation.

Restricted Gifts: Signed unconditional gift agreements to give cash are reported at fair value at the date the agreement is received. The gifts are reported as either temporarily or permanently restricted support if they are received with stipulations that limit the use of the donated assets. When a temporary restriction expires, that is, when a stipulated time restriction ends or specific purpose restriction is accomplished, they are reclassified as unrestricted net assets and reported in the statement of operations as net assets released from restrictions. Net assets released from restrictions for noncapital purposes are included within other operating revenue.

Performance Indicator: The consolidated statements of operations and changes in net assets include excess of revenue over expenses as the performance indicator. Consistent with industry practice, changes in unrestricted net assets excluded from excess of revenue over expenses include net assets released from restrictions for equipment purchases, forgiveness of debt of related party, permanent transfers of assets to and from affiliates for other than goods and services, contributions of long-lived assets (including donor restricted), changes to the pension liability, and unrealized gain and loss on investments.

Self-Insurance Plan: PHCSH maintains self-insured medical and dental plans and a large deductible workers' compensation plan. Claim expenses are accrued as the incidents occur. Unpaid accrued claim expenses (including estimates of the ultimate costs for both reported claims and claims incurred but not reported) are estimated based upon standard industry reserve factors and actual experience. Unpaid accrued claim expenses are reported as accrued expenses in the accompanying consolidated balance sheets. PHCSH purchases a stop loss commercial insurance policy to supplement its self-insured medical and pharmaceutical plans. This policy covers losses in excess of $300 per covered individual on an annual basis. Both estimated liabilities are included on the balance sheet in other noncurrent liabilities.

Professional Liability Insurance: PHCSH maintains a claims-made policy with various retroactive dates under several policies. The policies include a provision for prior acts coverage. Premiums are calculated based on PHCSH's exposures, loss experience and rates in effect at time of renewal. PHCSH also accrued estimated liabilities for instances that have occurred prior to the balance sheet date. The estimate of the gross liability and corresponding receivable for unasserted claims arising from unreported incidents is based on analysis of historical claims data by an independent actuary, which is recorded utilizing a 3.25% discount rate as of December 31, 2016 and 2015. As of December 31, 2016 and 2015, PHCSH recorded an insurance liability and corresponding receivable of $3,482 and $2,896, respectively, for claims that have been reported to its commercial insurance carrier and PHCSH also recorded estimated accrued liabilities of $2,268 and $2,158, respectively, for instances that have occurred prior to the balance sheet date for which a claim has not yet been made (incurred but not reported claims, also known as IBNR). Both estimated liabilities are included on the balance sheet in other noncurrent liabilities and the estimated insurance recoverable is included in other noncurrent assets.

(dollars in thousands)

Income Taxes: PHCSH, the System, Foundation, PMP, Princeton Medicine and PCG individually qualify as tax-exempt organizations under existing provisions of the Internal Revenue Code as described in Section 501(c). Per the requirement to assess for tax uncertainty, management has determined that it does not have any uncertain tax positions required to be accrued or reported.

Reclassifications: Certain prior year balances have been reclassified to be consistent with the current year presentation.

New Accounting Pronouncements*:* In May 2014, the FASB issued a standard on Revenue from Contracts with Customers. This standard implements a single framework for recognition of all revenue earned from customers. This framework ensures that entities appropriately reflect the consideration to which they expect to be entitled in exchange for goods and services by allocating transaction price to identified performance obligations and recognizing revenue as performance obligations are satisfied. Qualitative and quantitative disclosures are required to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The standard is effective for fiscal years beginning after December 15, 2016. PHCSH is evaluating the impact this will have on the consolidated financial statements beginning in Fiscal Year 2017.

Effective January 1, 2016, the System adopted Accounting Standard Update, Interest – Imputation of Interest, Simplifying the Presentation of Debt Issuance Costs. The new guidance requires that debt issuance costs be netted against the carrying value of the liability consistent with debt premium and discount. The effects of adopting this are addressed in Note 10. 2015 presentation has not been adjusted due to immateriality. Deferred financing costs associated with the Series 2016 Bonds, included with long-term debt, were $2,848 at December 31, 2016. Deferred financing costs associated with the 2011 bonds and bank loans, included with other assets, were $585 at December 31, 2015.

