KPMG

EASTERN VIRGINIA MEDICAL SCHOOL AND AFFILIATED ORGANIZATION

Consolidated Financial Statements

June 30, 2018

(With Independent Auditors' Reports Thereon)

EASTERN VIRGINIA MEDICAL SCHOOL
AND AFFILIATED ORGANIZATION

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KPMG LLP
Suite 1900
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Norfolk, VA 23510

Independent Auditors' Report

The Board of Visitors
Eastern Virginia Medical School:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Eastern Virginia Medical School and Affiliated Organization (EVMS), which comprise the consolidated balance sheet as of June 30, 2018, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit 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 audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Eastern Virginia Medical School and Affiliated Organization as of June 30, 2018, results of activities, and their cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.

Report on Summarized Comparative Information

We have previously audited EVMS' 2017 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated November 6, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2017 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 29, 2018 on our consideration of EVMS' 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 EVMS' 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 EVMS' internal control over financial reporting and compliance.

KPMG LLP

Norfolk, Virginia
October 29, 2018

EASTERN VIRGINIA MEDICAL SCHOOL
AND AFFILIATED ORGANIZATION

Consolidated Balance Sheet

June 30, 2018
(With summarized financial information as of June 30, 2017)

Assets	**2018**	**2017**
Current assets:		
Cash and cash equivalents (notes 3 and 7)	$ 43,444,317	29,090,910
Restricted cash and investments (notes 4 and 7)	7,027,241	5,508,453
Operating investments (notes 4 and 7)	16,577,386	23,172,252
Accounts receivable, net (notes 5 and 9)	23,611,418	24,602,458
Accounts receivable from affiliate (note 6)	771,962	1,634,597
Current portion of notes receivable from students	847,800	774,900
Prepaid expenses and other current assets	2,482,065	2,085,164
Total current assets	94,762,189	86,868,734
Property, plant, and equipment, net (note 8)	125,455,913	121,614,397
Other long-term assets:		
Operating investments (notes 4 and 7)	19,554,649	18,332,216
Notes receivable from students	4,373,064	5,448,703
Interest in net assets of affiliate (note 1)	76,328,078	68,704,398
Other long-term assets	3,790,349	3,664,605
Total other long-term assets	104,046,140	96,149,922
Total assets	$ 324,264,242	304,633,053
Liabilities and Net Assets		
Liabilities:		
Current liabilities:		
Current portion of long-term debt (note 10)	$ 4,500,000	4,010,000
Accounts payable – trade	8,890,151	7,713,577
Accrued compensation	5,445,571	7,203,795
Deferred income	5,826,240	4,836,653
Accrued expenses and other current liabilities	8,988,158	9,214,469
Total current liabilities	33,650,120	32,978,494
Long-term debt, excluding current portion and net of bond issuance costs (note 10)	33,536,921	39,246,542
Other long-term liabilities:		
Grant deposits (note 12)	2,633,439	3,359,522
Refundable federal student loans	4,417,445	5,599,771
Assets held for affiliate (note 13)	910,855	891,406
Other long-term liabilities	2,769,365	2,210,245
Total other long-term liabilities	10,731,104	12,060,944
Total liabilities	77,918,145	84,285,980
Net assets:		
Unrestricted:		
Operating	8,130,983	7,763,126
EVMS reserves	42,938,756	28,715,901
Department reserves	49,452,932	46,964,261
Net investment in plant	23,064,945	17,401,248
Parking facility reserves	163,210	75,493
Total unrestricted net assets	123,750,826	100,920,029
Temporarily restricted:		
Revolving student loans	1,715,685	1,722,041
Program restricted	686,970	2,370,442
Net investment in plant	43,864,538	46,630,163
Interest in net assets of affiliate (note 1)	76,328,078	68,704,398
Total temporarily restricted net assets	122,595,271	119,427,044
Total net assets	246,346,097	220,347,073
Commitments and contingencies (notes 9, 11, and 17)		
Total liabilities and net assets	$ 324,264,242	304,633,053

See accompanying notes to consolidated financial statements.

