

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS**

FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2016 AND 2015

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
TABLE OF CONTENTS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

INDEPENDENT AUDITORS' REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	3
FINANCIAL STATEMENTS	
STATEMENTS OF NET POSITION	9
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION	11
STATEMENTS OF CASH FLOWS	12
NOTES TO FINANCIAL STATEMENTS	14
REQUIRED SUPPLEMENTARY INFORMATION	
SCHEDULE OF THE HOSPITAL'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY (UNAUDITED)	37
SCHEDULE OF THE HOSPITAL'S CONTRIBUTIONS (UNAUDITED)	38
COMPLIANCE LETTER	
INDEPENDENT AUDITORS' REPORT ON MINNESOTA LEGAL COMPLIANCE	39

INDEPENDENT AUDITORS' REPORT

Board of Directors
Northfield Hospital
dba: Northfield Hospital & Clinics
Northfield, Minnesota

Report on the Financial Statements

We have audited the accompanying financial statements of Northfield Hospital dba: Northfield Hospital & Clinics (the Hospital), a component unit of the City of Northfield, Minnesota, which comprise the statements of net position as of December 31, 2016 and 2015, and the related statements of revenues, expenses, and changes in net positions, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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


Board of Directors
Northfield Hospital
dba: Northfield Hospital & Clinics

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Northfield Hospital as of December 31, 2016 and 2015, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

A handwritten signature in cursive script that reads "CliftonLarsonAllen LLP".

CliftonLarsonAllen LLP

Minneapolis, Minnesota
April 18, 2017

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

This section of the Hospital's annual audited financial report represents management's discussion and analysis of the Hospital's financial performance during the fiscal year ended December 31, 2016. The analysis will focus on the Hospital's financial performance as a whole. Please read it in conjunction with the audited financial report.

Using This Annual Report

The December 31, 2016 and 2015 audited financial statements that include:

- Independent Auditors' Report
- Statements of Net Position
- Statements of Revenues, Expenses, and Changes in Net Position
- Statements of Cash Flows
- Notes to Financial Statements

Financial Highlights

The Hospital's total assets and deferred outflows of resources increased by \$22,287,667 or 18.5% in 2016 and increased by \$10,702,708 or 9.7% in 2015.

The Hospital's net position increased by \$1,073,724 or 2.7% in 2016 and increased by \$3,515,961 or 9.7% in 2015.

The Hospital reported positive operating income of \$432,806 in 2016 and positive operating income \$2,723,828 in 2015. This represents an operating income decrease in 2016 of \$2,291,022 and a decrease in 2015 of \$1,407,676. These decreases in operating income were impacted by additional pension expense of \$4,463,231 in 2016 and \$504,348 in 2015 in accordance with Governmental Accounting Standards Board Statement No. 68, *Accounting and Financial Reporting for Pensions* (see Note 9).

The Statements of Net Position and Revenues, Expenses, and Changes in Net Position

These financial statements report information about the Hospital using standards issued by the Governmental Accounting Standards Board (GASB). The statement of net position provides information about the amounts of investments in resources (assets) and the obligations to Hospital creditors (liabilities). Revenues and expenses are reflected for the current and previous year on the Statements of Revenues, Expenses, and Changes in Net Position. This statement shows the results of the hospital's operations. The last financial statement is the statements of cash flows. Cash flow reflects the movement of money in and out of the hospital that determines the hospital's solvency. It is divided into cash flows from operating, noncapital financing, capital and related financing, and investing activities.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

Financial Analysis of the Hospital

The information from the statements of net position, statements of revenues, expenses, and changes in net position, and the statements of cash flows are summarized in the following tables. Table 1 reports on the net assets of the Hospital and the changes in them. Increases or decreases in net position are one indicator of whether or not the Hospital's financial health is improving. Table 2 summarizes information from the statements of revenues, expenses, and changes in net position. Other nonfinancial factors can also have an effect on the Hospital's financial position. These can include such things as changes in Medicare and Medicaid regulations and reimbursement, changes with other third party payers, as well as changes in the economic environment of Northfield and the surrounding areas.

Table 1: Assets, Liabilities, and Net Position

	2016	2015	2014
Assets:			
Current Assets	\$ 22,598,516	\$ 19,195,040	\$ 15,246,450
Noncurrent Cash and Investments	54,225,347	50,410,315	47,768,399
Capital Assets, Net	44,385,238	46,433,457	41,557,707
Total Assets	<u>121,209,101</u>	<u>116,038,812</u>	<u>104,572,556</u>
Deferred Outflows of Resources	<u>21,786,445</u>	<u>4,669,067</u>	<u>5,432,615</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 142,995,546</u>	<u>\$ 120,707,879</u>	<u>\$ 110,005,171</u>
Liabilities:			
Total Current Liabilities	\$ 14,700,734	\$ 13,400,492	\$ 12,913,333
Long-Term Debt (Less: Current Maturities)	30,633,748	32,428,168	25,527,526
Total Noncurrent Liabilities	<u>52,533,192</u>	<u>30,825,624</u>	<u>27,785,707</u>
Total Liabilities	<u>97,867,674</u>	<u>76,654,284</u>	<u>66,226,566</u>
Pension Related Deferred Inflows	4,267,255	4,266,702	7,507,673
Net Position:			
Net Investment in Capital Investments	11,884,963	12,540,289	15,065,181
Restricted by Bond Agreement	1,127,275	3,752,211	2,923,788
Unrestricted	<u>27,848,379</u>	<u>23,494,393</u>	<u>18,281,963</u>
Total Net Position	<u>40,860,617</u>	<u>39,786,893</u>	<u>36,270,932</u>
Total Liabilities and Net Position	<u>\$ 142,995,546</u>	<u>\$ 120,707,879</u>	<u>\$ 110,005,171</u>

The asset category changing significantly during 2016 was Deferred Outflows of Resources and Total Noncurrent Liabilities. Deferred Outflows of Resources increased by \$17,117,378 and Noncurrent Liabilities increased by \$21,707,568. Both 2016 increases were due to changes in the PERA net pension liability.

The current ratio (current assets divided by current liabilities) increased in 2016 to 1.54 from 1.43 in 2015. It is a measure of liquidity, providing an indication of the Hospital's ability to pay current liabilities.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

Financial Analysis of the Hospital (Continued)

Table 2 summarizes information from the statements of revenues, expenses, and changes in net position.

Table 2: Statement of Revenues, Expenses, and Changes in Net Position

	2016	2015	2014
Operating Revenue:			
Net Patient and Resident Service Revenue	\$ 101,103,618	\$ 89,985,659	\$ 85,689,216
EHR/Meaningful Use Incentive Payment	144,422	209,185	728,763
Other Revenues	1,249,614	938,744	801,893
Total Operating Revenue	<u>102,497,654</u>	<u>91,133,588</u>	<u>87,219,872</u>
Operating Expenses:			
Salaries and Wages	44,316,610	40,117,088	33,751,616
Employee Benefits	14,691,311	10,387,741	8,697,519
Supplies and Drugs	15,728,203	13,114,235	12,518,681
Purchased Services	12,863,673	11,091,551	15,180,120
Utilities	1,172,435	1,116,379	1,176,698
Other	4,031,070	3,968,214	3,564,600
Depreciation and Amortization	5,330,632	4,791,361	4,437,661
Interest	1,327,414	1,400,204	1,446,010
Taxes and Surcharges	2,603,500	2,422,987	2,315,463
Total Operating Expenses	<u>102,064,848</u>	<u>88,409,760</u>	<u>83,088,368</u>
Operating Income	432,806	2,723,828	4,131,504
Non-Operating Revenues (Loss), Net	<u>531,591</u>	<u>762,133</u>	<u>1,844,640</u>
Excess of Revenues over Expenses	964,397	3,485,961	5,976,144
Capital Grants	109,327	30,000	30,000
Net Position - Beginning of Year	<u>39,786,893</u>	<u>36,270,932</u>	<u>30,264,788</u>
Net Position - End of Year	<u>\$ 40,860,617</u>	<u>\$ 39,786,893</u>	<u>\$ 36,270,932</u>