In January 2016, the FASB issued a standard on Financial Instruments – Overall, Recognition and Measurement of Financial Assets and Financial Liabilities. This guidance supersedes the guidance to classify equity securities with readily determinable fair values into different categories, and requires equity securities to be measured at fair value with changes in the fair value recognized through net income. This guidance allows equity investments without readily determinable fair values to be remeasured at fair value either upon the occurrence of an observable price change or upon identification of an impairment and requires additional disclosures regarding these investments. This guidance is effective for PHCSH on January 1, 2019. PHCSH is currently evaluating the impact of adopting this guidance on the consolidated financial statements.

In February 2016, the FASB issued a standard on Leases. This guidance is effective for PHCSH on January 1, 2019. The most significant change from current practice is that this guidance requires the recognition of lease assets and liabilities for those leases classified as operating leases under current guidance. The guidance also provides guidance for the measurement of lease assets and liabilities and additional required disclosures. This guidance is effective for PHCSH on January 1, 2019 with modified retrospective presentation required. PHCSH is currently evaluating the impact of adopting this guidance on PHCSH's consolidated financial statements.

(dollars in thousands)

In January 2016, the FASB issued a standard on Recognition and Measurement of Financial Assets and Liabilities. This standard changes the accounting for equity investments and eliminates the requirement to disclose the fair value of financial instruments measured at amortized costs for non-public entities. PHCSH has early adopted this standard for the year ended December 31, 2016. As a result of the adoption, PHCSH eliminated the footnote disclosure of fair value for its bond obligations, which are measured at amortized cost.

In August 2016, the FASB issued a standard on the Presentation of Financial Statements of Not-for-Profit Entities. The new guidance requires improved presentation and disclosures to help not-for-profits provide more relevant information about their resources to donors, grantor, creditors and other users. The standard is effective for fiscal years beginning after December 15, 2017. PHCSH Management is evaluating the impact this will have on the consolidated financial statements beginning in Fiscal Year 2018.

Subsequent Events:

PHCSH has evaluated subsequent events in accordance with the statements through April 21, 2017. In December 2016, the PHCSH's Board of Trustees and the University of Pennsylvania's Board of Trustees have approved plans for Princeton HealthCare System (PHCS) to become a part of the University of Pennsylvania Health System. The agreement is contingent upon agreed upon closing conditions, including final approval by state (New Jersey and Pennsylvania) and federal authorities which is expected to take a year or more.

Penn Medicine is one of the world's leading academic medical centers, dedicated to the related missions of medical education, biomedical research, and excellence in patient care. PHCS believes that affiliating with Penn Medicine represents the best means of assuring that PHCS and its affiliates can continue to fulfill their mission and charitable objectives in the future. The Princeton HealthCare System Foundation will remain independent from the University of Pennsylvania and will continue to conduct charitable activities for the benefit of PHCSH.

3. Fair Value Measurements

All PHCSH investments (pension and non-pension) are under management of SEI or Grosvenor. Both use a manager-of-manager platform. Valuations are based on identifiable market transactions leading to a price. SEI manages alternative investment pension investments along with Grosvenor (Note 11). PHCSH considers observable data to be market data which is readily available, regularly distributed or updated, reliable and verifiable and provided by an independent source actively involved in the relevant market. The categorization of a financial instrument within the hierarchy is based upon the pricing transparency of the instrument and does not necessarily correspond to the PHCSH perceived risk of those investments.

The Grosvenor funds are invested in a globally diversified, multi-strategy, multi-manager portfolio that allocates its assets to hedge fund managers that specialize in a wide range of alternative investment strategies including: credit, relative value, multi-strategy, event driven, equities, macro, commodities and portfolio hedges. The alternative investment funds are measured at NAV, as reported by external managers, as a practical expedient for the fair value, and are excluded from the fair value hierarchy.

(dollars in thousands)

There are three primary investment objectives of Grosvenor as alternative investments: (1) to provide an additional source of investment diversification as these funds are less correlated to equity and fixed income markets, (2) to generate a superior absolute and risk-adjusted rate of return, with low performance volatility and low correlation with global equity and fixed income markets, over a full market cycle, and (3) to preserve capital during challenging market environments.

The pension plan investments in SEI's private equity are in the form of limited partnership interests. The fund managers primarily invest in private investments for which there is no readily determinable market value. The fund manager may value the underlying private investments based on an appraised value, discounted cash flow, industry comparables or some other method.

The table below summarizes the non-pension assets that are measured at fair value on a recurring basis in the balance sheet, including $42 and $33 of accrued interest for 2016 and 2015, respectively. No liabilities exist that are subject to this guidance.

