SOUTHWELL OBLIGATED GROUP AS DEFINED IN THE MASTER TRUST INDENTURE BETWEEN TIFT COUNTY HOSPITAL AUTHORITY, SOUTHWELL, INC. AND TIFT REGIONAL HEALTH SYSTEM, INC.

TIFTON,GEORGIA

COMBINED SPECIAL-PURPOSE FINANCIAL STATEMENTS

for the years ended September 30, 2019 and 2018

C O N T E N T S

Draffin Tucker

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Tift County Hospital Authority
Southwell, Inc.
Tift Regional Health System, Inc.
Tifton, Georgia

Report on the Financial Statements

We have audited the accompanying combined special-purpose balance sheets of Southwell Obligated Group as defined in the Master Trust Indenture (MTI) between the Tift County Hospital Authority (Authority), Southwell, Inc. (Southwell) and Tift Regional Health System, Inc. (System) (collectively Southwell Obligated Group) as Obligated Issuers and U.S. Bank National Association as Master Trustee dated as of December 1, 2002, as amended and supplemented from time to time, as of September 30, 2019 and 2018, and the related combined special-purpose statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes to the combined special-purpose financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these combined special-purpose financial statements in accordance with requirements set forth in the Master Trust Indenture. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of combined special-purpose financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

Continued

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An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined special-purpose financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined special-purpose financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to Southwell Obligated Group's preparation and fair presentation of the combined special-purpose 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 Southwell Obligated Group's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the combined special-purpose financial statements.

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

Opinion

In our opinion, the combined special-purpose financial statements referred to above present fairly, in all material respects, the financial position of Southwell Obligated Group as of September 30, 2019 and 2018, and the results of its operations, changes in net assets, and its cash flows for the years then ended in accordance with the basis of accounting described in Note 1.

Emphasis of Matter

As disclosed in Note 1 to the combined special-purpose financial statements, effective March 1, 2019, the Authority undertook a corporate restructuring and executed a Lease and Transfer Agreement with the System, whereby the System agreed to lease substantially all of the assets, liabilities, and operations of the Authority for an initial period of forty years. The System is a wholly own subsidiary of Southwell. Also effective March 1, 2019, Southwell and the System were added as Obligated Issuers to the Master Trust Indenture to which the Authority was the sole Obligated Issuer before that date. Our opinion is not modified with respect to this matter.

Basis of Accounting

The accompanying combined special-purpose financial statements were prepared for the purpose of complying with, and in conformity with, the accounting principles specified in Section 6.6 of the Master Trust Indenture as discussed in Note 1, and are not intended to be a presentation in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

Changes in Accounting Principle

As discussed in Note 1 to the combined special-purpose financial statements, Southwell Obligated Group adopted new accounting guidance, Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-14 *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities.* Our opinion is not modified with respect to this matter.

Continued

Restriction on Use

This report is intended solely for the information and use of the Board of Directors and management of the Southwell Obligated Group and U.S. Bank National Association, as Master Trustee, and each nationally recognized municipal securities information repository for the purpose of Rule 15c2-12(b)(5) adopted by the Securities and exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time, and is not intended to be and should not be used by anyone other than these specified parties.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 27, 2020, on our consideration of Southwell Obligated Group's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Southwell Obligated Group's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Southwell Obligated Group's internal control over financial reporting and compliance.

Draffin & Tucker, LLP

Atlanta, Georgia
February 27, 2020

SOUTHWELL OBLIGATED GROUP

Combined Special-Purpose Balance Sheets
September 30, 2019 and 2018

	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	$ 61,187,000	$ 60,882,000
Short-term investments	5,259,000	5,150,000
Patient accounts receivable, net	56,667,000	63,889,000
Supplies, at lower of cost and net realizable value	2,912,000	3,145,000
Professional insurance recoverable	1,188,000	-
Other current assets	7,303,000	8,708,000
Total current assets	134,516,000	141,774,000
Assets limited as to use	493,974,000	473,141,000
Property and equipment, net	269,696,000	228,971,000
Other investments	849,000	849,000
Prepaid recruitment expense	1,425,000	1,280,000
Goodwill	4,491,000	7,008,000
Total assets	$ 904,951,000	$ 853,023,000
Liabilities and Net Assets		
Current liabilities:		
Current portion of long-term debt	$ 25,124,000	$ 6,122,000
Accounts payable	26,068,000	23,090,000
Accrued expenses	26,307,000	32,217,000
Estimated third-party payor settlements	3,286,000	4,445,000
Professional insurance payable	1,543,000	1,000,000
Total current liabilities	82,328,000	66,874,000
Long-term debt, net of current portion	255,974,000	243,232,000
Total liabilities	338,302,000	310,106,000
Net assets without donor restrictions	566,649,000	542,917,000
Total liabilities and net assets	$ 904,951,000	$ 853,023,000

See accompanying notes to combined special-purpose financial statements.

SOUTHWELL OBLIGATED GROUP

Combined Special-Purpose Statements of Operations and Changes in Net Assets
Years Ended September 30, 2019 and 2018

	2019	2018
Revenues, gains, and other support:		
Net patient service revenue	$ 385,680,000	$ 403,576,000
Other revenue	6,225,000	5,334,000
Total revenues, gains, and other support	391,905,000	408,910,000
Expenses:		
Salaries and wages	167,730,000	164,347,000
Employee benefits	43,274,000	42,346,000
Contract and purchased services	19,446,000	24,225,000
Physician services	14,032,000	14,952,000
Supplies and drugs	72,098,000	68,781,000
Depreciation	32,774,000	26,009,000
Goodwill amortization	2,517,000	2,507,000
Interest expense	4,193,000	4,493,000
Other expense	34,965,000	35,133,000
Total expenses	391,029,000	382,793,000
Operating income	876,000	26,117,000
Nonoperating gains:		
Investment income	21,359,000	20,104,000
Rural hospital tax credit contribution	757,000	2,032,000
Total nonoperating gains	22,116,000	22,136,000
Excess of revenues over expenses	22,992,000	48,253,000
Transfers from affiliated entities	740,000	316,000
Change in net assets without donor restrictions	23,732,000	48,569,000
Net assets without donor restrictions, beginning of year	542,917,000	494,348,000
Net assets without donor restrictions, end of year	$ 566,649,000	$ 542,917,000

See accompanying notes to combined special-purpose financial statements.