Net patient service revenue made up 98.6% of the Hospital's total operating revenue in 2016 and 98.7% in 2015 of the Hospital's total operating revenue. To arrive at net patient service revenue, contractual adjustments have been made to gross patient service revenue due to agreements with third-party payors. The growth of patient volumes in the Cancer Care and Infusion Center, Surgery, and Emergency Department had the major impact on the net patient service revenue increase during 2016.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

Financial Analysis of the Hospital (Continued)

Table 3 below shows the contractual adjustments that were recognized:

Table 3: Net Patient Service Revenue and Contractual Adjustments

	2016	2015	2014
Total Patient Service Revenues	\$ 221,771,655	\$ 197,986,591	\$ 184,457,730
Contractual Adjustments and Provisions for Bad Debt	(120,668,037)	(108,000,932)	(98,768,514)
Net Patient Service Revenue	<u>\$ 101,103,618</u>	<u>\$ 89,985,659</u>	<u>\$ 85,689,216</u>
Contractual Adjustments and Bad Debts as a Percent of Revenues	<u>54.41%</u>	<u>54.55%</u>	<u>53.55%</u>

Total operating expenses increased \$13,655,088 or 15.4% in 2016 and increased \$5,321,392 or 6.4% in 2015. With the additional pension expense of \$4,463,231 in accordance with Governmental Accounting Standards Board Statement No. 68, *Accounting and Financial Reporting for Pensions* (see Note 9) and the increase of hospital and clinic volumes, the expenses for 2016 were well within the inflationary expectations.

The Operating Margin (total operating revenue less total operating expenses divided by total operating revenue) was .42% in 2016 down from 2.99% in 2015. Operating income in 2016 was \$432,806 and the operating income in 2015 was \$2,723,828.

EHR/Meaningful Use Incentive Payment decreased by \$64,763 in 2016 and had decreased in 2015 by \$519,578. The hospital had received all three years of Medicare and Medicaid hospital-based incentives prior to 2016. In 2016 the hospital received settlements of Medicare hospital-based incentives based on final settlement of cost reports as well as the physician incentives from Medicare and Medicaid.

Other Operating Revenue increased by \$310,870 or 33% in 2016 after a \$136,851 increase in 2015. The State Grant related to PERA was \$204,531 of the 2016 increase. The College Health Program revenue increased \$127,139 in 2016 and \$53,624 in 2015 due to a change in the relationship with St. Olaf. Previously the Hospital provided medical direction for the St. Olaf College Health program and for the 2015-16 collegiate year the Hospital provided the services. Table 4 shows the detail for this line item.

Table 4: Other Revenues

	2016	2015	2014
Outside Patient Services	\$ 271,427	\$ 260,265	\$ 270,925
College Health Program	194,763	67,624	14,000
Cafeteria and Coffee Shop	185,762	157,321	134,789
Support Services to Mayo Radiation Clinic	83,533	75,296	82,192
Meals on Wheels	64,546	61,936	41,978
Rent Received	34,840	89,716	89,353
State Grant PERA	204,531	-	-
Other	210,212	226,586	168,656
Total Other Revenues	<u>\$ 1,249,614</u>	<u>\$ 938,744</u>	<u>\$ 801,893</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

Hospital Statistical Data

Table 5 shows the Hospital's statistical data. This data demonstrates the direct correlation between utilization changes and revenue changes.

Table 5: Statistical Data

	2016	2015	2014
Patient Days			
Acute	4,367	4,213	4,220
Swing Bed	10	21	42
Newborn	1,062	977	1,035
Long-Term Care	14,171	14,265	14,321
Total	19,610	19,476	19,618
Admissions			
Acute	1,887	1,724	1,651
Swing Bed	7	13	13
Newborn	573	513	515
Long-Term Care	115	103	89
Total	2,582	2,353	2,268
Discharges			
Acute	1,884	1,721	1,652
Swing Bed	7	15	13
Newborn	572	514	517
Long-Term Care	115	103	89
Total	2,578	2,353	2,271
Average Length of Stay, Acute	2.31	2.44	2.56
Beds			
Acute and Swing	37	37	37
Long-Term Care	40	40	40
Occupancy Percentage			
Acute and Swing, Based on 37 Beds	32.3%	31.4%	31.6%
Long-Term Care, Based on 40 Beds	96.8%	97.7%	98.1%

The Hospital's Cash Flows

The Hospital's cash flows are consistent with the changes in operating income and financial performance, as discussed earlier.

Capital Assets

At December 31, 2016, the Hospital had \$44,385,238 invested in capital assets net of accumulated depreciation. The Hospital spent approximately \$3,305,000 on building renovations and equipment purchases in 2016.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

Long-Term Debt

Table 6 shows a summary of the Hospital's long-term debt outstanding.

Table 6: Long-Term Debt

	2016	2015	2014
2006 Revenue Bonds	\$ -	\$ 24,865,000	\$ 25,830,000
2015B Revenue Bonds	7,965,000	8,405,000	-
2016A Revenue Bonds	21,959,080	-	-
2016B Revenue Bonds	2,576,195	-	-
Total Long-Term Debt	<u>\$ 32,500,275</u>	<u>\$ 33,270,000</u>	<u>\$ 25,830,000</u>

The City of Northfield adopted a resolution authorizing the issuance of \$25,000,000 of Hospital Revenue Bonds in August 2016 to refund the 2006 revenue bonds to decrease the interest rate. The bonds are payable through August 1, 2031, with interest coupons payable monthly at an annual rate of 2.56%.

The City of Northfield adopted a resolution authorizing the issuance of \$8,405,000 of Hospital Revenue Bonds in December 2015 to fund the hospital surgery center expansion and the purchase of capital equipment. The bonds are payable through November 1, 2025, with interest coupons payable at May 1 and November 1 at an annual rate of 2.98%.

Economic Factors

The population of Northfield continues to grow at a reasonably healthy annual rate, and the populations of many surrounding communities that the Hospital serves are growing at rates higher than the state averages – especially to the north. The two private colleges, St. Olaf and Carleton College, remain very stable in both of their enrollments, financial strength and their economic support to the local community businesses.

At this time there are no signs of any new industries making a move to the community. The larger industrial employers remain stable in their employment and business production.

The economic outlook for the community remains steady to positive.

Contacting the Hospital

The financial report is designed to provide our citizens, customers, and creditors with a general overview of the Hospital's finances and to demonstrate the Hospital's accountability for the money it receives. If you have any questions about this report or need additional information, please contact Hospital Administration at Northfield Hospital & Clinics, 2000 North Avenue, Northfield, Minnesota 55057.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
STATEMENTS OF NET POSITION
DECEMBER 31, 2016 AND 2015**

	2016	2015
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 5,244,466	\$ 2,479,334
Current Portion of Noncurrent Cash and Investments	1,366,185	1,932,141
Patient Receivables, Less Allowance for Uncollectible Accounts (2016, \$4,375,000; 2015, \$3,655,000)	12,885,459	11,941,274
Accounts Receivable - Other	131,548	96,575
Inventories	2,004,920	1,855,737
Prepaid Expenses	965,938	889,979
Total Current Assets	<u>22,598,516</u>	<u>19,195,040</u>
NONCURRENT CASH AND INVESTMENTS		
Internally Designated for Health Benefits	1,366,185	1,932,141
Internally Designated for Capital Improvements	53,098,072	46,658,104
Restricted by Bond Agreement	1,127,275	3,752,211
Less: Current Portion of Noncurrent Cash and Investments	<u>(1,366,185)</u>	<u>(1,932,141)</u>
Noncurrent Cash and Investments	<u>54,225,347</u>	<u>50,410,315</u>
CAPITAL ASSETS, NET	<u>44,385,238</u>	<u>46,433,457</u>
Total Assets	121,209,101	116,038,812
DEFERRED OUTFLOWS OF RESOURCES		
Pension Related Deferred Outflows	21,197,841	3,748,420
Loss on Refunding	588,604	920,647
Total Deferred Outflows of Resources	<u>21,786,445</u>	<u>4,669,067</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 142,995,546</u>	<u>\$ 120,707,879</u>

See accompanying Notes to Financial Statements.