Investment Holdings – by Level
Basis of Fair Value Measurements as of December 31, 2016

	Total	Level 1	Level 2	Level 3
Fixed income securities	$ 3,789	$ 3,789	$ -	$ -
Fixed income mutual funds	52,724	52,724	-	-
Domestic equity mutual funds	30,035	30,035	-	-
International equity mutual funds	16,116	16,116	-	-
Investments subject to fair value leveling	102,664	$ 102,664	$ -	$ -
Investments measured using the practical expedient	17,713			
Total	$ 120,377			

Basis of Fair Value Measurements as of December 31, 2015

	Total	Level 1	Level 2	Level 3
Fixed income securities	$ 23,987	$ 23,987	$ -	$ -
Fixed income mutual funds	46,298	46,298	-	-
Domestic equity mutual funds	20,831	20,831	-	-
International equity mutual funds	13,325	13,325	-	-
Investments subject to fair value leveling	104,441	$ 104,441	$ -	$ -
Investments measured using the practical expedient	12,157			
Total	$ 116,598			

Included in the above table are Level 1 gift annuities of $185 and $177 at December 31, 2016 and 2015, respectively. The liabilities associated with the gift annuities have been recorded by PHCSH as other liabilities on the balance sheet. The amounts were $35 at both December 31, 2016 and 2015.

(dollars in thousands)

No unfunded commitments existed on December 31, 2016 or 2015.

4. Net Assets

Temporarily restricted net assets are those whose use by the PHCSH has been limited by contributions for a specific time period or purpose. Temporarily restricted net assets are available for the following purposes:

	2016	2015
Facility non programmatic support	$ 3,744	$ 4,911
Healthcare programmatic support	3,420	3,408
Foundation general operations	1,096	1,207
Religious Ministries	136	73
	$ 8,397	$ 9,599

PHCSH's endowment consists of twelve permanently restricted individual funds established for a variety of purposes. As required by GAAP, net assets associated with endowment funds, are classified and reported based on the existence of restrictions. The Board of Trustees of the System has interpreted the State of New Jersey's enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA) as requiring the preservation of the historic dollar value of endowment funds (absent explicit stipulations to the contrary). As a result of this interpretation, PHCSH classifies as permanently restricted net assets (a) the original value of gifts donated to the permanently restricted net assets (b) the original value of subsequent gifts to the permanent endowment (c) the net realizable value of future payments to permanently restricted net assets in accordance with the gift agreement (outstanding endowment pledges net of applicable discount) and (d) appreciation (depreciation), gains (losses) and income earned on the fund when the gift agreement states that such increases or decreases are to be treated as changes in permanently restricted net assets.

The Board of Trustees further understands that expenditure from an endowment fund is limited to the uses and purposes for which the fund is established and the use of net appreciation, realized gains (with respect to all assets) and unrealized gains (with respect only to readily marketable assets) is limited to the extent the fair value of the fund exceeds the historic dollar value of the fund (unless the applicable gift agreement indicates that net appreciation shall not be expended) to the extent that such expenditure is prudent, considering the long and short term needs of PHCSH in carrying out its purposes, its present and anticipated financial requirements, expected total return on its investments, price level trends and general economic conditions.

PHCSH's endowment investments fall under the investment policy guidelines as established, and reviewed annually, by the System's Investment Committee expenditure, based on a twelve quarter rolling market value average, was approved. PHCSH's endowment policy and procedures allows for a maximum annual expenditure of 6%, based on a twelve quarter rolling market value average, with 2% being expended in 2016.

PHCSH's endowment spending policies are consistent with the gift agreement's objectives to utilize income to support mission-critical programs while ensuring the preservation of capital and long-term endowment growth.

(dollars in thousands)

Changes in endowment net assets for the fiscal year ended December 31, 2016 consisted of the following:

	Temporarily Restricted	Permanently Restricted
Endowment net assets, beginning of year	$ 391	$ 10,102
Investment return:		
Investment income	352	-
Realized and unrealized gains	357	-
Total investment gain	709	-
Contributions and pledges	-	41
Amortization of pledge discounts and bad debt write off	-	3
Appropriation of endowment assets for expenditure	(216)	-
Endowment net assets, end of year	$ 884	$ 10,146

Changes in endowment net assets for the fiscal year ended December 31, 2015 consisted of the following:

	Temporarily Restricted	Permanently Restricted
Endowment net assets, beginning of year	$ 365	$ 9,921
Investment return:		
Investment income	573	-
Realized and unrealized (losses)	(427)	-
Total investment gain	146	-
Contributions and pledges	-	143
Amortization of pledge discounts and bad debt write off	-	38
Appropriation of endowment assets for expenditure	(120)	-
Endowment net assets, end of year	$ 391	$ 10,102

(dollars in thousands)

Permanently restricted net assets, net of pledge discounts, are held in perpetuity as endowments for the following purposes:

	2016	2015
Community Health Center	$ 2,287	$ 2,287
Cardiac and Pulmonary Care Center	2,000	2,000
Total Joint Replacement Center	2,000	2,000
Geriatric care	1,992	1,992
Religious ministries programs	1,077	1,038
Art Gallery at UMCPP	299	299
Nursing development	249	247
Orthopedic nursing education	100	100
Volunteer services	71	71
Medical grand rounds lecture	46	43
OR staff professional development	25	25
	$ 10,146	$ 10,102

5. Functional Expenses

PHCSH provides general healthcare services to residents within its geographic area. Expenses related to providing these services for the years ended December 31, 2016 and 2015 are as follows:

	2016	2015
Healthcare services	$ 355,911	$ 322,252
General and administrative	104,535	113,569
Fundraising	1,927	2,246
	$ 462,373	$ 438,067

6. Reimbursement

PHCSH records gross patient service revenue on an accrual basis at established rates, with contractual and other allowances deducted from such amounts to determine net patient service revenue, before provision for bad debts. PHCSH maintains policies and records to identify and monitor these contractual allowances and its level of charity care. These records include the amount of deductions from gross revenue due to qualified services provided under the State of New Jersey's charity care guidelines.

(dollars in thousands)

The process for estimating the collection of receivables involves significant assumptions and judgments. For each business entity, the System has implemented a monthly standardized approach to estimate and review the collectability of receivables by services based on (inpatient versus outpatient) the payer classification and the period from which the receivables have been outstanding. Account balances are written off against the allowance or bad debt expense (for self-pay balances) when management feels it is probable the receivable will not be recovered. Historical collection and payer reimbursement experience is an integral part of the estimation process related to reserves for doubtful accounts. In addition, the System assesses the current state of its billing functions in order to identify any known collection or reimbursement issues and assess the impact, if any, on reserve estimates.

PHCSH derives its gross patient service revenue for inpatient and outpatient services from the following payers at December 31:

	2016	2015
Medicare and Medicaid (Traditional and Managed)	47 %	46 %
Managed Care	14	15
Blue Cross	18	18
Aetna	12	12
Commercial and other	6	6
Self-pay patients	3	3
	100 %	100 %

Net patient service revenue consists of the following at December 31:

	2016	2015
Gross charges	$ 1,888,577	$ 1,771,783
Contractual and other allowances	(1,438,843)	(1,345,255)
Net patient service revenue after provision for bad debts	$ 449,734	$ 426,528

(dollars in thousands)

Charity Care

The System provides care to patients who meet certain criteria defined by the New Jersey Department of Health and Senior Services ("DOHSS") without charge or at amounts less than its established rates. The majority of patients qualify for charity care where household income is less than 200% of the family federal poverty guidelines or their financial condition is such that requiring payment would impose a hardship on the patient. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The System's records identify and monitor the level of charity care it provides and the amount of charges foregone for services and supplies furnished. The costs associated with charity care during the years ended December 31, 2016 and 2015 were approximately $6,903 and $7,321, respectively. The estimated cost of providing charity services is based on valuing all charity care claims using the System's decision support system that utilizes cost to charge ratios derived from the most recently filed Medicare cost reports. DOHSS charity care guidelines require participation and specific documentation of the patient in order to be identified as a charity care account. In addition to charity care, the System provides a significant amount of community benefit that includes community outreach programs, subsidized medical education costs and unreimbursed costs of providing care to Medicare and Medicaid beneficiaries.

The New Jersey Health Care Subsidy Fund was established for various purposes including the distribution of charity care and hospital relief fund payments to hospitals statewide. As of December 31, 2016 and 2015, the System received subsidy amounts of $835 and $1,519, respectively, which are included in net patient service revenue.

Additionally, the State of New Jersey established a Mental Health Subsidy Fund to pay for specific behavioral health services. The System received $1,257 for these services in both 2016 and 2015.