EASTERN VIRGINIA MEDICAL SCHOOL
AND AFFILIATED ORGANIZATION

Consolidated Statement of Activities

Year ended June 30, 2018
(With summarized financial information for the year ended June 30, 2017)

		Unrestricted net assets	Temporarily restricted net assets	Total	2017 total
Operating revenues and support:					
Tuition and fees, net	$	44,317,668	—	44,317,668	41,511,122
State appropriations (note 14)		25,787,561	—	25,787,561	24,976,933
Municipal subsidies		1,382,004	—	1,382,004	1,372,944
Federal grants and contracts		24,872,597	—	24,872,597	24,772,208
State grants and contracts		1,069,240	—	1,069,240	990,446
Private grants, contracts, and gifts		3,674,473	—	3,674,473	3,887,336
EVMS Foundation endowment income and gifts		6,581,038	—	6,581,038	5,753,144
Patient care services, net		55,749,885	—	55,749,885	57,059,568
Contractual services of graduate school residents		36,220,301	—	36,220,301	34,903,901
Contractual services		35,379,068	—	35,379,068	22,938,074
Sales and services of auxiliary enterprises		6,737,470	—	6,737,470	6,303,650
Other sources		11,997,435	(118,675)	11,878,760	22,564,698
Interest and investment income		1,242,782	13,930	1,256,712	834,404
Released from restriction		5,196,930	(4,350,708)	846,222	—
Total operating revenues and support		260,208,452	(4,455,453)	255,752,999	247,868,428
Operating expenses (notes 11, 15, and 16):					
Program services:					
Undergraduate instruction		52,096,734	—	52,096,734	47,116,813
Graduate instruction		28,233,863	—	28,233,863	27,987,948
Research		27,306,656	—	27,306,656	32,826,399
Patient services		69,033,816	—	69,033,816	69,575,025
Total program services		176,671,069	—	176,671,069	177,506,185
Management and general:					
Academic support		8,810,018	—	8,810,018	7,486,028
Institutional support		20,250,138	—	20,250,138	18,660,201
Auxiliary services		23,946,062	—	23,946,062	22,857,049
Patient services support		7,926,780	—	7,926,780	7,097,082
Total management and general		60,932,998	—	60,932,998	56,100,360
Total operating expenses		237,604,067	—	237,604,067	233,606,545
Changes in net assets from operations		22,604,385	(4,455,453)	18,148,932	14,261,883
Nonoperating items:					
Unrealized gains (losses) from investments, net		(919,578)	—	(919,578)	771,561
Change in interest of net assets of affiliate (note 1)		—	7,623,680	7,623,680	6,900,019
Change in fair value of interest rate swaps (note 10)		1,145,990	—	1,145,990	1,978,826
Changes in net assets		22,830,797	3,168,227	25,999,024	23,912,289
Net assets at beginning of year		100,920,029	119,427,044	220,347,073	196,434,784
Net assets at end of year	$	123,750,826	122,595,271	246,346,097	220,347,073

See accompanying notes to consolidated financial statements.

EASTERN VIRGINIA MEDICAL SCHOOL
AND AFFILIATED ORGANIZATION

Consolidated Statement of Cash Flows

Year ended June 30, 2018
(With summarized financial information for the year ended June 30, 2017)