	2016	2015
LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION		
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 1,866,527	\$ 1,465,000
Accounts Payable, Trade	2,961,649	2,911,840
Construction Payable	613,197	268,503
Accrued Payroll and Benefits	8,848,162	7,827,223
Accrued Interest Payable	91,902	224,007
Third-Party Payor Settlements Payable	319,297	703,919
Total Current Liabilities	<u>14,700,734</u>	<u>13,400,492</u>
LONG-TERM DEBT, Less Current Maturities	30,633,748	32,428,168
NONCURRENT LIABILITIES		
Net Pension Liability	<u>52,533,192</u>	<u>30,825,624</u>
Total Liabilities	97,867,674	76,654,284
DEFERRED INFLOWS OF RESOURCES		
Pension Related Deferred Inflows	<u>4,267,255</u>	<u>4,266,702</u>
NET POSITION		
Net Investment in Capital Assets	11,884,963	12,540,289
Restricted:		
Expendable Under Bond Agreement	1,127,275	3,752,211
Unrestricted	<u>27,848,379</u>	<u>23,494,393</u>
Total Net Position	<u>40,860,617</u>	<u>39,786,893</u>
Total Liabilities, Deferred Inflows of Resources and Net Position	<u>\$ 142,995,546</u>	<u>\$ 120,707,879</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
YEARS ENDED DECEMBER 31, 2016 AND 2015**

	2016	2015
OPERATING REVENUES		
Net Patient and Resident Service Revenue, Net of Provision for Bad Debts of \$2,253,836 in 2016 and \$1,594,122 in 2015	\$ 101,103,618	\$ 89,985,659
EHR/Meaningful Use Incentive Payment	144,422	209,185
Other Revenues	1,249,614	938,744
Total Operating Revenues	<u>102,497,654</u>	<u>91,133,588</u>
OPERATING EXPENSES		
Salaries and Wages	44,316,610	40,117,088
Employee Benefits	14,691,311	10,387,741
Supplies and Drugs	15,728,203	13,114,235
Purchased Services	12,863,673	11,091,551
Utilities	1,172,435	1,116,379
Other	4,031,070	3,968,214
Depreciation and Amortization	5,330,632	4,791,361
Interest	1,327,414	1,400,204
Taxes and Surcharges	2,603,500	2,422,987
Total Operating Expenses	<u>102,064,848</u>	<u>88,409,760</u>
OPERATING INCOME	432,806	2,723,828
NON-OPERATING REVENUES AND EXPENSES		
Investment Income	761,580	868,338
Gifts and Grants	115,636	109,492
Gain (Loss) on the Sale/Disposal of Assets	(1,603)	2,618
Miscellaneous Expenses	(344,022)	(218,315)
Total Non-Operating Revenues and Expenses, Net	<u>531,591</u>	<u>762,133</u>
EXCESS OF REVENUES OVER EXPENSES	964,397	3,485,961
Capital Grants	<u>109,327</u>	<u>30,000</u>
INCREASE IN NET POSITION	1,073,724	3,515,961
Net Position - Beginning of Year	<u>39,786,893</u>	<u>36,270,932</u>
NET POSITION - END OF YEAR	<u><u>\$ 40,860,617</u></u>	<u><u>\$ 39,786,893</u></u>

See accompanying Notes to Financial Statements.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2016 AND 2015**

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash Received from Patients and Third-Party Payors	\$ 99,919,233	\$ 86,656,292
Cash Paid to Employees	(57,986,982)	(49,617,785)
Cash Paid to Suppliers and Contractors	(31,983,471)	(31,382,238)
Other Receipts and Payments, Net	1,214,641	1,101,447
Net Cash Provided by Operating Activities	<u>11,163,421</u>	<u>6,757,716</u>
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Unrestricted Gifts and Grants	115,636	109,492
Miscellaneous Expenses	(344,022)	(218,315)
Net Cash Used by Non-Capital Financing Activities	<u>(228,386)</u>	<u>(108,823)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of Capital Assets	(2,953,469)	(9,814,459)
Proceeds (Loss) from Sale of Capital Assets	14,147	2,987
Proceeds from Issuance of Long-Term Debt	-	8,405,000
Principal Payments on Long-Term Debt	(1,369,497)	(965,000)
Interest Payments on Long-Term Debt	(1,482,915)	(1,447,036)
Capital Contributions	109,327	30,000
Net Cash Used by Capital and Related Financing Activities	<u>(5,682,407)</u>	<u>(3,788,508)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Increase in Noncurrent Cash and Investments	(3,213,882)	(2,934,762)
Investment Income	726,386	870,070
Net Cash Used by Investing Activities	<u>(2,487,496)</u>	<u>(2,064,692)</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	2,765,132	795,693
Cash and Cash Equivalents - Beginning of Year	<u>2,479,334</u>	<u>1,683,641</u>
CASH AND CASH EQUIVALENTS - END OF YEAR	<u><u>\$ 5,244,466</u></u>	<u><u>\$ 2,479,334</u></u>

See accompanying Notes to Financial Statements.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
STATEMENTS OF CASH FLOWS (CONTINUED)
YEARS ENDED DECEMBER 31, 2016 AND 2015**

	2016	2015
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating Income	\$ 432,806	\$ 2,723,828
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:		
Depreciation	5,330,632	4,791,361
Interest	1,327,414	1,400,204
Provision for Bad Debt Expense	2,253,836	1,594,122
Amortization of Deferred Loss on Refinancing	332,043	58,146
(Increase) Decrease in:		
Patient Receivables	(3,198,021)	(4,111,886)
Inventories, Prepaids, and Other Receivables	(260,115)	(344,019)
Pension Related Deferred Outflow	(17,449,421)	705,402
Increase (Decrease) in:		
Accounts Payable	49,809	275,356
Third-Party Payor Settlements Payable	(384,622)	(1,020,788)
Accrued Expenses	1,020,939	887,044
Net Pension Liability	21,707,568	3,039,917
Pension Related Deferred Inflow	553	(3,240,971)
Net Cash Provided by Operating Activities	<u>\$ 11,163,421</u>	<u>\$ 6,757,716</u>
NONCASH FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Amortization of Net Premium as a Component of Interest Expense	<u>\$ (23,396)</u>	<u>\$ 39,358</u>
Construction Payable	<u>\$ 613,197</u>	<u>\$ 268,503</u>
Long-Term Debt issued to Refund Bonds	<u>\$ 25,000,000</u>	<u>\$ -</u>

See accompanying Notes to Financial Statements.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Northfield Hospital dba: Northfield Hospital & Clinics (the Hospital), including the Northfield Hospital Long Term Care Center, onsite Women's Health and Medical Clinics, and offsite Orthopedic, Ophthalmology, and Medical Clinics at Lonsdale, Farmington, Elko New Market and Lakeville, is operated by and is a component unit of the City of Northfield, Minnesota (the City) and is governed by the Board of Directors of Northfield Hospital. The Hospital is exempt from federal and state income taxes and property taxes. The Physician-Based clinics are subject to property tax.

Reporting Entity

For financial reporting purposes, the Hospital has included all funds, organizations, account groups, agencies, boards, commissions, and authorities. The Hospital has also considered all potential units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Hospital are such that exclusion would cause the Hospital's financial statements to be misleading or incomplete. The Government Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the organization to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Hospital. The Hospital has no funds which meet the Governmental Accounting Standards Board criteria. The Hospital is considered a part of the reporting entity of the City of Northfield, Minnesota and is included in the City's financial statements as a component unit.