7. Investment Return

A summary of the total investment return for the years ended December 31 is as follows:

	2016	2015
Interest and dividend income, net of fees	$ 2,871	$ 2,876
Realized gain on sales of securities	20	440
Net unrealized gain / (loss) on alternative investments	731	(24)
Net unrealized gain / (loss) on investments	1,952	(2,256)
Unrestricted total investment return	5,574	1,036
Interest and dividend income, net of fees	355	574
Realized (loss) / gain on investments	(18)	288
Unrealized gain / (loss) on investments	374	(718)
Temporarily restricted total investment return	711	144
Total investment return	$ 6,285	$ 1,180

(dollars in thousands)

8. Investments in Other Entities

The net book value of the PHCSH's investments in other entities represents PHCSH's initial capital investment plus PHCSH's share of the income less PHCSH's share of the distributions received since the commencement of the joint venture.

The System was a 50% general partner in Princeton Radiology Oncology Center ("PROC"), a free-standing radiation oncology treatment center located in Monroe Township, New Jersey. On December 22, 2016, the System sold its 50% interest to Hopewell Radiology Group Limited Partnership (Hopewell Radiology), the other 50% general partner. The current amount of the investment was $0 and $304 at December 31, 2016 and 2015, respectively.

The System was a 50% general partner in Princeton Imaging Ventures ("PIV"), a free-standing imaging center with locations in Monroe Township and Princeton New Jersey. On December 22, 2016, the System sold its 50% interest to Hopewell Radiology, the other 50% general partner. The current amount of the investment was $0 and $162 at December 31, 2016 and 2015, respectively.

The System was a 50% owner in Imaging Ventures of Princeton ("IVP"), a limited liability corporation imaging center. IVP also owns 50% of both Windsor Imaging Center ("WIC") and Hillsborough Imaging Center ("HIC"), which are free-standing imaging centers located in their respective towns in central New Jersey. On December 22, 2016, the System sold its 50% interest to Hopewell Radiology, the other 50% general partner. The current amount of the investment in the corporation was $0 and $463 at December 31, 2016 and 2015, respectively.

The following is a summary of PROC, PIV and IVP's investment balances as of the date of the sale, notes received from the purchaser and gain recognized:

	PROC	PIV	IVP	Total
Investment balance as of Investment date	$ 657	$ (80)	$ 487	$ 1,064
Sales price received in the form of a note	657	115	648	1,420
Gain on the sale	$ -	$ 195	$ 161	$ 356

The gain on the sale disclosed within "gain/loss on sale of assets". Notes received by the System from Hopewell Radiology are payable in 36 monthly installments beginning January 2017 and ending in December 2019. The notes bear interest at the Applicable Federal Rate as of December 22, 2016 which was 0.74% per annum.

The System has a 26.47% ownership in UMCP SurgiCenter Partners, LLC, a corporation formed with physicians and physician practices to provide administrative services, medical oversight, management services, equipment, supplies and certain nonclinical personnel to the outpatient surgery center owned by the System and located on UMCPP's Plainsboro campus. The current amount of the investment was $643 and $539 at December 31, 2016 and 2015, respectively.

The System has a 20% ownership in UMCP-Monroe Surgical Partners, LLC, a corporation formed with Forsgate ASC Partners, LLC to provide, among other things, certain administrative services, medical oversight, management services, equipment, supplies and certain non-clinical personnel to

(dollars in thousands)

the outpatient surgery center owned by the System and located in Monroe Township, New Jersey. The current amount of the investment was $72 and $23 at December 31, 2016 and 2015, respectively.

PHI is a 25% partner in Princeton Fitness & Wellness Center ("PF&WC"), a for-profit joint venture located in Princeton, New Jersey. The current amount of the investment in PF&WC was $307 and $298 as of December 31, 2016 and 2015, respectively.

PHI is a 47.5% owner in Princeton Endoscopy Center, LLC, ("PEC") a for-profit corporation located in Princeton, New Jersey. The current amount of the investment in PEC was $202 and $208 as of December 31, 2016 and 2015, respectively.

PHI is a 25% partner in Princeton Fitness & Wellness Center at Plainsboro ("PF&WCP"), a for-profit joint venture located on UMCPP's Plainsboro campus. The current amount of the investment in PF&WCP was $1,376 and $1,536 as of December 31, 2016 and 2015, respectively.

9. Property, Plant, Equipment and Construction-in-Progress

Property, plant, equipment and construction-in-progress consist of the following at December 31:

	2016	2015
Land	$ 39,812	$ 40,435
Land improvements	26,661	26,341
Buildings and leasehold improvements	473,272	473,982
Furniture and equipment	101,693	97,815
Information technology related	40,610	36,161
Construction-in-progress	1,164	2,981
	683,212	677,715
Less: Accumulated depreciation	234,698	195,102
Property, plant, equipment and construction-in-progress, net	$ 448,514	$ 482,613

Depreciation expense for the years ended December 31, 2016 and 2015 was $40,437 and $40,919, respectively.