SOUTHWELL OBLIGATED GROUP

Combined Special-Purpose Statements of Cash Flows
Years Ended September 30, 2019 and 2018

	2019	2018
Cash flows from operating activities:		
Receipts from and on behalf of patients	$ 392,902,000	$ 381,101,000
Payments to employees	(216,914,000)	(142,630,000)
Payments to suppliers and contractors	(137,874,000)	(201,616,000)
Other receipts	6,225,000	5,334,000
Interest paid	(4,531,000)	(4,725,000)
Investment income	20,360,000	2,527,000
Rural hospital tax credit contributions	757,000	2,032,000
Transfer from affiliates	740,000	316,000
Net cash provided by operating activities	61,665,000	42,339,000
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	80,130,000	108,968,000
Payments on long-term debt	(48,048,000)	(6,008,000)
Net cash provided by financing activities	32,082,000	102,960,000
Cash flows from investing activities:		
Purchases of property and equipment, net of retirements	(73,499,000)	(51,263,000)
Sale of debt and equity securities	241,929,000	199,523,000
Purchase of debt and equity securities	(232,299,000)	(312,499,000)
Sale of short-term investments	5,300,000	5,050,000
Purchase of short-term investments	(5,153,000)	(4,800,000)
Net cash used by investing activities	(63,722,000)	(163,989,000)
Net change in cash and cash equivalents	30,025,000	(18,690,000)
Cash and cash equivalents, beginning of year	69,949,000	88,639,000
Cash and cash equivalents, end of year	$ 99,974,000	$ 69,949,000

Continued

Combined Special-Purpose Statements of Cash Flows, Continued
Years Ended September 30, 2019 and 2018

	2019	2018
Reconciliation of cash and cash equivalents to the balance sheets:		
Cash and cash equivalents	$ 61,187,000	$ 60,882,000
Cash and cash equivalents included in short-term investments	609,000	353,000
Cash and cash equivalents included in assets limited as to use	38,178,000	8,714,000
Total cash and cash equivalents	$ 99,974,000	$ 69,949,000
Reconciliation of change in net assets to net cash provided by operating activities:		
Change in net assets	$ 23,732,000	$ 48,569,000
Adjustments to reconcile change in net assets to cash provided by operating activities:		
Depreciation	32,774,000	26,009,000
Goodwill amortization	2,517,000	2,507,000
Change in unrealized gains and losses on investments	(999,000)	(17,577,000)
Bond premium amortization	(338,000)	(232,000)
Changes in:		
Patient accounts receivable	7,222,000	(22,475,000)
Supplies	233,000	(144,000)
Professional insurance recoverable	(1,188,000)	-
Other current assets	1,405,000	(1,301,000)
Prepaid recruitment expense	(145,000)	451,000
Accounts payable	2,978,000	(1,042,000)
Accrued expenses	(5,910,000)	5,159,000
Estimated third-party payor settlements	(1,159,000)	2,415,000
Professional insurance payable	543,000	-
Net cash provided by operating activities	$ 61,665,000	$ 42,339,000

See accompanying notes to combined special-purpose financial statements.

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

Reporting entity. The accompanying combined special-purpose financial statements of Southwell Obligated Group are comprised of Tift County Hospital Authority, Southwell, Inc., and Tift Regional Health System, Inc.

Tift County Hospital Authority (Authority) is a public body corporate and politic organized under the Hospital Authorities Law of the State of Georgia. Prior to the lease transaction described below, the Authority owned and operated Tift Regional Medical Center (an acute care hospital), Southwell Medical (an acute care hospital formerly known as Cook Medical Center), Southwell Health and Rehabilitation (a nursing home formerly known as Cook Senior Living Center), and several physician practices. The Authority provided short-term medical, surgical, obstetrical, pediatric, geriatric psychiatry, and physician care and long-term nursing care to patients in Tift County and the surrounding area.

Southwell, Inc. (Southwell) (formerly known as Keystone Medical Services Corporation), is the sole member of Tift Regional Health System, Inc. (System) (formerly known as Healthway Medical Services, Inc.).

Effective March 1, 2019, the Authority undertook a corporate restructuring and executed a Lease and Transfer Agreement (Agreement) with the System. Under the Agreement, the System assumed substantially all of the operations, assets, and liabilities of the Authority and agreed to operate the facilities for an initial period of forty years. Also, the System makes nominal lease payments to the Authority plus amounts sufficient to make debt service payments on Authority conduit debt obligations as they come due, and assumes all operational, financial, indigent care, and community responsibilities.

The combined special-purpose financial statements are prepared on a basis of accounting described in the Master Trust Indenture (MTI) between the Authority, Southwell, and the System as Obligated Issuers (Southwell Obligated Group) and U.S. Bank National Association as Master Trustee dated as of December 1, 2002, as amended and supplemented from time to time. The MTI requires a combined balance sheet and combined statement of operations and changes in net assets for Southwell Obligated Group. The accompanying combined special-purpose financial statements were prepared based on audited financial statements in accordance with generally accepted accounting principles for Southwell and the Authority. The System is included in Southwell's consolidated financial statements as a wholly owned subsidiary.

Southwell is subject to pronouncements of the Financial Accounting Standards Board (FASB) and the Authority is subject to pronouncements of the Governmental Accounting Standards Board (GASB). As Southwell is the more significant of the two entities, Southwell Obligated Group will apply the provisions of pronouncements issued by FASB in all areas of the combined special-purpose financial statements.

The accompanying combined special-purpose financial statements include Southwell, the System, and the Authority. All significant intercompany transactions have been eliminated.

Continued

1. Description of Reporting Entity and Summary of Significant Accounting Policies, Continued

Use of estimates. The preparation of combined special-purpose financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the combined special-purpose financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Significant items subject to such estimates and assumptions include the determination of variable consideration for patient contracts, estimated third-party payor settlements, and insurance reserves. In particular, laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates associated with these programs will change by a material amount in the near term.

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

Short-term investments. Short-term investments consist of certificates of deposit with maturities ranging from 6 months to 12 months.

Investments. Investments in equity securities with readily determinable fair values and all investments in debt securities, which are all classified as trading securities, are measured at fair value in the balance sheet. Investments without a readily determinable fair value are measured at cost, minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment of the same issuer. Investment income or loss (including interest, dividends, and gains and losses, both realized and unrealized) is included in excess of revenues over expenses unless the income is restricted by donor or law.

Investments without a readily determinable fair value are included in other investments on the balance sheets. These investments consist of an 8.00% investment in Distribution Cooperative, Inc. and a 15.12% investment in Stratus Healthcare, LLC.

Fair value measurements. FASB ASC 820, *Fair Value Measurement and Disclosures* defines fair value as the amount that would be received for an asset or paid to transfer a liability (i.e., an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes a fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. FASB ASC 820 describes the following three levels of inputs that may be used:

- *Level 1:* Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets and liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Continued

1. Description of Reporting Entity and Summary of Significant Accounting Policies, Continued

Fair value measurements, continued.

- *Level 2:* Observable prices that are based on inputs not quoted on active markets but corroborated by market data.
- *Level 3:* Unobservable inputs when there is little or no market data available, thereby requiring an entity to develop its own assumptions. The fair value hierarchy gives the lowest priority to Level 3 inputs.