Use of Estimates

The preparation of 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 disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

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

Investments in Debt and Equity Securities

Investments in debt and equity securities are reported at fair value except for short-term highly liquid investments that have a remaining maturity at the time they are purchased of one year or less. These investments are carried at amortized cost. Interest, dividends and gains and losses, both realized and unrealized, on investments in debt and equity securities are included in nonoperating revenue when earned.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Patient Receivables

The Hospital provides an allowance for uncollectible accounts using management's judgment. Acute-care patients are not required to provide collateral for services rendered. Nursing home residents are required to make a prepayment for the estimated monthly amount when Medicaid, Medicare or private insurance is not paying for room and board. Payment for services is required within 30 days of receipt of invoice. Past due accounts are individually analyzed for collectability, and then turned over to collection agents. Accounts for which no payments have been received are analyzed and after approval are written off. In addition, an allowance is estimated for other accounts based on historical experience of the Hospital. At December 31, 2016 and 2015, the allowance for uncollectible accounts was \$4,375,000 and \$3,655,000, respectively.

Inventories

The inventories are recorded at the lower of cost or market using the latest invoice cost, which approximates the first-in, first-out method.

Noncurrent Cash and Investments

Noncurrent cash and investments include assets set aside by the board of directors for future capital improvements, assets set aside under bond indenture agreements and assets set aside under employee health insurance arrangements.

Deferred Outflows of Resources

Deferred outflows of resources represent a consumption of net position that applies to a future period(s) and will not be recognized as an outflow of resources (expense) until then. Deferred outflows of resources consist of unrecognized items not yet charged to pension expense and contributions from the employer after the measurement date but before the end of the employer's reporting period. Deferred outflows also include the unamortized loss on refinancing that is being amortized over the period the obligation is outstanding, using the straight line method.

Capital Assets

Capital assets are reported at cost, if purchased or at fair market value on the date received, if donated. Depreciation is provided on a straight-line basis over the estimated useful lives of the property. Useful lives are assigned based on estimated useful lives of depreciable assets recommended by the American Hospital Association. It is the Hospital's policy to include amortization expense on assets acquired under capital leases with depreciation on owned assets.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Net Patient and Resident Service Revenue

Net patient/resident service revenue is reported at the estimated net realizable amounts from patients, residents, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with 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.

Electronic Health Record Incentive Payments

As discussed in Note 11, the Hospital received funds under the Electronic Health Records (EHR) Incentive Program during 2016 and 2015. The Hospital recognizes revenue at the completion of the EHR reporting period and after all meaningful use objectives and any other specific grant requirements that are applicable are met.

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources, and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Public Employees' Retirement System (PERA) and additions to/deductions from PERA'S fiduciary net position have been determined on the same basis as they are reported by PERA. For this purpose, benefit payments (including refunds or employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Deferred Inflows of Resources

Although certain revenues are measurable, they are not available. Available means collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Deferred inflows of resources represents the amount of assets that have been recognized, but the related revenue has not been recognized since the assets are not collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Deferred inflows of resources consist of pension related deferred inflows.

Net Position

Net position of the Hospital is classified in three components. *Net position invested in capital assets net of related debt* consist of capital assets net of accumulated depreciation and reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted net position* is noncapital net assets that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Hospital, including amounts deposited with trustees as required by revenue bond indentures. *Unrestricted net position* is the remaining net assets that do not meet the definition of *net position invested in capital assets net of related debt or restricted*.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Contributions

From time to time, the Hospital receives contributions from individuals and private organizations. Revenue contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues. Amounts restricted to capital acquisitions are reported after nonoperating revenues and expenses.

Restricted Resources

When the Hospital has both restricted and unrestricted resources available to finance a particular program, it is the Hospital's policy to use restricted resources before unrestricted resources.

Operating Revenues and Expenses

The Hospital's statement of revenues, expenses and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues result from transactions associated with providing health care services – the Hospital's principal activity. Other revenues, including interest income, grants, and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, including interest expense.

Concentrations of Credit Risk

The Hospital grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements.

Charity Care

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

Recent Accounting Pronouncements

For the year ended December 31, 2016, the Hospital adopted the provisions of GASB Statement No. 72, *Fair Value Measurement and Application*, which is effective for financial statement periods beginning after June 15, 2015. GASB Statement No. 72 requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and the valuation techniques. See Note 4 to the financial statements for disclosure of fair value measurements.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair Value Measurements

To the extent available, the Hospital's investments are recorded at fair value. GASB Statement No. 72 – *Fair Value Measurement and Application*, 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. This statement establishes a hierarchy of valuation inputs based on the extent to which inputs are observable in the marketplace. Inputs are used in applying the various valuation techniques and take in to account the assumptions that market participants use to make valuation decisions. Inputs may include price information, credit data, interest and yield curve data, and other factors specific to the financial instrument. Observable inputs reflect market data obtained from independent sources.

In contrast, unobservable inputs reflect an entity's assumptions about how market participants would value the financial instrument. Valuation techniques should maximize the use of observable inputs to the extent available. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used for financial instruments measured at fair value on a recurring basis:

Level 1 – Inputs that utilize quoted prices (unadjusted) in active markets for identical assets or liabilities that the Hospital has the ability to access.

Level 2 – Inputs that include quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Fair values for these instruments are estimated using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows.

Level 3 – Inputs that are unobservable inputs for the asset or liability, which are typically based on an entity's own assumptions, as there is little, if any, related market activity.

NOTE 2 DESIGNATED FUNDS

For the years ended December 31, 2016 and 2015, the board of directors has designated \$53,098,072 and \$46,658,105, respectively, for capital expenditures and \$1,366,185 and \$1,932,141, respectively, for the payment of health benefits. Designated funds remain under the control of the board of directors, which may at its discretion later use the funds for other purposes. Designated funds are reflected in noncurrent cash and investments.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 3 NET PATIENT SERVICE REVENUE

The Hospital and the nursing facility have entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates. The base payment for the nursing facility includes room charges and ancillary services to nursing facility residents. Revenue is recorded at established billing rates, net of contractual adjustments, resulting from agreements with third-party payors.

Medicare

By Minnesota Statute, a nursing facility, which participates in the Medicaid program, must also participate in the Medicare program. This program is administered by United States Centers for Medicare and Medicaid Services (CMS).

The Northfield Hospital Long Term Care Center is paid under the Medicare Prospective Payment System (PPS) for residents who are Medicare Part A eligible and meet the coverage guidelines for skilled nursing facility services (SNFs). The PPS is a per diem price-based system.

Nursing facilities licensed for participation in the Medicare and Medicaid programs are subject to annual surveys. If it is determined that a nursing facility is not in substantial compliance with the requirements of participation, CMS may impose sanctions and penalties during the period of noncompliance, which would have a negative impact on the revenues of the nursing facility.

Inpatient acute care services provided to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors.

Outpatient services provided to Medicare outpatient program beneficiaries are subject to the Ambulatory Payment Classification (APC) method. Medicare reimburses the Hospital a predetermined amount for most outpatient services. The following services are excluded from the APC payment methodology; services already paid on a fee schedule, services to SNF residents which are already included in the SNF's payment, and certain drugs, biologicals and medical devices identified as pass-through items. The APC payments are not based on the provider's annual cost report.

Physician-Based Clinic services are reimbursed using the Medicare Physician Fee Schedule.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 3 NET PATIENT SERVICE REVENUE (CONTINUED)

Medicaid

The Northfield Hospital Long Term Care Center participates in the Medicaid program that is administered by the Minnesota Department of Human Services (DHS). Medicaid and private paying residents are classified into one of 48 Resource Utilization Groups (RUG) for purposes of establishing payment rates.

Effective January 1, 2016, nursing facilities are paid under the Value Based Nursing Facility Reimbursement System (VBR) as approved during the 2015 Minnesota State Legislative Session. Under the VBR system, care related costs are reimbursed at actual cost subject to certain limitations. Other operating costs are reimbursed using a pricing model, which results in the rates of these costs being the same for all nursing facilities in the state. Certain other costs, such as qualifying employer health insurance costs, are reimbursed at an external fixed payment rate and will be cost based with no limitations. Reimbursement for historic property related costs is a separate component of the rate that has been frozen since 2010. Additional reimbursement for new property related costs is possible under certain conditions.

The change to the VBR system includes a hold harmless provision which protects nursing home facilities from being paid at rates lower than those in effect December 31, 2015. Nursing facilities are also protected from significant decreases in rates in a single year due to changes in care related costs.