(dollars in thousands)

10. Long-Term Debt and Capital Lease Obligations

Long-term debt and capital lease obligations consist of the following at December 31:

	2016	2015
Long term debt		
2016 Series A revenue bonds		
$190,065 tax exempt plus $28,720 of Original Issue Premium, with stated interest rates between 2% and 5% with yields to maturity estimated between 0.5% and 4.075%. Total interest costs are estimated at 3.66%.	$ 188,030	$ -
2016 Series B Bank placement bonds		
$65,000, Wells Fargo, tax exempt direct loan at 70% of the 30-day LIBOR plus 75 basis points. Monthly rate ranged from 1.048% to 1.180% in 2016.	65,000	
2016 Series C Bank placement bonds		
$20,000, Bank of America, tax exempt direct loan at 67% of the 30-day LIBOR plus 95 basis points. Monthly rate ranged from 1.238% to 1.370% in 2016.	20,000	
Wells Fargo term loan		
$1,390, Wells Fargo 4-year term loan collateralized by medical equipment. 48 equal monthly installments with a 2.4% interest rate.	1,251	
Park Assessment Bond		
$7,120 Plainsboro Township special assessment. 15 year annual installments, terminating on April 1, 2026 with a 3.836% interest rate.	4,828	5,162
Bank of America loan		
$125,000, Bank of America, was remarketed in 2011 from a weekly rate bond secured by a letter of credit to a taxable, direct loan with a variable weekly rate that ranged from 1.55% to 1.64% in 2015.	-	104,955
2010 Series B bond		
$55,000, TD Bank, was remarketed in 2011 from a weekly rate bond secured by a letter of credit to tax exempt, direct purchase bonds with a variable weekly rate that ranged from 2.09% to 2.15% in 2015.	-	46,190
2010 Series C bond		
$100,000, Wells Fargo Bank, was modified in 2011 from index rate bonds to 2.79% fixed rate bonds, but still tax exempt and directly purchased.	-	84,335
2010 Series D bond		
$75,000, JPMorgan Chase Bank, was modified in 2011 from index bonds to 2.7% fixed rate bonds, but still tax exempt and directly purchased.	-	62,980
Unamortized premium paid at issuance of 2016 Series A bonds. (Original Issue premium was $28,720)	26,499	-
Unamortized cost of issuance - 2016 Series A, B, and C	(2,848)	-
Total long-term debt	302,760	303,622
Less: Current portion	5,418	7,310
Long-term debt, net of current portion	$ 297,342	$ 296,312
Capital lease obligations		
Canon Business Solutions commitment of $1,490 for Imagerunner equipment commenced on April 20, 2012 and will terminate on June 30, 2017.	$ 163	$ 478
Bank of America loan commitment of $1,052 for McKesson MedCarousel commenced on December 9, 2011, first payment due June 2012 and will terminate May 2017. The annual interest rate is 3.49%	95	317
Stryker Finance loan commitment of $448 for surgical medical equipment commenced on December 21, 2012, first payment due August 2013, and will terminate in July 2016. The annual interest rate is 2.25%.	-	90
Total obligation under capital leases	258	885
Less: Current portion	258	627
Obligation under capital leases, net of current portion	$ -	$ 258

(dollars in thousands)

On January 20, 2016, PHCSH refinanced all its debt, except for the $5,162 still outstanding on the Park Assessment Bond, by issuing the Series 2016 A Revenue Bonds($190,065 plus $28,720 Original Issue Premium) and direct Bank Placement Bonds (Series 2016 B and 2016 C Bonds totaling $85,000). The proceeds were used to i) refund and redeem on a current refunding basis all of the Authority's outstanding Revenue Bonds Series 2010 B, 2010 C and 2010 D, ii) refinance a commercial bank loan, iii) finance certain capital expenditures including but not limited to a surface parking lot and iv) pay the costs of issuance of the Series 2016 A bonds. The debt was structured such that PHCSH would pay annual level debt service payments of approximately $15,459 per year through 2039 and $15,098 annually from 2040 to 2045. The Series 2016 A Revenue Bonds were issued at a premium of $28,720 with stated fixed interest rates between 2% to 5% on the Serial and Term Bonds with yields to maturity estimated between 0.5% to 4.075%. The total interest costs for the Series 2016 A Bonds are estimated at 3.66%.