Assets limited as to use. Assets limited as to use include assets held by trustee for capital acquisitions and for debt service reserve, and assets internally designated for capital acquisitions and malpractice self-insurance, over which the Board retains control and may at its discretion subsequently use for other purposes.

Property and equipment. Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed on the straight-line method. Buildings and equipment under capital lease obligations are amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the building or equipment. Such amortization is included in depreciation in the combined special-purpose financial statements.

Gifts of long-lived assets such as land, buildings, or equipment are reported as increases in net assets without donor restrictions, and are excluded from excess of revenues over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as increases in net assets with donor restrictions. 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.

Impairment of long-lived assets. Southwell Obligated Group evaluates on an ongoing basis the recoverability of its assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is required to be recognized if the carrying value of the asset exceeds the undiscounted future net cash flows associated with that asset. The impairment loss to be recognized is the amount by which the carrying value of the long-lived asset exceeds the asset's fair value. In most instances, the fair value is determined by discounted estimated future cash flows using an appropriate interest rate. Southwell Obligated Group has not recorded any impairment charges in the accompanying combined special-purpose statement of operations and changes in net assets for the years ended September 30, 2019 and 2018.

Continued

1. Description of Reporting Entity and Summary of Significant Accounting Policies, Continued

Prepaid recruitment expense. Southwell Obligated Group has entered into recruiting arrangements and educational loans with physicians that are to be repaid with interest at the prime rate plus 1%. The loans may be considered repaid by the physicians meeting certain community service obligations for a period of time. When and if these conditions are met, the loans are forgiven. If the physician ceases to meet the community service obligations before the loan is forgiven, the outstanding principal and accrued interest becomes due immediately. The amount of loans to physicians charged to expense was approximately $565,000 and $765,000 during 2019 and 2018, respectively. These expenses are reflected in physician services in the accompanying combined special-purpose statement of operations and changes in net assets.

Costs of borrowing. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Interest cost capitalized was approximately $3,226,000 and $896,000 during 2019 and 2018, respectively.

Costs incurred in connection with the issuance of long-term debt are deferred and amortized over the term of the debt using the effective interest method. Debt issuance costs related to a recognized debt liability are presented in the balance sheet as a direct deduction from the carrying amount of the related debt liability.

Goodwill. Goodwill represents the excess of the acquisition price over the fair value of net assets acquired through business combinations. Goodwill is being amortized over five years, the time period of restrictive non-compete covenants included with the acquisition of physician practices. When events or circumstances indicate that goodwill may be impaired, goodwill is tested for impairment. Impairment, if any, will be recognized for the difference between the fair value of the physician practice and its carrying amount and will be limited to the carrying amount of goodwill.

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

- *Net assets without donor restrictions* – net assets available for use in general operations and not subject to donor-imposed restrictions. The Board of Directors has discretionary control over these resources. Designated amounts represent those net assets that the Board has set aside for a particular purpose. All revenue not restricted by donors and donor restricted contributions whose restrictions are met in the same period in which they are received are accounted for in net assets without donor restrictions.

- *Net assets with donor restrictions* – net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. All revenues restricted by donors as to either timing or purpose of the related expenditures or required to be maintained in perpetuity as a source of investment income are accounted for in net assets with donor restrictions. When a donor restriction expires, that is when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions.

Continued

1. Description of Reporting Entity and Summary of Significant Accounting Policies, Continued

Excess of revenues over expenses. The combined special-purpose statements of operations and changes in net assets includes excess of revenues over expenses. Changes in net assets without donor restrictions which are excluded from excess of revenues over expenses, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets).

Net patient service revenue. Southwell Obligated Group has agreements with third-party payors that provide for payments to Southwell Obligated Group at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the amount that reflects the consideration to which Southwell Obligated Group expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors, and others and includes variable consideration for retroactive revenue adjustments under reimbursement arrangements with third-party payors. Retroactive adjustments are included in the determination of the estimated transaction price and adjusted in future periods as settlements are determined.

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

Donor restricted gifts. Unconditional promises to give cash and other assets to Southwell Obligated Group are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as increases in the appropriate categories of net assets in accordance with donor restrictions.

Estimated malpractice and other self-insurance costs. The provisions for estimated medical malpractice claims and other claims under self-insurance plans include estimates of the ultimate costs for both reported claims and claims incurred but not reported.

Income taxes. The Authority is a governmental entity and is exempt from income taxes. Southwell and the System are not-for-profit corporations and have been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code.

Southwell Obligated Group applies accounting policies that prescribe when to recognize and how to measure the financial statement effects of income tax positions taken or expected to be taken on its income tax returns. These rules require management to evaluate the likelihood that, upon examination by the relevant taxing jurisdictions, those income tax positions would be sustained. Based on that evaluation, Southwell Obligated Group only recognizes the maximum benefit of each income tax position that is more than 50% likely of being sustained. To the extent that all or a portion of the benefits of an income tax position are not recognized , a liability would be recognized for the unrecognized benefits, along with any interest and penalties that would result from disallowance of the position. Should any such penalties and interest be incurred, they would be recognized as operating expenses.

Continued

1. Description of Reporting Entity and Summary of Significant Accounting Policies, Continued

Income taxes, continued. Based on the results of management's evaluation, no liability is recognized in the accompanying balance sheets for unrecognized income tax positions. Further, no interest or penalties have been accrued or charged to expense as of September 30, 2019 and 2018 or for the years then ended. Southwell Obligated Group's tax returns are subject to possible examination by the taxing authorities. For federal income tax purposes, the tax returns essentially remain open for possible examination for a period of three years after the respective filing deadlines of those returns.

Recently adopted accounting pronouncements. In 2019, Southwell Obligated Group adopted FASB ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606),* which is a new comprehensive revenue recognition standard. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Southwell Obligated Group adopted ASU No. 2014-09 on October 1, 2018 using the full retrospective method of transition with practical expedients in FASB ASC 606-10-65-1(f) with no significant impact. Southwell Obligated Group performed an analysis of revenue streams and transactions under ASU No. 2014-09. In particular, for net patient service revenue, Southwell Obligated Group performed an analysis into the application of the portfolio approach as a practical expedient to group patient contracts with similar characteristics, such that revenue for a given portfolio would not be materially different than if it were evaluated on a contract-by-contract basis. Upon adoption, the majority of what was previously classified as provision for bad debts (representing approximately $67,214,000 for the year ended September 30, 2018) and presented as a reduction to net patient service revenue on the statements of operations is now treated as a price concession that reduces the transaction price, which is reported as net patient service revenue. Changes in credit issues not assessed at the date of service, are recognized as bad debt expense and included as a component of operating expenses on the statement of operations. The new standard also requires enhanced disclosures related to the disaggregation of revenue and significant judgments made in measurement and recognition. The adoption of this guidance did not materially impact total operating revenues, excess of revenues over expenses, or net assets.