By Minnesota Statute, a nursing facility may not charge private paying residents in multiple occupancy rooms per diem rates in excess of the approved Medicaid rates for similar services.

Hospital inpatient services rendered to Medicaid program beneficiaries are reimbursed under a reimbursement methodology similar to inpatient Medicare. Hospital outpatient and Physician-Based clinic Medicaid services are reimbursed using the Medicaid fee schedule.

Other

The Hospital has also entered into payment agreements with Blue Cross and other commercial insurance carriers. The basis for reimbursement under these agreements includes discounts from established charges and prospectively determined rates. As of August 1, 2014, the Hospital Blue Cross contract moved to APR-DRG for inpatient acute care services and EAPG for outpatient services.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 3 NET PATIENT SERVICE REVENUE (CONTINUED)

Laws and regulations governing 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 in the near term. Net patient and resident service revenue increased for the year ended December 31, 2016 by approximately \$63,806 and increased by \$57,960 for the year ended December 31, 2015 due to changes in estimated settlement amounts.

A summary of patient and resident revenues and contractual adjustments is as follows:

	2016	2015
Total Patient and Resident Revenues	\$ 221,771,655	\$ 197,986,591
Contractual Adjustments:		
Medicare	(48,221,909)	(40,566,304)
Medicaid	(4,183,924)	(10,171,537)
Commercial/HMOs	(59,638,621)	(50,525,195)
Provision for Bad Debts	(2,253,836)	(1,594,122)
Other	(6,369,747)	(5,143,774)
Total Contractual Adjustments	(120,668,037)	(108,000,932)
Net Patient and Resident Revenues	<u>\$ 101,103,618</u>	<u>\$ 89,985,659</u>

NOTE 4 DEPOSITS AND INVESTMENTS

Deposits

Custodial Credit Risk – Custodial credit risk is the risk that in the event of a bank failure, the Hospital's deposits may not be returned to it in full. The Hospital follows the Minnesota Statutes for deposits. The Hospital does not have a formal policy regarding the holding of securities by counterparties; however, as of December 31, 2016 or 2015, the Hospital did not have any such arrangements.

In accordance with Minnesota Statutes, the Hospital maintains deposits at financial institutions that are authorized by the Hospital's Board of Directors.

Minnesota Statutes require that all Hospital deposits be protected by insurance, surety bond or collateral. The market value of the collateral pledged must equal 110% of the deposits not covered by insurance or bonds.

Authorized collateral includes certain U.S. government securities, state or local government obligations, and other securities authorized by Minn. Stat. 118.A.03. Minnesota Statutes require that securities pledged as collateral be held in safekeeping by the Treasurer or in a financial institution other than that furnishing collateral.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 4 DEPOSITS AND INVESTMENTS (CONTINUED)

Deposits (Continued)

The Hospital's deposits in banks at December 31, 2016 and 2015 were entirely covered by federal depository insurance or by collateral held by the Hospital's custodial bank in the Hospital's name.

Investments

The Hospital may also invest idle funds as authorized by Minnesota Statutes as follows:

- Direct obligations or obligations guaranteed by the United States or its agencies.
- Shares of investment companies registered under the Federal Investment Company Act of 1940 and receives the highest credit rating, is rated in one of the two highest rating categories by a statistical rating agency and all of the investments have a final maturity of thirteen months or less.
- General obligations rated "A" or better; revenue obligations rated "AA" or better.
- General obligations of the Minnesota Housing Finance Agency rated "A" or better.
- Bankers' acceptances of United States banks eligible for purchase by the Federal Reserve System.
- Commercial paper issued by United States corporations or their Canadian subsidiaries, of the highest quality category by at least two nationally recognized rating agencies, and maturing in 270 days or less.
- Guaranteed Investment Contracts guaranteed by a United States commercial bank, domestic branch of a foreign bank, or a United States insurance company, and with a credit quality in one of the top two highest categories.
- Repurchase or reverse purchase agreements and securities lending agreements financial institutions qualified as a "depository" by the government entity, with banks that are members of the Federal Reserve System with capitalization exceeding \$10,000,000, a primary reporting dealer in U.S. government securities to the Federal Reserve Bank of New York, or certain Minnesota securities broker-dealers.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 4 DEPOSITS AND INVESTMENTS (CONTINUED)

Investments (Continued)

The Hospital had the following investments at December 31, 2016 and 2015:

	2016	2015
Federal Home Loan Bank	\$ 10,485,252	\$ 13,226,273
Federal National Mortgage Association	4,367,055	6,924,355
Federal Home Loan Mortgage Corp	12,145,898	10,691,299
Federal Agricultural Mortgage Corp	1,071,837	1,048,868
Federal Farm Credit Bank	11,325,925	6,925,964
US Treasury Notes	4,033,866	6,178,270
Certificate of Deposit	7,927,342	5,420,483
Total	<u>\$ 51,357,175</u>	<u>\$ 50,415,512</u>

- **Federal Home Loan Bank:** Consists of discount notes and notes with interest rates of 0.75% to 5.375% maturing from 2018 to 2026 and have AA+ to AAA ratings by Standard & Poor's.
- **Federal National Mortgage Association:** Consists of discount notes and notes with interest rates of .875% to 2.0% maturing from 2018 to 2020 and have AA+ ratings by Standard & Poor's.
- **Federal Home Loan Mortgage Corp:** Consists of discount notes with interest rates of .875% to 4.875% maturing from 2018 to 2031 and have AA+ to AAA ratings by Standard & Poor's.
- **Federal Agricultural Mortgage Corp:** Consists of discount notes with interest rates of .93% maturing in 2018 and have AA+ ratings by Standard & Poor's.
- **Federal Farm Credit Bank:** Consists of discount notes with interest rates ranging from 1.36% to 2.61% maturing in 2019 to 2027 and have AA+ ratings by Standard & Poor's.
- **US Treasury Notes:** Consists of discount notes with interest rates ranging from 0.625% to 2.125% maturing in 2017 to 2021 and have AA+ ratings by Standard & Poor's.
- **Certificates of Deposits (CD):** Consists of deposits with interest rates ranging from .95% to 1.95% maturing in 2017 to 2021.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 4 DEPOSITS AND INVESTMENTS (CONTINUED)

Investments (Continued)

Fair Value Measurements

The Hospital uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. For additional information on how the hospital measures fair value refer to Note 1 – Summary of Significant Accounting Policies. The following table presents the fair value hierarchy for the balances of the assets and liabilities of the Hospital measured at fair value on a recurring basis as of December 31, 2016 and 2015:

2016				
Investment Type	Level 1	Level 2	Level 3	Total
Cash and Cash Equivalents	\$ 9,478,823	\$ -	\$ -	\$ 9,478,823
Certificates of Deposit	7,927,342	-	-	7,927,342
U.S. Treasuries	-	4,033,866	-	4,033,866
U.S. Government Agencies	-	39,395,967	-	39,395,967
Totals	<u>17,406,165</u>	<u>43,429,833</u>	<u>-</u>	<u>60,835,998</u>

2015				
Investment Type	Level 1	Level 2	Level 3	Total
Cash and Cash Equivalents	\$ 4,406,278	\$ -	\$ -	\$ 4,406,278
Certificates of Deposit	5,420,483	-	-	5,420,483
U.S. Treasuries	-	6,178,270	-	6,178,270
U.S. Government Agencies	-	38,816,759	-	38,816,759
Totals	<u>9,826,761</u>	<u>44,995,029</u>	<u>-</u>	<u>54,821,790</u>

Interest Rate Risk

The Hospital has a formal investment policy that addresses permissible investments, portfolio diversification and instrument maturities. Within these parameters, the liquidity of the investments are a concern maximizing income and the quality of the investment are paramount.