		2018	2017
Cash flows from operating activities:			
Changes in net assets	$	25,999,024	23,912,289
Adjustments to reconcile changes in net assets to net cash provided by operating activities:			
Depreciation and amortization		10,248,539	10,336,371
Change in fair value of interest rate swaps (note 10)		(1,145,990)	(1,978,826)
Net realized and unrealized (gains) losses on investments		786,056	(771,561)
Gain on patent licensing agreement		—	(4,891,023)
Change in interest of net assets of affiliate (note 1)		(7,623,680)	(6,900,019)
Net (gain) loss on sale of property, plant, and equipment		(230,211)	41,262
Provision for bad debts		14,221,057	12,178,164
Amortization of bond issuance costs		26,369	26,377
State appropriation for property, plant, and equipment (note 14)		(1,369,021)	(729,607)
Changes in:			
Accounts receivable		(13,089,928)	(11,935,790)
Accounts receivable from affiliate		862,635	(1,295,831)
Prepaid expenses and other current assets		(396,901)	980,747
Other long-term assets		(2,396)	(2,404)
Accounts payable – trade		1,176,574	1,794,756
Accrued compensation		(1,758,224)	(1,836,364)
Deferred income		989,587	(695,062)
Accrued expenses and other current liabilities		(226,311)	(6,221,813)
Grant deposits		(726,083)	505,578
Assets held for affiliate		19,449	18,701
Other long-term liabilities		559,120	741,234
Net cash provided by operating activities		28,319,665	13,277,179
Cash flows from investing activities:			
Purchases of restricted cash and investments		(7,846,004)	(9,719,671)
Proceeds from restricted cash and investments		6,327,216	9,121,066
Purchases of operating investments		(1,125,678)	(552,559)
Proceeds from sales and maturities of operating investments		5,712,055	104,004
Purchases of property, plant, and equipment		(14,239,649)	(5,601,770)
Proceeds from sale of property, plant, and equipment		379,805	—
Disbursements for notes receivable from students		(310,600)	(698,111)
Collections of notes receivable from students		1,173,250	1,083,624
Change in cash surrender value of life insurance		(123,348)	(112,366)
Net cash used in investing activities		(10,052,953)	(6,375,783)
Cash flows from financing activities:			
State appropriation for property, plant, and equipment (note 14)		1,369,021	729,607
Principal payments on bonds		(4,100,000)	(4,130,000)
Refundable federal student loans		(1,182,326)	(133,271)
Net cash used in financing activities		(3,913,305)	(3,533,664)
Net increase in cash and cash equivalents		14,353,407	3,367,732
Cash and cash equivalents at beginning of year		29,090,910	25,723,178
Cash and cash equivalents at end of year	$	43,444,317	29,090,910
Supplemental disclosures of cash flow information:			
Cash paid for interest, net of amounts capitalized	$	1,325,134	1,528,810
Purchases of property, plant, and equipment included in accounts payable – trade		589,914	600,417

See accompanying notes to consolidated financial statements.

(1) EVMS and Affiliated Organization

The Eastern Virginia Medical School (EVMS or the School) was created in 1964 by enabling legislation of the General Assembly of Virginia to identify, document, and evaluate needs, problems, and resources relating to health and medical care within its service area and to plan, develop, and implement programs to meet such needs on both an immediate and long-range basis. EVMS may plan, design, construct, remove, enlarge, equip, maintain, and operate medical educational institutions and medical and paramedical facilities, together with related and supporting facilities, and do all things necessary and convenient to carry out any of its purposes. EVMS' powers also include the right of eminent domain within the City of Norfolk and the authorization to borrow funds and issue bonds. EVMS has been classified as an organization described in Section 501(c)(3) of the Internal Revenue Code (IRC). As such, EVMS is exempt from federal and state income taxation, and contributions to it are tax deductible.

EVMS Medical Group (EVMS MG) is a nonmember organization incorporated under the Virginia Non Stock Corporation Act. Prior to July 1, 1989, EVMS MG was an operating division of EVMS. Effective July 1, 1989, EVMS MG began operations as a not-for-profit foundation through the approval of EVMS MG's Articles of Incorporation and Bylaws by the EVMS Board of Visitors. EVMS MG bylaws cannot be altered or amended without the approval of the EVMS Board of Visitors. EVMS MG has been classified as an organization described in Section 501(c)(3) of the IRC and is exempt from federal and state income taxation. The accounts of EVMS MG are included in the accompanying consolidated financial statements.