In 2019, Southwell Obligated Group adopted FASB ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities.* This comprehensive standard provides guidance on net asset classification and required disclosures on liquidity and availability of resources, requires expanded disclosure about expense and investment returns, and eliminates the requirement to present or disclose the indirect method reconciliation if using the direct method when presenting cash flows. Southwell Obligated Group has adjusted the presentation of these financial statements for all periods presented, except for the disclosures around liquidity and availability of resources and analysis of expenses by nature and function. Those disclosures have been presented for 2019 only.

In 2019, Southwell Obligated Group adopted FASB ASU No. 2019-06, *Intangibles – Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958),* which allows goodwill to be amortized on a straight-line basis and tested for impairment only when events or circumstances indicate that goodwill is impaired. Management believes that this accounting method more accurately reflects the financial position and results of operations.

Continued

1. Description of Reporting Entity and Summary of Significant Accounting Policies, Continued

Recently adopted accounting pronouncements, continued. In 2019, Southwell Obligated Group early adopted FASB ASU No. 2016-01, *Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial* Assets *and Financial Liabilities.* The new guidance requires equity investments (except those accounted for under the equity method or those that result in consolidation) to be measured at fair value, with changes in fair value recognized in net income; simplifies the impairment assessment of equity investments without readily determinable fair values; and amends certain disclosure requirements associated with the fair value of financial instruments.

In 2019, Southwell Obligated Group early adopted FASB ASU 2016-18, *Statement of* Cash *Flows – Restricted* Cash, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows.

Accounting pronouncement not yet adopted. In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842),* which is a new comprehensive lease accounting model. The new standard clarifies the definition of a lease and requires lessees to recognize right-of-use assets and related lease liabilities for all leases with terms greater than twelve months. The new guidance, including subsequent amendments, is effective for Southwell Obligated Group as of October 1, 2019. Southwell Obligated Group is continuing to evaluate the impact the guidance will have on the financial statements.

Subsequent event. In preparing these financial statements, Southwell Obligated Group has evaluated events and transactions for potential recognition or disclosure through February 27, 2020, the date the financial statements were issued.

2. Net Patient Service Revenue

Net patient service revenue is reported at the amount that reflects the consideration to which Southwell Obligated Group expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others and includes variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, Southwell Obligated Group bills the patients and third-party payors several days after the services are performed and/or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. Southwell Obligated Group believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients receiving inpatient, outpatient, and emergency care services. Southwell Obligated Group measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. These services are considered to be a single performance obligation and have a duration of less than one year. Revenue for performance obligations satisfied at a point in time is recognized when services are provided and it is believed that additional services are not required to be provided to the patient.

Continued

2. Net Patient Service Revenue, Continued

Because all of its performance obligations relate to contracts with a duration of less than one year, Southwell Obligated Group has elected to apply the optional exemption provided in FASB ASC 606-10-50-14(a) and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

Southwell Obligated Group is utilizing the portfolio approach practical expedient in ASC 606 for contracts related to net patient service revenue. Southwell Obligated Group accounts for the contracts within each portfolio as a collective group, rather than individual contracts, based on the payment pattern expected in each portfolio category and the similar nature and characteristics of the patients within each portfolio. As a result, Southwell Obligated Group has concluded that revenue for a given portfolio would not be materially different than if accounting for revenue on a contract by contract basis.

Southwell Obligated Group has arrangements with third-party payors that provide for payments to Southwell Obligated Group at amounts different from its established rates. For uninsured patients that do not qualify for charity care, Southwell Obligated Group recognizes revenue on the basis of its standard rates, subject to certain discounts and implicit price concessions as determined by Southwell Obligated Group. Southwell Obligated Group determines the transaction price based on standard charges for services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with Southwell Obligated Group's policy, and implicit price concessions provided to uninsured patients. Implicit price concessions represent difference between amounts billed and the estimated consideration Southwell Obligated Group expects to receive from patients, which are determined based on historical collection experience, current market conditions, and other factors. Southwell Obligated Group determines its estimates of contractual adjustments and discounts based on contractual agreements, discount policies, and historical experience.

Agreements with third-party payors typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payors follows:

- *Medicare.* Inpatient and outpatient services rendered to Medicare program beneficiaries are generally are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Certain other reimbursable items are reimbursed at a tentative rate with final settlement determined after submission of annual cost reports by Southwell Obligated Group and audits thereof by the Medicare Administrative Contractor (MAC). Southwell Obligated Group's Medicare cost reports have been settled by the MAC through September 30, 2014.

  Nursing home services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system called Resource Utilization Groups (RUGs).

Continued

2. Net Patient Service Revenue, Continued

- *Medicaid.* Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates. Outpatient services rendered to Medicaid program beneficiaries are generally reimbursed under a cost reimbursement methodology. Southwell Obligated Group is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by Southwell Obligated Group and audits thereof by the Medicaid fiscal intermediary. Southwell Obligated Group's Medicaid cost reports have been settled by the Medicaid fiscal intermediary through September 30, 2015.

  Southwell Obligated Group has also entered into contracts with certain care management organizations (CMOs) to receive reimbursement for providing services to selected enrolled Medicaid beneficiaries. Payment arrangements with these CMOs consist primarily of prospectively determined rates and discounts from established charges.

  Long-term care services are reimbursed by the Medicaid program based on a prospectively determined per diem. The per diem is determined by the facility's historical allowable operating costs adjusted for certain incentives and inflation factors.

  Southwell Obligated Group participates in the Indigent Care Trust Fund (ICTF) Program. Southwell Obligated Group receives ICTF payments for treating a disproportionate number of Medicaid and other indigent patients. ICTF payments are based on Southwell Obligated Group's estimated uncompensated cost of services to Medicaid and uninsured patients. The net amount of ICTF payments recognized in net patient service revenue was approximately $2,739,000 and $4,412,000 for the years ended September 30, 2019 and 2018, respectively.

  The State of Georgia has legislation known as the Provider Payment Agreement Act (Act) whereby hospitals in Georgia are assessed a “provider payment” in the amount of 1.45% of their net patient revenue. The provider payments are due on a quarterly basis to the State of Georgia. The payments are used for the sole purpose of obtaining federal financial participation for medical assistance payments to providers on behalf of Medicaid recipients. The provider payment results in a corresponding increase in Medicaid payments for hospital services of approximately 11.88%. Southwell Obligated Group made provider payments to the State of Georgia of approximately $4,105,000 and $3,660,000 for the years ended September 30, 2019 and 2018, respectively. The payments are included in other expense in the accompanying statements of operations.

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

Continued

2. Net Patient Service Revenue, Continued

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge Southwell Obligated Group's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon Southwell Obligated Group. In addition, the contracts Southwell Obligated Group has with commercial payors also provide for retroactive audit and review of claims.