The Bank Placement Bonds are issued at variable rates. The Series 2016 B Bank Placement Bonds ($65,000) are at 70% of the 30-day LIBOR plus 75 basis points which was 1.04% at closing. The Series 2016 C Bank Placement Bonds ($20,000) are at 67% of the 30-day LIBOR plus 95 basis points which was 1.23% at closing.

The Obligated Group is in compliance with all covenants required by the Authority and the Banks in the Loan Agreements.

The terms of the Series 2016 A, B, and C bonds Park Assessment Bond include scheduled principal payments through 2045. The following five years' scheduled principal payments on all debt are as follows:

2017	$ 5,418
2018	5,606
2019	5,855
2020	5,961
2021	6,015
	$ 28,855

The System has non-cancelable capital leases for medical equipment which have gross carrying values of $8,700 at December 31, 2016 and 2015. Accumulated depreciation related to these capital leases totaled $7,800 and $7,300 at December 31, 2016 and 2015, respectively.

11. Pension Plans

The System previously offered a defined benefit pension plan which was "frozen" as of December 31, 2011 and replaced by a self-directed 401(a) defined contribution plan effective January 1, 2012. Defined contribution plan funding for services earned in 2015 was funded in July of 2016, likewise, services earned in 2016 will be funded in 2017. Both plans cover substantially all of PHCSH's employees.

As of December 31, 2016 and 2015, the frozen defined benefit pension plan's assets were comprised of primarily equity, fixed income securities, and alternative investments.

(dollars in thousands)

The following table sets forth the funded status of the defined benefit plan at December 31:

	2016	2015
Change in projected benefit obligation		
Benefit obligation at beginning of year	$ 157,386	$ 166,117
Interest cost	6,296	6,100
Actuarial (gain) loss	3,706	(7,782)
Benefits paid	(7,108)	(7,049)
Projected benefit obligation at end of year	160,280	157,386
Change in plan assets		
Fair value of plan assets at beginning of year	115,704	119,824
Actual return on plan assets	8,885	(192)
Employer contribution	8,200	3,966
Expenses	(1,060)	(845)
Benefits paid	(7,108)	(7,049)
Fair value of plan assets at end of year	124,621	115,704
Amounts included in the balance sheets	$ 35,659	$ 41,682

The total amount recognized in net periodic benefit cost and change in unrestricted net assets includes the following components at December 31:

	2016	2015
Service cost	$ -	$ -
Interest cost on projected benefit obligation	6,296	6,100
Expected return on plan assets	(6,839)	(7,311)
Amortization of transition (asset)		
Amortization of prior service cost	-	(1,274)
Amortization of net loss	6,093	6,420
Net periodic pension cost	5,550	3,935
Net loss	2,720	565
Amortization of net (loss)	(6,092)	(6,420)
Amortization of prior service cost	-	1,274
Total recognized in change in unrestricted net assets	(3,372)	(4,581)
Total recognized in net periodic benefit cost and change in unrestricted net assets	$ 2,178	$ (646)

(dollars in thousands)

Assumptions used in determining net benefit pension cost and the periodic obligation at December 31 are as follows:

	2016	2015
Benefit obligations		
Discount rates	4.00 %	4.17 %
Net periodic benefit cost		
Discount rates	4.17 %	3.78 %
Expected return on assets	7.00 %	7.00 %

The following benefit payments, which reflect expected future service, as appropriate are expected to be paid as follows:

Estimated future benefit payments at December 31 (unaudited):	
2017	$ 10,618
2018	10,485
2019	10,288
2020	9,834
2021	9,086
2022 through 2026	43,860

Plan assets consisted of the following at December 31:

	2016	2015
Plan assets		
Equity securities	48 %	48 %
Debt securities	38	38
Hedge fund of funds	10	10
Private equity funds	4	4
	100 %	100 %

All pension assets are managed by SEI with the exception of $12,188 of hedge fund of funds managed by Grosvenor. The fair values of pension plan investments included in pension plan assets as of December 31, 2016, utilizing the fair value hierarchy discussed in Note 3, *Fair Value Measurements*, are:

	Level 1	Level 2	Level 3	Total
Money market fund	$ 543	$ -	$ -	$ 543
Equity and fixed income mutual funds	107,632	-		107,632
Investments subject to fair value leveling	$ 108,175	$ -	$ -	108,175
Investments measured using the practical expedient				16,446
				$ 124,621

(dollars in thousands)

The information below shows the redemption frequency of the investments measured using the practical expedient.