The Eastern Virginia Medical School Foundation (EVMS Foundation) is a nonprofit organization established to provide financial support to EVMS. The EVMS Foundation qualifies as a charitable foundation and is exempt from federal and state income taxation under Section 501(c)(3) of the IRC. As such, contributions to it are tax deductible. The accounts of EVMS Foundation are not included in the consolidated financial statements of EVMS. Amounts received from the EVMS Foundation are reported as endowment income in EVMS' consolidated financial statements. EVMS' beneficial interest in the net assets of EVMS Foundation related to estimated future distributions totaling $76,328,078 and $68,704,398 as of June 30, 2018 and 2017, respectively, is presented as interest in net assets of affiliate and temporarily restricted net assets. Changes in the interest of the net assets of EVMS Foundation are included in nonoperating items on the accompanying consolidated statement of activities. During the years ended December 31, 2018 and 2017, income from the EVMS Foundation of $6,581,038 and $5,753,144, respectively, is presented in operating revenues and support on the accompanying consolidated statement of activities.

EVMS has defined its mission as a community-based academic institution dedicated to medical and health education, research, and patient care.

(a) Education

Undergraduate Education – Opened in 1973, EVMS offers a Doctor of Medicine (M.D.) degree. In 2004, the Association of American Medical Colleges' Liaison Committee on Medical Education awarded EVMS continued full accreditation of the educational program leading to the M.D. degree.

In 2009, the Southern Association of Colleges and Schools awarded EVMS a continuation of accreditation for a 10-year period.

EVMS also offers several health professions programs, including master's degrees in art therapy, public health, physician assistant, clinical embryology, surgical assistant, biotechnology and biomedical sciences, and doctoral degrees in clinical psychology and biomedical sciences in conjunction with other local universities.

Graduate Medical Education (GME) – Founded in 1974, GME offers residency and fellowship programs at numerous healthcare facilities in EVMS' service area. Programs are accredited by the Accreditation Council of Graduate Medical Education or the American Psychological Association or are approved by specialty boards.

(b) Research

EVMS conducts numerous research projects in various areas including proteomics, cancer, reproductive medicine, systemic diseases and infectious diseases. EVMS-sponsored research is supported by various federal and state agencies, pharmaceutical companies, and private foundations.

(c) Patient Care

Clinical care is provided through the following affiliates:

EVMS MG – EVMS MG was formed exclusively for charitable, scientific, and educational purposes and to further the mission and goals of EVMS. EVMS MG is organized and shall at all times operate to fulfill its corporate purpose by supporting clinical practice and research in conjunction with providing faculty the opportunity to teach in a physician group practice setting within the academic environment of EVMS. EVMS MG also provides education and training to EVMS students and residents. EVMS MG incorporates the professional practice units of the EVMS faculty in all departments except pediatrics. The practice units are staffed solely by faculty members of EVMS who provide professional patient care at EVMS facilities or through agreements with other area hospitals.

EVMS Pediatrics, formerly Pediatric Faculty Associates, Inc. (PFA) – PFA was established through an affiliation agreement between EVMS, Children's Hospital of the King's Daughters (CHKD), and Children's Health System, Inc. During fiscal year 1998, PFA underwent significant organizational and structural changes. A majority of the full-time faculty members in the pediatric specialties established a for-profit professional limited liability company, Children's Specialty Group, PLLC (CSG). On June 30, 2008, the PFA corporate status was dissolved. All assets and liabilities were transferred to EVMS and reported as EVMS Pediatrics.

EVMS Pediatrics, along with CSG, incorporates the professional practice units of the EVMS faculty in the pediatric specialties. They provide professional patient care at EVMS or CHKD facilities or through agreements with other area hospitals.

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(2) Summary of Significant Accounting Policies

(a) Basis of Presentation and Consolidation

EVMS' consolidated financial statements have been prepared on the accrual basis of accounting. All significant intercompany balances and transactions have been eliminated in consolidation. These consolidated financial statements have been prepared to focus on EVMS as a whole and to present balances and transactions according to the existence or absence of donor-imposed restrictions. Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions and are segregated into three net asset groups as follows:

Unrestricted net assets – Net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that may or will be met by actions of EVMS and/or the passage of time.

Permanently restricted net assets – Net assets subject to donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of EVMS. There were no permanently restricted net assets at EVMS as of June 30, 2018 or 2017.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted or temporarily restricted net assets. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications from temporarily restricted net assets to unrestricted net assets.