Credit Risk

State law limits investments in commercial paper and corporate bonds to the top two ratings issued by nationally recognized statistical rating organizations. As of December 31, 2016, the Hospital's investments were rated as shown above.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 4 DEPOSITS AND INVESTMENTS (CONTINUED)

Concentration of Credit Risk

The Hospital does not place a limit on the amount of the total portfolio that may be invested in any one depository or issuer. The Finance Department is responsible for the formulation, documentation and monitoring of investment strategy consistent with the investment policy.

At December 31, 2016 and 2015, deposits and investments are presented in the financial statements as follows:

	2016	2015
Deposits	\$ 9,478,823	\$ 4,406,278
Federal Home Loan Bank	10,485,252	13,226,273
Federal National Mortgage Association	4,367,055	6,924,355
Federal Home Loan Mortgage Corp	12,145,898	10,691,299
Federal Agricultural Mortgage Corp	1,071,837	1,048,868
Federal Farm Credit Bank	11,325,925	6,925,964
Federal Reserve Note	4,033,866	6,178,270
Certificate of Deposit	7,927,342	5,420,483
Total	<u>\$ 60,835,998</u>	<u>\$ 54,821,790</u>

	2016	2015
Included in the Following Balance Sheet Captions:		
Cash and Cash Equivalents	\$ 5,244,466	\$ 2,479,334
Noncurrent Cash and Investments:		
Internally Designated for Health Benefits	1,366,185	1,932,141
Internally Designated for Capital Improvements	53,098,072	46,658,104
Restricted by Bond Agreement	1,127,275	3,752,211
Total	<u>\$ 60,835,998</u>	<u>\$ 54,821,790</u>

As of December 31, 2016 and 2015, accrued interest of \$235,365 and \$200,171, respectively, is included in Internally Designated for Capital Improvements in the above schedules.

For the years ended December 31, 2016 and 2015, investment returns are as follows:

	2016	2015
Interest and Dividend Income	\$ 967,594	\$ 842,259
Realized and Unrealized Loss on Investments	(206,014)	26,079
Total	<u>\$ 761,580</u>	<u>\$ 868,338</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 5 PATIENT RECEIVABLES

Patient receivables reported as current assets by the Hospital at December 31, 2016 and 2015 consist of the following:

	2016	2015
Receivable from Patients and Their Insurance Carriers	\$ 13,926,046	\$ 12,683,456
Receivables from Medicare	2,271,427	1,977,484
Receivables from Medicaid	1,062,986	935,334
Total Patient Receivables	17,260,459	15,596,274
Less: Allowance for Doubtful Accounts	(4,375,000)	(3,655,000)
Patient Receivables, Net	<u>\$ 12,885,459</u>	<u>\$ 11,941,274</u>

NOTE 6 DEFERRED OUTFLOWS OF RESOURCES

The loss of \$605,421 from the refinancing of the 2006 Revenue Bonds is shown net of accumulated amortization. The remaining refunding loss to be amortized is \$588,604 at December 31, 2016. Amortization expense was \$16,817 for the year ended December 31, 2016. The loss is amortized over the life of the bonds.

See details on Pension Related Deferred Outflows in Note 9.

NOTE 7 CAPITAL ASSETS, NET

A summary of capital assets and related accumulated depreciation is as follows:

	January 1, 2016	Additions and Transfers	Retirements	December 31, 2016
Capital Assets				
Land	\$ 3,694,360	\$ -	\$ -	\$ 3,694,360
Land Improvements	742,412	18,596	-	761,008
Buildings	58,978,829	36,867	-	59,015,696
Building Equipment	1,927,406	110,285	(34,448)	2,003,243
Movable Equipment	27,850,429	4,117,538	(2,026,076)	29,941,891
Other Real Estate	105,396	-	-	105,396
Construction in Progress	1,316,873	(978,121)	-	338,752
Totals	94,615,705	3,305,165	(2,060,524)	95,860,346
Accumulated Depreciation				
Land Improvements	297,133	69,451	-	366,584
Buildings	25,034,450	2,751,356	-	27,785,806
Building Equipment	1,105,991	147,255	(34,448)	1,218,798
Movable Equipment	21,639,278	2,362,567	(2,003,321)	21,998,524
Other Real Estate	105,396	-	-	105,396
Totals	48,182,248	\$ 5,330,629	\$ (2,037,769)	51,475,108
	<u>\$46,433,457</u>			<u>\$44,385,238</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 7 CAPITAL ASSETS, NET (CONTINUED)

	January 1, 2015	Additions and Transfers	Retirements	December 31, 2015
Capital Assets				
Land	\$ 3,694,360	\$ -	\$ -	\$ 3,694,360
Land Improvements	386,681	355,731	-	742,412
Buildings	52,965,806	6,013,023	-	58,978,829
Building Equipment	1,474,471	458,367	(5,432)	1,927,406
Movable Equipment	23,775,571	4,401,000	(326,142)	27,850,429
Other Real Estate	105,396	-	-	105,396
Construction in Progress	2,877,235	(1,560,362)	-	1,316,873
Totals	85,279,520	9,667,759	(331,574)	94,615,705
Accumulated Depreciation				
Land Improvements	244,712	52,421	-	297,133
Buildings	22,445,277	2,589,173	-	25,034,450
Building Equipment	991,173	120,206	(5,388)	1,105,991
Movable Equipment	19,935,255	2,029,561	(325,538)	21,639,278
Other Real Estate	105,396	-	-	105,396
Totals	43,721,813	\$ 4,791,361	\$ (330,926)	48,182,248
	<u>\$41,557,707</u>			<u>\$46,433,457</u>

Construction in progress at December 31, 2016 consists of costs related to various capital projects. These projects will be funded using internal funds or construction funds from previous bond proceeds and expect to be completed in 2017/2018.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 8 LONG-TERM DEBT

Long-term debt consists of the following as of December 31, 2016 and 2015:

	Balance January 1, 2016	Additions	Payments/ Amortization	Balance December 31, 2016	Amounts Due Within One Year
Hospital Revenue Bonds, Series 2006	\$ 24,865,000	\$ -	\$(24,865,000)	\$ -	\$ -
Hospital Revenue Bonds, Series 2015B	8,405,000	-	(440,000)	7,965,000	470,000
Hospital Revenue Bonds, Series 2016A	-	22,375,000	(415,920)	21,959,080	1,249,865
Hospital Revenue Bonds, Series 2016B	-	2,625,000	(48,805)	2,576,195	146,662
Bond Premium	623,168	-	(623,168)	-	-
Total Long-Term Debt	<u>\$ 33,893,168</u>	<u>\$ 25,000,000</u>	<u>\$(26,392,893)</u>	<u>\$ 32,500,275</u>	<u>\$ 1,866,527</u>

	Balance January 1, 2015	Additions	Payments/ Amortization	Balance December 31, 2015	Amounts Due Within One Year
Hospital Revenue Bonds, Series 2006	\$ 25,830,000	\$ -	\$ (965,000)	\$ 24,865,000	\$ 1,025,000
Hospital Revenue Bonds, Series 2015B	-	8,405,000	-	8,405,000	440,000
Bond Premium	662,526	-	(39,358)	623,168	-
Total Long-Term Debt	<u>\$ 26,492,526</u>	<u>\$ 8,405,000</u>	<u>\$ (1,004,358)</u>	<u>\$ 33,893,168</u>	<u>\$ 1,465,000</u>

The following is a summary of the provisions of each major component of long-term debt:

Hospital Revenue Bonds, Series 2015B

These bonds were issued December 29, 2015 in the amount of \$8,405,000 to provide funding for construction of the expansion of the surgery center and purchase of the MRI and other diagnostic equipment. The bonds are limited obligations of the City and are payable primarily from the net revenues of the Hospital and are secured by a mortgage and security agreement between the City and Wells Fargo Bank, MN NA as Trustee.

Interest on the bond is 2.98%, and is due each May 1 and November 1, with principal payments due each November 1 through November 1, 2025.

Hospital Revenue Bonds, Series 2016

These bonds were issued August 5, 2016 in the amount of \$25,000,000 to extinguish the Hospital Revenue Bonds Series 2006. The bonds are limited obligations of the City and are payable primarily from the net revenues of the Hospital and are secured by a mortgage and security agreement between the City and Wells Fargo Bank, MN NA as Trustee.