Settlements with third-party payors for retroactive adjustments due to audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor and Southwell Obligated Group's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available), or as years are settled or are no longer subject to such audits, reviews, and investigations. Adjustments arising from a change in the transaction price, were not significant in 2019 and 2018.

Generally patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. Southwell Obligated Group also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. Southwell Obligated Group estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. Adjustments arising from a change in the transaction price were not significant for the years ending September 30, 2019 and 2018. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense. Bad debt expense for the years ended September 30, 2019 and 2018 were not significant.

Consistent with Southwell Obligated Group's mission, care is provided to patients regardless of their ability to pay. Therefore, Southwell Obligated Group has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles).

Patients who meet Southwell Obligated Group's criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue.

Continued

2. Net Patient Service Revenue, Continued

Net patient service revenue by major payor source for the years ended September 30, 2019 and 2018 is as follows:

	2019	2018
Medicare	$ 150,033,000	$ 168,276,000
Medicaid	25,859,000	45,291,000
Blue Cross	129,679,000	137,304,000
Other third-party payors	80,109,000	52,705,000
Total	$ 385,680,000	$ 403,576,000

Net patient service revenue by facility and timing of revenue recognition for the years ended September 30, 2019 and 2018 is as follows:

	2019	2018
Tift Regional Medical Center	$ 371,238,000	$ 387,821,000
Southwell Medical	14,442,000	15,755,000
Total services transferred over time	$ 385,680,000	$ 403,576,000

Net patient service revenue includes a variety of services mainly covering inpatient acute care services requiring overnight stays, outpatient procedures that require anesthesia or use of diagnostic and surgical equipment, and emergency care services. Performance obligations are satisfied over time as the patient simultaneously receives and consumes the benefits Southwell Obligated Group performs. Requirements to recognize revenue for inpatient services are generally satisfied over periods that average approximately five days and for outpatient services are generally satisfied over a period of less than one day. For employee pharmacy and cafeteria, recorded in other revenue on the combined statement of operations, performance obligations are satisfied at a point in time when the goods are provided.

Southwell Obligated Group has elected the practical expedient allowed under FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to Southwell Obligated Group's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, Southwell Obligated Group does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Southwell Obligated Group has applied the practical expedient provided by FASB ASC 340-40-25-4 and all incremental customer contract acquisition costs are expensed as they are incurred as the amortization period of the asset that Southwell Obligated Group otherwise would have recognized is one year or less in duration.

Continued

3. Uncompensated Care

Southwell Obligated Group was compensated for services at amounts less than its standard charges. Net patient service revenue includes amounts representing the transaction price based on standard charges reduced by variable considerations such as contractual adjustments, discounts, and implicit price concessions. The following is a reconciliation of gross patient revenue at standard charges to net patient service revenue:

	2019	2018
Gross patient charges	$ 1,440,720,000	$ 1,367,815,000
Uncompensated services:		
Medicare	608,233,000	547,614,000
Medicaid	165,916,000	116,281,000
Blue Cross	44,105,000	27,950,000
Other third-party payors	82,488,000	131,406,000
Charity/indigent/uninsured discount	86,028,000	73,774,000
Price concessions	68,270,000	67,214,000
Total uncompensated care	1,055,040,000	964,239,000
Net patient service revenue	$ 385,680,000	$ 403,576,000

The estimated cost of charity/indigent care/uninsured discount was approximately $23,349,000 and $20,646,000 in 2019 and 2018. The estimated cost of charity/indigent care/uninsured discount includes the direct and indirect cost of providing charity/indigent care/uninsured discount services and is estimated by utilizing a ratio of cost to gross charges applied to the gross uncompensated charges associated with providing charity/indigent care.

4. Concentrations of Credit Risk

Southwell Obligated Group grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables from patients and third-party payors at September 30, 2019 and 2018 was as follows:

	2019	2018
Medicare	28%	30%
Medicaid	9%	11%
Blue Cross	25%	26%
Other third-party payors	34%	33%
Self-pay	4%	- %
Total	100%	100%

Southwell Obligated Group maintains deposits at major financial institutions which exceed the $250,000 Federal Deposit Insurance Corporation limit. Management believes the credit risks related to these deposits is minimal.

Continued

5. Assets Limited as to Use

The composition of assets limited as to use as of September 30, 2019 and 2018 is set forth in the following table.

	2019	2018
Internally designated for capital acquisitions:		
Cash	$ 101,000	$ 13,000
Money market (cash equivalent)	10,544,000	5,248,000
Certificates of deposit	2,831,000	1,221,000
U.S. Treasury obligations	49,917,000	30,116,000
U.S. Government agency obligations	8,136,000	14,090,000
Corporate obligations	56,349,000	49,233,000
Asset-backed securities	81,136,000	67,363,000
Marketable equity securities	142,269,000	162,684,000
Non-U.S. equity mutual funds	18,159,000	18,141,000
Commodity funds	15,997,000	18,441,000
Other mutual funds	19,003,000	18,496,000
Total	404,442,000	385,046,000
Internally designated for self-insurance:		
Cash	784,000	759,000
Certificates of deposit	3,100,000	3,100,000
Total	3,884,000	3,859,000
Held by trustee for capital acquisitions:		
Money market (cash equivalent)	26,570,000	2,694,000
U.S. Treasury obligations	58,899,000	81,542,000
Total	85,469,000	84,236,000
Held by trustee for debt service reserve:		
Cash	179,000	-
Total assets limited as to use	$ 493,974,000	$ 473,141,000

Continued

5. Assets Limited as to Use, Continued

The fair values of investments measured on a recurring basis at September 30, 2019 and 2018 are as follows:

	2019			
	Total	Level 1	Level 2	Level 3
Money market funds	$ 37,114,000	$ 37,114,000	$ -	$ -
Certificates of deposit	5,931,000	5,931,000	-	-
U.S. Treasury obligations	108,816,000	108,816,000	-	-
U.S. Government agency obligations	8,136,000	8,136,000	-	-
Corporate obligations	56,349,000	-	56,349,000	-
Asset-backed securities	81,136,000	-	81,136,000	-
Marketable equity securities	142,269,000	142,269,000	-	-
Non-U.S. equity mutual funds	18,159,000	18,159,000	-	-
Commodity mutual funds	15,997,000	15,997,000	-	-
Other mutual funds	19,003,000	19,003,000	-	-
Total	$ 492,910,000	$ 355,425,000	$ 137,485,000	$ -

	2018			
	Total	Level 1	Level 2	Level 3
Money market funds	$ 7,942,000	$ 7,942,000	$ -	$ -
Certificates of deposit	4,321,000	4,321,000	-	-
U.S. Treasury obligations	111,658,000	111,658,000	-	-
U.S. Government agency obligations	14,090,000	14,090,000	-	-
Corporate obligations	49,233,000	-	49,233,000	-
Asset-backed securities	67,363,000	-	67,363,000	-
Marketable equity securities	162,684,000	162,684,000	-	-
Non-U.S. equity mutual funds	18,141,000	18,141,000	-	-
Commodity mutual funds	18,441,000	18,441,000	-	-
Other mutual funds	18,496,000	18,496,000	-	-
Total	$ 472,369,000	$ 355,773,000	$ 116,596,000	$ -

Continued

5. Assets Limited as to Use, Continued

A summary of investment income follows:

	2019	2018
Interest and dividends	$ 10,930,000	$ 7,880,000
Realized gains from sale of investments	9,136,000	(4,480,000)
Unrealized gains on investments	999,000	17,577,000
Rental income, net of expenses	(111,000)	(163,000)
Gain on disposal of capital assets	(76,000)	(773,000)
Other income	481,000	63,000
Total	$ 21,359,000	$ 20,104,000

Southwell Obligated Group's investments are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying combined special-purpose financial statements.