The consolidated financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. generally accepted accounting principles (GAAP). Accordingly, such information should be read in conjunction with EVMS' consolidated financial statements as of and for the year ended June 30, 2017, from which the summarized information was derived. In addition, certain reclassifications have been made to the prior year amounts in order to conform to the current year presentation.

(b) Cash and Cash Equivalents

EVMS considers all highly liquid investments with original maturities of three months or less when purchased to be cash equivalents for consolidated financial statement presentation, except for those short-term investments managed by EVMS' investment managers as part of their long-term investment portfolio. Cash equivalents consist primarily of temporary investments in bank repurchase agreements, money market funds, and cash reserve funds. Cash equivalents make up substantially all of the balance in cash and cash equivalents on the consolidated balance sheet as of June 30, 2018 and 2017.

(c) Restricted Cash and Investments

Restricted cash and investments represents funds that have been externally restricted or internally designated by management for a specific purpose and are reported on the consolidated balance sheet at fair value.

(d) Investments

Investments are classified as trading and are reported on the consolidated balance sheet at fair value. Net realized gains and losses on investments are reflected in operating revenues and support in the accompanying consolidated statement of activities. Net unrealized gains and losses on investments are reflected in nonoperating items in the accompanying consolidated statement of activities. The current year gains and losses on investments have been recognized in the accompanying consolidated statement of activities as increases or decreases in unrestricted net assets, unless their use is restricted by explicit donor stipulations.

(e) Patient Accounts Receivable

Patient receivables are recorded net of allowances for contractual adjustments and uncollectible receivables. The allowance for doubtful accounts is EVMS MG's best estimate of the amount of probable credit losses in its existing receivables. EVMS MG determines the allowance based on historical write-off experience. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. EVMS MG does not have any off-balance-sheet credit exposure related to its customers. Patient service revenue is presented net of contractual allowances and discounts and the provision for bad debts.

(f) Property, Plant, and Equipment

Property, plant, and equipment are stated at cost or at estimated fair value at date of gift if acquired by gift. Depreciation is computed using the straight-line method over the estimated useful lives of the property, plant, and equipment.

The estimated useful lives are as follows:

Land improvements	5–20 years
Buildings and improvements	5–40 years
Equipment	3–20 years

(g) Other Long-Term Assets

Other long-term assets in the accompanying consolidated balance sheet are primarily comprised of cash surrender value of life insurance policies held by EVMS MG.

EVMS MG is the owner of two insurance policies for current and retired faculty of EVMS, where EVMS MG is the beneficiary. These policies are recorded at their net cash surrender values, as reported by the issuing insurance company, whose Standard & Poor's financial strength rating is AA+. The net cash surrender values totaled $3,663,691 and $3,540,343 as of June 30, 2018 and 2017, respectively.

The cash surrender value of life insurance is valued under Level 2 of the fair value hierarchy at June 30, 2018 and 2017. The cash surrender value of life insurance was determined by the underwriting insurance company's valuation models, which take into account the passage of time, mortality tables, interest rates, cash values for paid-up additions, and dividend accumulations. The cash surrender value represents the guaranteed value EVMS MG would receive upon surrender of these policies held on key employees as of June 30, 2018.

(h) Refundable Federal Student Loans

Funds provided by the U.S. government under the Federal Perkins and Health Professions Student Loan Programs are loaned to qualified students and may be reloaned after collections. These funds are ultimately refundable to the government and are reported as liabilities in the accompanying consolidated balance sheet. Due to the dissolution of the Perkins Loan program, no new Perkins Loans were disbursed during the year ended June 30, 2018.

(i) Tuition and Fees

Student tuition and fees are recorded as revenue during the year that the related academic services are rendered. Student tuition and fees received in advance of services to be rendered are recorded as deferred income.

(j) Patient Care Services

EVMS MG has agreements with third-party payers that provide for payments to EVMS MG at amounts different from its established rates. Payment arrangements include prospectively determines rates, reimbursement costs, discounted charges, and per diem payments. Patient care services revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered. Reimbursements from third-party payers are subject to examination by the agencies administering the programs from compliance with procedures and documentation standards.