Interest on the bond is 2.56%, and is due monthly from September 2016, through August, 2031.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 8 LONG-TERM DEBT (CONTINUED)

The revenue bonds loan agreement places limits on the incurrence of additional borrowings and requires the Hospital to satisfy certain measures of financial performance.

The following is a summary of debt service requirements for both the Series 2015 and 2016 to maturity:

<u>Year Ending December 31,</u>	<u>Long-Term Debt</u>	
	<u>Principal</u>	<u>Interest</u>
2017	\$ 1,866,527	\$ 849,150
2018	1,917,701	798,970
2019	1,964,811	747,407
2020	2,017,883	694,584
2021	2,071,941	640,328
2022-2026	13,836,916	2,239,113
2027-2031	8,824,496	546,968
Total	<u>\$ 32,500,275</u>	<u>\$ 6,516,520</u>

NOTE 9 RETIREMENT PLANS

Plan Description

The Hospital participates in the following defined benefit pension plans administered by the Public Employees Retirement Association (PERA). PERA's defined benefit pension plans are established and administered in accordance with Minnesota Statutes, Chapters 353 and 356. PERA's defined benefit pension plans are tax qualified plans under Section 401(a) of the Internal Revenue Code.

All full-time and certain part-time employees of the Hospital are covered by the General Employees Retirement Fund (GERF). GERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. The Basic Plan was closed to new members in 1967. All new members must participate in the Coordinated Plan.

Benefits Provided

PERA provides retirement, disability, and death benefits. Benefit provisions are established by state statute and can only be modified by the state legislature.

Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Members in plans that are at least 90% funded for two consecutive years are given 2.5% increases. Members in plans that have not exceeded 90% funded, or have fallen below 80%, are given 1% increases.

The benefit provisions stated in the following paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet are bound by the provisions in effect at the time they last terminated their public service.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 9 RETIREMENT PLANS (CONTINUED)

Benefits Provided (Continued)

Benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service. Two methods are used to compute benefits for PERA's Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2% of average salary for each of the first 10 years of service and 2.7% for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2% of average salary for each of the first 10 years and 1.7% for each remaining year. Under Method 2, the annuity accrual rate is 2.7% of average salary for Basic Plan members and 1.7% for Coordinated Plan members for each year of service. For members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66. Disability benefits are available for vested members, and are based upon years of service and average high-five salary.

Contributions

Minnesota Statutes, Chapter 353, sets the rates for employer and employee contributions. Contribution rates can only be modified by the state legislature.

Basic Plan members were required to contribute 6.5% of their annual covered salary in calendar year 2015 and the Hospital was required to contribute 7.5% of pay for Basic Plan members. The Hospital's contributions to the GERS for the plan's fiscal years ended December 31, 2016 and 2015 were \$3,118,000 and \$2,878,000, respectively. The Hospital's contributions were equal to the required contributions for each year as set by state statute.

Pension Costs

At December 31, 2016 and 2015, the Hospital reported a liability of \$52,533,192 and \$30,825,624, respectively, for its proportionate share of the GERS's net pension liability. The Hospital's net pension liability reflected a reduction due to the State of Minnesota's contribution of \$6 million to the fund in 2016. The State of Minnesota is considered a nonemployer contributing entity and the state's contribution meets the definition of a special funding situation. The State of Minnesota's proportionate share of the net pension liability associated with the Hospital totaled \$204,531. The net pension liability was measured as of June 30, 2016 and 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of those dates. The Hospital's proportion of the net pension liability was based on the Hospital's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2015, through June 30, 2016 and July 1, 2014 through June 30, 2015, relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2016, the Hospital's proportion share was .6470%, which was an increase of .0522% from its proportion measured as of June 30, 2015.

There were no benefit provision changes during the measurement period.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 9 RETIREMENT PLANS (CONTINUED)

Pension Costs (Continued)

For the years ended December 31, 2016 and 2015, the Hospital recognized pension expense of \$7,581,536 and \$3,381,963, respectively. These amounts consisted of the Hospital's proportionate share of the GERS's pension expense, plus additional amortized net expenses associated with differences between estimated and actual experience of various actuarial assumptions associated with the plan.

At December 31, 2016 and 2015, the Hospital reported its proportionate share of the GERS's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

<u>December 31, 2016</u>	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences Between Expected and Actual Experience	\$ 155,479	\$ 4,267,255
Changes of Assumptions	11,330,144	-
Net Difference Between Projected and Actual Earnings on Pension Plan Investments	5,864,967	-
Changes in Proportion and Differences Between Hospital Contributions and Proportionate Share of Contributions of Contributions	2,258,424	-
Hospital Contributions Subsequent to the Measurement Date	1,588,827	-
Total	<u>\$ 21,197,841</u>	<u>\$ 4,267,255</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 9 RETIREMENT PLANS (CONTINUED)

Pension Costs (Continued)

December 31, 2015	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences Between Expected and Actual Experience	\$ 284,284	\$ 1,554,137
Changes of Assumptions	1,909,064	-
Net Difference Between Projected and Actual Earnings on Pension Plan Investments	-	2,712,565
Changes in Proportion and Differences Between Hospital Contributions and Proportionate Share of Contributions of Contributions	116,263	-
Hospital Contributions Subsequent to the Measurement Date	<u>1,438,809</u>	<u>-</u>
Total	<u>\$ 3,748,420</u>	<u>\$ 4,266,702</u>

\$1,588,827 reported as deferred outflows of resources related to pensions resulting from the Hospital's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year Ending September 30,</u>	<u>Amount</u>
2016	\$ 4,421,748
2017	3,222,174
2018	5,799,958
2019	1,897,879
2020	-
Thereafter	-

Actuarial Assumptions

The total pension liability in the June 30, 2016, actuarial valuation was determined using the following actuarial assumptions:

Inflation	2.50% per Year
Active Member Payroll Growth	3.25% per Year
Investment Rate of Return	7.50%

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 9 RETIREMENT PLANS (CONTINUED)

Actuarial Assumptions (Continued)

Salary increases were based on a service-related table. Mortality rates for active members, retirees, survivors and disabilitants were based on RP-2014 tables for males or females, as appropriate, with slight adjustments. Cost of living benefit increases for retirees are assumed to be 1% for all future years.

Actuarial assumptions used in the June 30, 2016, valuation were based on the results of actuarial experience studies. The most recent four-year experience study in the General Employees Plan was completed in 2015.

The following changes in actuarial assumptions occurred in 2016:

- The assumed post-retirement benefit increase rate was changed from 1.0% per year through 2035 and 2.5% per year thereafter to 1.0% per year for all future years.
- The assumed investment return was changed from 7.9% to 7.5%. The single discount rate was changed from 7.9% to 7.5%.
- Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed future salary increases, payroll growth, and inflation were decreased by 0.25% to 3.25% for payroll growth and 2.50% for inflation.

The long-term expected rate of return on pension plan investments is 7.5%. The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness of the long-term expected rate of return on a regular basis using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Asset Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic Stocks	45%	5.50 %
International Stocks	15	6.00
Bonds	18	1.45
Alternative Investments	20	6.40
Cash	2	0.50

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 9 RETIREMENT PLANS (CONTINUED)

Discount Rate

The discount rate used to measure the total pension liability in 2016 was 7.5%, a reduction from the 7.9% used in 2015. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rate specified in statute. Based on that assumption, each of the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Pension Liability Sensitivity

The following presents the Hospital's proportionate share of the net pension liability for all plans it participates in, calculated using the discount rate disclosed in the preceding paragraph, as well as what the Hospital's proportionate share of the net pension liability would be if it were calculated using a discount rate 1 percentage point lower or 1 percentage point higher than the current discount rate:

	1% Decrease (6.5%)	Discount Rate (7.5%)	1% Increase (8.5%)
Hospital's Proportionate Share of the Net Pension Liability	\$ 74,601,168	\$ 52,525,071	\$ 34,340,376

Detailed information about the pension plan's fiduciary net position is available in a separately-issued PERA financial report that includes financial statements and required supplementary information. That report may be obtained on the Internet at www.mnpera.org.