6. Property and Equipment

A summary of property and equipment at September 30, 2019 and 2018 follows:

	2019	2018
Land	$ 9,749,000	$ 9,498,000
Land improvements	3,526,000	3,411,000
Buildings and improvements	190,334,000	187,242,000
Fixed equipment	24,966,000	24,947,000
Major movable equipment	308,347,000	294,168,000
	536,922,000	519,266,000
Less accumulated depreciation	339,806,000	310,126,000
	197,116,000	209,140,000
Construction-in-progress	72,580,000	19,831,000
Property and equipment, net	$ 269,696,000	$ 228,971,000

Contracts of approximately $154,716,000 exist for the construction of a new patient tower, the renovation and expansion of the emergency center, the construction of the Cook Medical Center replacement facility, and various other projects. At September 30, 2019, the remaining commitment on these contracts approximated $102,210,000.

Continued

7. Goodwill

Goodwill is related to the purchases of Tiftarea Surgical Partners, LLC (TSP), Georgia Sports Medicine & Orthopedic Clinic, P.C. (GSM), Tiftarea Urology, P.C. (TU), Urosurg, LLC (US), and Tifton Ophthalmology Associates, P.C. (TOA). The changes in the carrying amount of goodwill are as follows:

	Balance at September 30, 2018	Additions	Amortization	Balance at September 30, 2019
TSP and GSM	$ 1,659,000	$ -	$ 995,000	$ 664,000
TU and US	5,241,000	-	1,497,000	3,744,000
TOA	108,000	-	25,000	83,000
Total	$ 7,008,000	$ -	$ 2,517,000	$ 4,491,000

	Balance at September 30, 2017	Additions	Amortization	Balance at September 30, 2018
TSP and GSM	$ 2,654,000	$ -	$ 995,000	$ 1,659,000
TU and US	6,739,000	-	1,498,000	5,241,000
TOA	-	122,000	14,000	108,000
Total	$ 9,393,000	$ 122,000	$ 2,507,000	$ 7,008,000

8. Long-Term Debt

A summary of long-term debt at September 30, 2019 follows:

	2019	2018
2013 Series – 2.00% to 5.00% 2013 Series Revenue Anticipation Certificates, principal maturing in varying annual amounts and interest payable semi-annually, secured by the Trust Estate and an intergovernmental contract with Tift County, due December 1, 2042.	$ 76,100,000	$ 77,840,000
2016-A Bank – 1.80% note payable, payable in monthly installments of $383,000 including interest, secured by EMR system and Trust Estate, due July 2026.	29,508,000	33,198,000

Continued

8. Long-Term Debt, Continued

	2019	2018
2016-B Bank – interest at a rate equal to 67% of the LIBOR daily floating rate plus 0.45%, interest payable monthly and principal due at maturity, secured by the Trust Estate, due December 18, 2018.	$ -	$ 37,982,000
2018-A Bank – 2.80% note payable, interest payable quarterly and principal payment due at maturity, secured by Trust Estate, due March 24, 2022.	90,300,000	90,300,000
2018-C Bank – interest at a rate equal to 81.50% of the sum of the LIBOR daily floating rate plus 0.29% (1.95% at September 30, 2019), interest payable monthly and principal due at maturity, secured by the Trust Estate, due February 27, 2020.	18,200,000	3,800,000
2018-D Bank – interest at a rate equal to 81.50% of the sum of the LIBOR daily floating rate plus 0.29% (1.95% at September 30, 2019), interest payable monthly and principal due at maturity, secured by the Trust Estate, due February 27, 2020.	20,000,000	-
2019-USDA – 2.375% note payable, payable in monthly installments of $163,000 including interest, secured by the Trust Estate, due November 17, 2048.	41,130,000	-
Building lease – interest at a rate equal to 65% of the prime rate published by the *Wall Street Journal* (3.58% at September 30, 2019), secured by leased building. Payable in monthly installments of $4,000 including interest, due October 16, 2034.	634,000	669,000
Total long-term debt	275,872,000	243,789,000
Add unamortized bond premium	5,226,000	5,565,000
Less current portion of long-term debt	(25,124,000)	(6,122,000)
Long-term debt, net of current portion	$ 255,974,000	$ 243,232,000

Continued

8. Long-Term Debt, Continued

Southwell Obligated Group operates under a Master Trust Indenture (MTI) that provides for the issuance of long-term debt under an obligated group structure. Through February 28, 2019, the Authority was the sole member of the Obligated Group. Effective March 1, 2019, Southwell and the System were added as members of the Obligated Group. All bonds and notes payable are covered under the MTI. Debt agreements covered by the MTI are secured by the Trust Estate which consists of a first pledge and lien on gross revenues of the Obligated Group.

On January 17, 2013, Southwell Obligated Group issued $83,260,000 Revenue Anticipation Certificates Series 2013 (2013 Series). As security, Southwell Obligated Group created a first pledge of and lien on the gross revenues of Southwell Obligated Group. Pursuant to an intergovernmental contract, Tift County is obligated to make payments, if necessary, in amounts sufficient (limited to ad valorem tax not to exceed 7 mills) to enable Southwell Obligated Group to provide for the payment of principal and interest on the 2013 Series. Proceeds from the Series 2013 were issued to (i) finance or refinance certain additions, extensions, and improvements to Southwell Obligated Group's healthcare and related facilities, (ii) refund Southwell Obligated Group's outstanding 2002 Fixed, (iii) repay a bank loan, and (iv) pay the cost of issuing the 2013 Series.

On July 1, 2016, Southwell Obligated Group entered into a master equipment lease/purchase agreement (2016-A Bank) for $42,000,000 with a financial institution. Proceeds of the 2016-A Bank will be used for the acquisition, installation, and implementation of an Electronic Medical Records (EMR) system. During the term of the 2016-A Bank, Southwell Obligated Group must maintain a debt service coverage ratio greater than or equal to 1.10.