(k) Charity Care

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

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(l) Sponsored Grants and Contracts

Revenues under grants, contracts, and similar agreements with sponsoring organizations are recognized as expenses are incurred for agreement purposes. The revenues include recoveries of indirect costs and fringe benefits, which are generally determined as a negotiated or agreed-upon percentage of direct costs with certain exclusions.

(m) Donated Services

A number of volunteers have made contributions of time to the School's program and support functions. The value of this contributed time does not meet the accounting criteria for recognition of contributed services and, accordingly, is not reflected in the accompanying consolidated financial statements.

(n) Functional Expenses

EVMS allocates its expenses on a functional basis among its various programs and supporting services. Expenses that can be identified with a specific program or supporting service are allocated directly. Other expenses that are common to several functions are allocated on various statistical bases.

(o) Derivative Instruments

EVMS utilizes derivative financial instruments to reduce its exposure to cash flow risks from changes in interest rates, specifically, variable interest rates. EVMS is exposed to credit losses in the event of nonperformance by the counterparty to the interest rate swap; however, the counterparty is a major financial institution, and the risk of loss due to nonperformance is considered remote. Interest rate differentials paid or received on the swap are recognized as adjustments to expense in the period earned or incurred. Interest rate swaps are recorded at fair value and reflected as assets or liabilities in the accompanying consolidated balance sheet. Changes in the fair value of interest rate swaps are reflected as nonoperating items in the accompanying consolidated statement of activities.

(p) Concentration of Credit Risk

Financial instruments, which potentially subject EVMS and its affiliated organization to concentration of credit risk, consist principally of cash, investments, patient receivables, and student notes receivable.

EVMS and its affiliated organization place unrestricted cash and temporary overnight investments with high credit quality financial institutions. EVMS and the EVMS Foundation's endowment assets are allocated between several established, reputable asset management firms and, according to their investment policy, are invested in investment-grade instruments. The asset management firms are independent of the funds' trustees, who review their performance on a periodic basis.

(q) Long-Lived Assets

Long-lived assets, such as property, plant, and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require a long-lived asset or asset group to be tested for possible impairment, EVMS first compares undiscounted cash flows expected to be generated by that asset or asset group to its carrying amount. If the carrying amount of the long-lived asset or asset group is not recoverable on an undiscounted cash flow basis, an impairment is recognized to the extent that the carrying amount exceeds its fair value. Fair value is determined through various valuation techniques including discounted cash flow models, quoted market values, and third-party independent appraisals, as considered necessary. There was no impairment recorded in fiscal years 2018 or 2017.

(r) Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP 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 consolidated financial statements and reported amount 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 useful life of fixed assets, allowance for doubtful accounts, the valuation of derivatives, and investments.

(s) Income Taxes

EVMS is exempt from income taxes under Section 501(a) of the IRC as an organization described in Section 501(c) (3). Accordingly, no provision for income taxes is made in the consolidated financial statements. As of June 30, 2018 and 2017, there were no uncertain tax positions.

(t) Release from Restriction

EVMS received temporarily restricted revenue from the Commonwealth of Virginia to fund the construction and purchase of certain real property during the years ended June 30, 2009–2018. As a part of the agreement, EVMS was required to fund a percentage of the cost of the project. EVMS' share of the cost was funded through fund-raising and the issuance of long-term debt. The restriction on the funds received from the Commonwealth of Virginia is being released over the life of the debt EVMS issued to fund the project.