Voluntary Plans

The Hospital offers a voluntary salary deferral plan under IRC Section 457(b). All employees are eligible to participate in the plan; approximately \$7,689,993 and \$7,067,244 has been deferred as of December 31, 2016 and 2015, respectively, based on elections made by the participants. The hospital made no contributions to, nor received any benefit payments from the plan for the years ended December 31, 2016 and/or 2015.

NOTE 10 OPERATING LEASES

The Hospital leases equipment and facilities under operating leases expiring at various dates through January 2020. The leases have been classified as operating leases and, accordingly, all rents are charged to expenses as incurred. The following is a schedule by year of future minimum lease payments under operating leases as of December 31, 2016, that have initial or remaining lease terms in excess of one year.

<u>Year Ending December 31,</u>	<u>Amount</u>
2017	\$ 153,549
2018	95,858
2019	55,317
2020	4,625
Total	<u>\$ 309,349</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 11 ELECTRONIC HEALTH RECORD INCENTIVE PROGRAM

The Electronic Health Record (EHR) incentive program was enacted as part of the American Recovery and Reinvestment Act of 2009 (ARRA) and the Health Information Technology for Economic and Clinical Health (HITECH) Act. These Acts provided for incentive payments under both the Medicare and Medicaid programs to eligible hospitals and providers that demonstrate meaningful use of certified EHR technology.

The Hospital initially demonstrated meaningful use in 2011. Incentive payments of \$144,422 and \$209,185 were received in the fiscal years ended December 31, 2016 and 2015, respectively. This amount is recognized as other operating revenue in the statement of revenues, expenses and changes in net position. The final amount of the payment related to the hospital's attestation of Meaningful Use will be determined based on information from the organization's Medicare cost report for the year ended December 31, 2014. Events could occur that would cause the final payment to differ materially upon final settlement, therefore the hospital has estimated a 10% reserve for a potential payback of the incentive dollars for the hospital.

NOTE 12 COMMITMENTS AND CONTINGENCIES

Land Lease

The Hospital leases the land on which the facility is located from a local college. The lease term is for 60 years with two 20-year options. The annual rent expense for the first 20 years of the lease is approximately \$6,000. The rent expense in subsequent years will be equal to 5% of the appraised market price for rural agricultural land in the Dakota/Rice County Region. The rent expense would be adjusted to current market rates if certain events were to occur, such as the sale of the Hospital.

Self-Insurance Plan

The Hospital self-insures their employee health and dental insurance program. The Hospital has entered into an agreement with an insurance company to provide stop-loss insurance to limit the losses on individual and aggregate claims and to provide claims processing and other administrative functions. Claims are accrued as incurred. The amounts charged to expense include administrative fees, stop-loss insurance premiums, claims paid, and accruals for claims incurred but not yet paid at year-end. The total health and dental insurance expense for the years ended December 31, 2016 and 2015 was \$3,861,915 and \$4,076,702, respectively, and are included with Accrued Payroll and Benefits.

Estimates of amounts incurred but not reported at December 31, 2016 and 2015 are as follows:

	2016	2015
Beginning IBNR	\$ 1,932,141	\$ 1,641,027
Claims Paid	(5,598,184)	(4,632,063)
Claims Incurred	5,032,228	4,923,177
Ending IBNR	<u>\$ 1,366,185</u>	<u>\$ 1,932,141</u>

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2016 AND 2015**

NOTE 12 COMMITMENTS AND CONTINGENCIES (CONTINUED)

Medical Malpractice Insurance

The Hospital purchases medical malpractice insurance under a "claims made" policy on a fixed-premium basis. The Hospital has coverage for any individual claims exceeding \$1,000,000, and for aggregate claims exceeding \$3,000,000 for a policy year. Should this policy lapse and not be replaced with equivalent coverage, claims based upon occurrence during its term, but reported subsequent thereto, will be uninsured.

Risk Management

The Hospital is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters. These risks are covered by commercial insurance purchased from independent third parties. There has been no significant reduction in insurance coverage from the previous year in any of the Hospital's policies. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years.

Healthcare Legislation and Regulation

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violation of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Congress passed the Medicare Modernization Act in 2003, which among other things established a demonstration of The Medicare Recovery Audit Contractor (RAC) program. During fiscal year 2007, the RAC's identified and corrected a significant amount of improper overpayments to providers in the demonstration states, which did not include Minnesota. In 2006, Congress passed the Tax Relief and Health Care Act of 2006 which authorized the expansion of the RAC program to all 50 states. While the hospital was selected for a RAC audit during 2016 and 2015, they were not materially impacted and appear to have appropriate policies and procedures to mitigate the risks related to RAC reviews.

Management believes that the Hospital is in substantial compliance with fraud and abuse as well as other applicable government laws and regulations. Compliance with such laws and regulations is subject to government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
SCHEDULE OF THE HOSPITAL'S PROPORTIONATE
SHARE OF THE NET PENSION LIABILITY (UNAUDITED)
DECEMBER 31, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>
Hospital's Proportion of the Net Pension Liability	0.6470%	0.5948%
Hospital's Proportionate Share of the Net Pension Liability	\$ 52,533,192	\$ 30,825,624
Hospital's Covered-Employee Payroll	\$ 44,316,610	\$ 40,117,088
Hospital's Proportionate Share of the Net Pension Liability as a Percentage of its Covered-Employee Payroll	118.54%	76.84%
Plan Fiduciary Net Position as a Percentage of the Total Pension Liability	68.91%	78.20%

**NORTHFIELD HOSPITAL
DBA: NORTHFIELD HOSPITAL & CLINICS
SCHEDULE OF THE HOSPITAL'S CONTRIBUTIONS (UNAUDITED)
DECEMBER 31, 2016 AND 2015**

	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Statutorily Required Contribution	\$ 3,118,305	\$ 2,877,619	\$ 2,327,602	\$ 2,135,716
Contributions in Relation to the Statutorily Required Contribution	<u>3,118,305</u>	<u>2,877,619</u>	<u>2,327,602</u>	<u>2,135,716</u>
Contribution Deficiency (Excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Hospital Covered-Employee Payroll	\$ 44,316,610	\$ 40,117,088	\$ 33,751,616	\$ 31,123,432
Contributions as a Percentage of Covered-Employee Payroll	7.04%	7.17%	6.90%	6.86%
	<u>2012</u>			
Statutorily Required Contribution	\$ 1,956,802			
Contributions in Relation to the Statutorily Required Contribution	<u>1,956,802</u>			
Contribution Deficiency (Excess)	<u>\$ -</u>			
Hospital Covered-Employee Payroll	\$ 29,562,894			
Contributions as a Percentage of Covered-Employee Payroll	6.62%			

Note: GASB 68 requires ten years of information to be presented in this table. However, until a full ten years is compiled, the Hospital will present information for those years for which information is available.

INDEPENDENT AUDITORS' REPORT ON MINNESOTA LEGAL COMPLIANCE

Board of Directors
Northfield Hospital
dba: Northfield Hospital & Clinics
Northfield, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of Northfield Hospital dba: Northfield Hospital & Clinics (the Hospital), as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements, and have issued our report thereon dated April 18, 2017.

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Audit pursuant to Min. Stat. § 6.65, identifies six categories of compliance to be tested in connection with the audit of a Northfield Hospital's financial statements: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions. Our audit considered all of the listed categories.

In connection with our audit, nothing came to our attention that caused us to believe that Northfield Hospital dba: Northfield Hospital & Clinics failed to comply with the provisions of the Minnesota Legal Compliance Audit Guide for Political Subdivisions. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding Northfield Hospital's noncompliance with the above-referenced provisions, insofar as they relate to accounting matters.

The purpose of this report is solely to describe the scope of our testing of compliance relating to the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions* and the results of that testing, and not to provide an opinion on compliance. Accordingly, this report is not suitable for any other purpose.



CliftonLarsonAllen LLP

Minneapolis, Minnesota
April 18, 2017