On December 20, 2016, Southwell Obligated Group entered into a loan agreement (2016-B Bank) for $47,695,000 with a financial institution. Proceeds of the 2016-B Bank was used for (i) financing the costs of certain additions, extensions, and improvements to Southwell Obligated Group's facilities, (ii) repay a bank loan, and (iii) paying the closing costs of the loan. During the term of the 2016-B Bank, Southwell Obligated Group must maintain a debt service coverage ratio greater than or equal to 1.25 and days unrestricted cash on hand greater than or equal to 90. The 2016-B Bank was paid off with proceeds of the 2019-USDA loan.

On September 24, 2018, Southwell Obligated Group entered into a loan agreement (2018-A Bank) for $90,300,000 with a financial institution. Proceeds of the 2018-A Bank will be used for the construction of a patient tower and a new emergency center. During the term of the 2018-A Bank, Southwell Obligated Group must maintain a debt service coverage ratio greater than or equal to 1.25 and days unrestricted cash on hand greater than or equal to 75. Also on that date, Southwell Obligated Group obtained a nonrevolving line-of-credit with the financial institution for $62,020,000 (2018-B Bank) subject to the same use and covenants as the 2018-A Bank. As of September 30, 2019, Southwell Obligated Group had not drawn on 2018-B Bank.

On February 28, 2018, Southwell Obligated Group entered into a loan agreement (2018-C Bank) for $18,200,000 with a financial institution. Proceeds of the 2018-C Bank will be used for the Cook Medical Center replacement facility. During the term of the 2018-C Bank, Southwell Obligated Group must maintain a debt service coverage ratio greater than or equal to 1.25 and days unrestricted cash on hand greater than or equal to 75. Also on that date, Southwell Obligated Group entered into a loan agreement with the financial institution for $20,000,000 (2018-D Bank) subject to the same use and covenants as the 2018-C Bank.

Continued

8. Long-Term Debt, Continued

On December 17, 2018, Southwell Obligated Group entered into a loan agreement (2019-USDA) for $41,856,000 with the United States Department of Agriculture (USDA). Proceeds of the 2019-USDA were used to repay the 2016-B Bank. During the term of the 2019-USDA, Southwell Obligated Group must maintain a debt service coverage ratio greater than or equal to 1.10 and fund a debt service reserve fund.

On December 19, 2016, Southwell Obligated Group received a loan commitment from the USDA to borrow $90,300,000 for the future refinancing of the 2018-A Bank. On August 22, 2017, Southwell Obligated Group received a loan commitment from the USDA to borrow $20,000,000 for the future refinancing of the 2018-D Bank. All of the USDA loans will be payable over 30 years.

On October 15, 2004, Southwell Obligated Group entered into a contract for the construction and lease of a medical office building. Southwell Obligated Group and the Tift County Development Authority (Tift Development) each provided $800,000 towards the acquisition of property and construction of a building used for occupational health services. Tift Development holds title to the premises and leases the premises to Southwell Obligated Group. The lease is for a primary term of ten years without any rental payments or accrued interest and for an extended twenty-year term at a monthly rental sufficient in amount to amortize Tift Development's $800,000 investment in equal and consecutive payments. The payments include interest computed at a rate equal to 65% of the prime rate published by *The Wall Street Journal* and adjusted on January 1 of each year. The Southwell Obligated Group may purchase the premises at any time during the primary or extended term of the lease for the unamortized balance of Tift Development's investment plus $1,000.

As a condition of its worker's compensation insurance, Southwell Obligated Group has a letter-of-credit from a bank. The letter-of-credit is for $1,095,000 for insurance policy year ending December 31, 2019. As of September 30, 2019, Southwell Obligated Group had not drawn on the letter-of-credit.

Scheduled principal repayments on long-term debt and payments on capital lease obligations are as follows:

Year Ending September 30,	Long-Term Debt	Capital Lease Obligations
2020	$ 25,320,000	$ 36,000
2021	7,484,000	37,000
2022	8,711,000	38,000
2023	9,982,000	38,000
2024	10,246,000	39,000
Thereafter	213,495,000	446,000
Total	275,238,000	634,000
Add unamortized bond premium	5,226,000	-
Total	$ 280,464,000	$ 634,000

Continued

9. Retirement Plans

Southwell Obligated Group has defined contribution plans established to provide benefits at retirement to all employees. All employees may make contributions up to a maximum annual amount as set periodically by the Internal Revenue Service. Southwell Obligated Group makes matching contributions to the plans. Southwell Obligated Group’s contributions to the plans were approximately $6,019,000 and $8,724,000 during 2019 and 2018, respectively.

10. Commitments and Contingencies

Operating leases. Southwell Obligated Group leases various equipment and facilities under operating leases. Total rental expense for all operating leases was approximately $859,000 and $982,000 in 2019 and 2018, respectively. There are no future minimum lease payments under operating leases that have initial or remaining lease terms in excess of one year.

Litigation. Southwell Obligated Group is involved in litigation, regulatory investigations, and compliance matters arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on Southwell Obligated Group's future financial position or results from operations.

Medicare recovery audit contractors. The Centers for Medicare and Medicaid Services utilizes Recovery Audit Contractors (RACs) who are paid a contingent fee to detect and correct improper Medicare payments. RACs have authority to pursue improper payments with a three year look back from the date a claim was paid.

Southwell Obligated Group has received notifications from RACs regarding potential Medicare overpayments due to incorrect coding of claims. When notification of a potential claim overpayment is received, Southwell Obligated Group accrues a liability for the estimated amount of Medicare overpayment. The liability is then reduced when claims are refunded to Medicare or successfully appealed. Southwell Obligated Group has recorded an estimated liability of $250,000 and $1,352,000 at September 30, 2019 and 2018, respectively, related to claims being audited by the RAC. The estimated liability is reported in estimated third-party payor settlements in the balance sheets.

Health care reform. There has been increasing pressure on Congress and some state legislatures to control and reduce the cost of healthcare at the national and the state levels. Legislation has been passed that includes cost controls on healthcare providers, insurance market reforms, delivery system reforms, and various individual and business mandates among other provisions. The costs of certain provisions will be funded in part by reductions in payments by government programs, including Medicare and Medicaid. There can be no assurance that these changes will not adversely affect Southwell Obligated Group.

Continued

11. Insurance Arrangements

General and professional liability. Southwell Obligated Group has claims-made insurance coverage for professional liability and occurrence insurance coverage for general liability. The insurance policies have limits of $1,000,000 per claim/occurrence and $3,765,000 annual aggregate. Southwell Obligated Group is self-insured to cover the deductible portion of its general and professional insurance policy. Southwell Obligated Group's deductible is $50,000 for individual claims or $500,000/$150,000 (professional/general) annual aggregate. Southwell Obligated Group had professional insurance payable of $1,543,000 and $1,000,000 and professional insurance recoverable of $1,188,000 and $-0- at September 30, 2019 and 2018, respectively.