	Fair Market Value December 31, 2016	Fair Market Value December 31, 2015	Redemption Frequency (if currently available)	Redemption Notice Period
Private equity	$ 4,258	$ 4,430	Quarterly	30-60 days
Hedge Fund of Funds	$ 12,188	$ 11,924	Quarterly	30-60 days

Unfunded commitments during the years ended December 31, 2016 and 2015 were $3,385 and $3,325, respectively.

All pension assets are managed by SEI with the exception of $11,924 of hedge fund of funds managed by Grosvenor. The fair values of pension plan investments included in pension plan assets as of December 31, 2015, utilizing the fair value hierarchy discussed in Note 3, *Fair Value Measurements*, are:

	Level 1	Level 2	Level 3	Total
Money market fund	$ 395	$ -	$ -	$ 395
Equity and fixed income mutual funds	98,955	-	-	98,955
Investments subject to fair value leveling	$ 99,350	$ -	$ -	99,350
Investments measured using the practical expedient				16,354
				$ 115,704

Investment Policy and Strategy
The System's Investment Committee is responsible for establishing the investment policy for the Plan assets. A long-term actuarial return on plan assets of 7.0% was adopted by the Investment Committee in 2015 given a more conservative asset allocation. The Investment Committee reviews the investment policy guidelines annually in consultation with its investment managers. The current strategic asset allocation guidelines for Plan assets is 30% to 60% equities, 30% to 60% fixed income, and 0% to 20% alternative investments. The allocation between equities and fixed income may be adjusted from time to time based on market conditions and risk/return considerations.

The expected long-term rate of return for the Plan's total assets is based on the current and expected future asset allocations and long-term historic and expected future investment returns and is consistent with assumptions used by plans of similar size.

12. Concentration of Credit Risk

The System grants credit without collateral to its patients, most of who are local residents and are insured under third-party payer agreements. Net accounts receivable from patients and third-party payers were as follows at December 31:

(dollars in thousands)

	2016	2015
Medicare and Medicaid	33 %	34 %
Managed care	15	16
Blue Cross	19	16
Aetna	13	11
Commercial and other	11	12
Self-pay patients (including balances after insurance)	9	11
	100 %	100 %

13. Operating Leases

PHCSH utilizes various types of equipment, office space and vehicles under separate operating leases. The related expenses for those leases for the years ended December 31, 2016 and 2015 were $16,786 and $16,742, respectively. Facility leases, including common area maintenance (CAM) charges, comprised 92% of the 2016 lease expenses, which included $8,809 related to the Power Plant and Medical Arts Pavilion ("MAP") leases.

The following is a projection of the future minimum payments for the next five years required under operating leases currently in effect:

Years ending December 31,	
2017	$ 12,904
2018	11,893
2019	11,680
2020	10,867
2021	9,730
	$ 57,074

14. Commitments and Contingencies

(dollars in thousands)

Various investigations, suits and claims arising in the normal course of operations are pending or are on appeal against PHCSH. Such suits and claims are either specifically covered by insurance or are not material. While the outcome of such actions cannot be determined at this time, legal counsel and management believe that any loss which may arise from these actions will not have a material effect on the financial position or results of operations of PHCSH.

In order to meet patient care needs within the community served by the System, it has provided assistance to third party organizations that provide certain medical related services. The System has guaranteed these organizations an annual income guaranty for the provision of services to patients. These revenue payments are to be refunded back to the System if the organization is unable to meet certain commitments. The System made payments of $487 in 2016 and $427 in 2015. In 2016 and 2015, the System recorded a 50% reserve against the guaranty balance. The net receivable balance is $942 and $948, at December 31, 2016 and December 31, 2015, respectively.

15. Pledges

A summary of pledges receivable is as follows at December 31, 2016 and 2015:

	2016	2015
Unconditional promises expected to be collected in		
Less than one year	$ 2,037	$ 2,839
One year to five years	2,096	2,697
Over five years	550	850
Pledges receivable, gross	4,683	6,386
Less: NPV discount	(198)	(257)
Less: Bad debt reserve	(244)	(128)
Pledges receivable, net	4,241	6,001
Less: Current portion	(1,846)	(2,782)
Long term pledges receivable	$ 2,395	$ 3,219

Outstanding pledge balances are discounted to their net present value, using discount rates between 1.28% and 3.84%.