Employee health. Southwell Obligated Group has a self-insured health plan for its employees. Southwell Obligated Group has purchased stop loss insurance to supplement the health plan, which will reimburse Southwell Obligated Group for individual claims in excess of $150,000 annually. Southwell Obligated Group incurred expense related to this plan of approximately $28,382,000 and $31,372,000 in 2019 and 2018, respectively. Estimated accruals for claims incurred but not reported have been recorded in accrued expenses on the balance sheets. Estimated accruals were approximately $3,245,000 and $6,610,000 at September 30, 2019 and 2018, respectively.

Also, Southwell Obligated Group has entered into a loss financing agreement with other Georgia hospitals through a program developed by Georgia ADS, LLC. The program is designed to provide for the financing and payment of covered claims between $225,000 and $650,000. Commercial insurance has been obtained to provide coverage for claims exceeding $500,000. Estimated accruals for amounts owed to the program under the loss financing agreement have been recorded in accrued expenses on the balance sheets. Estimated accruals were approximately $288,000 and $17,000 at September 30, 2019 and 2018, respectively.

12. Functional Expenses

Southwell Obligated Group provides health care services to residents within its geographic location. Expenses related to providing these services in 2019 are as follows:

	Patient Care Services	General and Administrative	Total
Salaries and wages	$ 133,244,000	$ 34,486,000	$ 167,730,000
Employee benefits	34,387,000	8,887,000	43,274,000
Contract and purchased services	11,753,000	7,693,000	19,446,000
Physician services	12,496,000	1,536,000	14,032,000
Supplies and drugs	67,802,000	4,296,000	72,098,000
Depreciation	29,824,000	2,950,000	32,774,000
Goodwill amortization	2,517,000	-	2,517,000
Interest expense	4,193,000	-	4,193,000
Other expense	9,359,000	25,606,000	34,965,000
Total	$ 305,575,000	$ 85,454,000	$ 391,029,000

For 2018, Southwell has $291,048,000 of patient care services and $91,745,000 in general and administrative expenses.

Continued

12. Functional Expenses, Continued

The combined special-purpose financial statements report certain expense categories that are attributable to more than one health care service or support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Cost not directly attributable to a function is depreciation which is allocated to a function based on square footage. Employee benefits are allocated based on salaries and wages.

13. Fair Value of Financial Instruments

The following methods and assumptions were used by Southwell Obligated Group in estimating the fair value of its financial instruments:

- *Cash and cash equivalents, short-term investments, accounts payable, accrued expenses, and third-party payor settlements:* The carrying amount reported in the balance sheet approximate their fair value due to the short-term nature of these instruments.

- *Assets as limited as to use:* Amounts reported in the balance sheet are at fair value. See Note 5 for fair value measurement disclosures.

- *Long-term debt:* Fair value of Southwell Obligated Group's revenue anticipation certificates are based on quoted market prices and the carrying amounts for other long-term debt approximate their fair value.

	2019		2018	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt	$ 280,464,000	$ 280,832,000	$ 248,685,000	$ 247,240,000

Following is a description of the valuation methodologies used for assets at fair value. There have been no changes in the methodologies used at September 30, 2019 and 2018.

Money market funds and certificates of deposit: Valued at amortized cost, which approximates fair value.

U.S. Treasury obligations and U.S. Government agency obligations: Certain U.S. government securities are valued at the closing price reported in the active market in which the individual security is traded. Other U.S. government securities are valued based on yields currently available on comparable securities of issuers with similar credit ratings.

Corporate obligations: Certain corporate obligations are valued at the closing price reported in the active market in which the security is traded. Other corporate obligations are valued based on yields currently available on comparable securities of issuers with similar credit ratings. When quoted prices are not available for identical or similar securities, the security is valued under a discounted cash flows approach that maximizes observable inputs, such as current yields of similar instruments, but includes adjustments for certain risks that may not be observable, such as credit and liquidity risks.

Continued

13. Fair Value of Financial Instruments, Continued

Asset-backed securities: Asset-backed securities use valuation techniques that reflect market participants' assumptions and maximize the use of relevant observable inputs including quoted prices for similar assets, benchmark yield curves, and market corroborated inputs.

Marketable equity securities, non-U.S. equity mutual funds, commodity mutual funds, and other mutual funds: Certain equity securities and mutual funds are valued at the closing price reported on the active market on which the individual securities are traded. Other equity securities and mutual funds are valued based on quoted prices for similar investments in active or inactive markets or valued using observable market data.

14. Rural Hospital Tax Credit Contributions

The State of Georgia (State) passed legislation which will allow individuals or corporations to receive a State tax credit for making a contribution to certain qualified rural hospital organizations during calendar years 2017 through 2021. Southwell Obligated Group submitted the necessary documentation and was approved by the State to participate in the rural hospital tax credit program for calendar years 2017, 2018, and 2019. Contributions received under the program approximated $757,000 and $2,032,000 during fiscal years 2019 and 2018, respectively. Southwell Obligated Group will have to be approved by the State to participate in the program in each subsequent year.

15. Liquidity and Availability

Financial assets available for general expenditure within one year of September 30, 2019, consist of the following:

Cash and cash equivalents	$ 61,187,000
Short-term investments	5,259,000
Patient accounts receivable, net	56,667,000
Total	$ 123,113,000

Southwell Obligated Group has internally designated and held by trustee assets limited as to use, which are more fully described in Note 5, that are not available for expenditure within the next year and not reflected in the amounts above. However, the internally designated amounts could be made available if necessary.

As of September 30, 2019, Southwell Obligated Group was in compliance with loan covenants regarding days cash on hand.

16. Subsequent Events

On October 21, 2019, Southwell Ambulatory, Inc. (Ambulatory), a Georgia not-for-profit corporation, was created with Southwell as the sole member. On January 1, 2020, Ambulatory purchased Valdosta Endoscopy Center, LLC and Valdosta Gastroenterology Associates, LLC for approximately $1,895,000. Also on January 1, 2020, Ambulatory purchased Lowndes County Ambulatory Surgical Center, Inc. for approximately $1,856,000.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
Tift County Hospital Authority
Southwell, Inc.
Tift Regional Health System, Inc.
Tifton, Georgia

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the combined special-purpose financial statements of Southwell Obligated Group, which comprise the combined special-purpose balance sheet as of September 30, 2019, and the related combined special-purpose statements of operations and changes in net assets, and cash flows for the year then ended, and the related notes to the combined special-purpose financial statements, and have issued our report thereon dated February 27, 2020.

Internal Control over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Authority's financial statements will not be prevented, or detected and corrected on a timely basis.

Continued

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

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

Purpose of this Report

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

Draffin & Tucker, LLP

Atlanta, Georgia
February 27, 2020