(u) Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance, and requires significantly expanded disclosures about revenue recognition. The core principle of the revenue model is than 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. The standard is effective for EVMS as of July 1,

(Continued)

2019. Early adoption is permitted. EVMS is currently evaluating the impact on the consolidated financial statements and the options of adopting using either the retrospective or cumulative effect transition method.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, intended to improve financial reporting about leasing transactions. The new lease standard requires lessees to put most leases on their balance sheets but recognize expenses on their income statements in a manner similar to today's accounting. The guidance also eliminates today's real-estate specific provisions and changes the sale and leaseback accounting model for all entities. For lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. The standard is effective for EVMS as of July 1, 2020. Early adoption is permitted. EVMS is currently evaluating the impact of adoption of the new lease standard on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The ASU reduces the number of net asset classes presented from three to two: with donor restrictions and without donor restrictions; requires all not-for-profit entities (NFPs) to present expenses by their functional and natural classifications in one location in the financial statements; and requires NFPs to provide quantitative and qualitative information about management of liquid resources and availability of financial assets to meet cash needs within one year of the balance sheet date. The standard is effective for EVMS as of July 1, 2018. EVMS is currently evaluating the impact of adoption on the consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which clarifies whether an entity should account for a grant, or similar transaction, as a contribution or as an exchange transaction. The standard is effective for EVMS as of July 1, 2019. Early adoption is permitted. EVMS is currently evaluating the impact of adoption on the consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*, which eliminates, amends, and adds disclosure requirements for fair value measurements. The standard is effective for EVMS as of July 1, 2020. Early adoption is permitted. EVMS is currently evaluating the impact of adoption on the consolidated financial statements.

(v) Subsequent Events

EVMS has evaluated subsequent events from the consolidated balance sheet date through October 29, 2018, the date at which the consolidated financial statements were available to be issued, and determined there are no items to disclose.

(3) Cash and Cash Equivalents

Cash and cash equivalents at June 30, 2018 and 2017 are summarized as follows:

		2018	2017
EVMS	$	42,688,617	26,525,692
EVMS MG		755,700	2,565,218
	$	43,444,317	29,090,910

(4) Operating Investments and Restricted Cash

(a) Operating investments at June 30, 2018 and 2017 were comprised of the following:

		2018	2017
Money market funds	$	734,498	1,995,050
Equity securities		491,157	1,251,920
Certificates of deposit		4,513,081	5,382,668
Mutual fund – fixed income		4,121,280	4,088,945
Corporate debt		10,384,302	7,618,367
Asset-backed securities		346,717	2,594,274
U.S. government securities		14,295,432	13,496,693
Equity method investment		133,527	—
Cash reserve fund		1,112,041	5,076,551
Total operating investments		36,132,035	41,504,468
Less amounts available for current obligations		(16,577,386)	(23,172,252)
Long-term operating investments	$	19,554,649	18,332,216

(b) Restricted cash and investments at June 30, 2017 and 2016 were comprised of the following:

		2018	2017
Restricted for parking garage operations – cash	$	675,772	615,881
Restricted for student loans – money market funds		2,895,847	2,013,525
Restricted for cash pension fund – mutual funds – large cap		725,060	445,640
Restricted for interest, debt retirement, and construction per trust indentures:			
General Revenue Refunding Bonds, Series 2001:			
Interest fund – money market funds		13,938	8,973
Principal fund – money market funds		702,741	1,205,288
Total Bonds, Series 2001		716,679	1,214,261
General Revenue Refunding Bonds, Series 2002:			
Interest fund – money market funds		4,936	4,325
Principal fund – money market funds		377,649	429,001
Total Bonds, Series 2002		382,585	433,326
General Revenue Bonds, Series 2006:			
Interest fund – money market funds		15,897	17,015
Principal fund – money market funds		278,097	268,490
Total Bonds, Series 2006		293,994	285,505
General Revenue Refunding Bonds, Series 2010:			
Interest fund – money market funds		26,113	25,189
Principal fund – money market funds		251,520	233,405
Total Bonds, Series 2010		277,633	258,594
General Revenue Bonds, Series 2010:			
Capitalized interest fund – money market funds		11	4,577
Interest fund – money market funds		19,865	14,996
Principal fund – money market funds		730,981	145,888
Total Bonds, Series 2010		750,857	165,461
General Revenue Bonds, Series 2011:			
Interest fund – money market funds		17,420	17,833
Principal fund – money market funds		292,393	58,351

	2018	2017
Capitalized interest fund – money market funds	$ 1	76
Total Bonds, Series 2011	309,814	76,260
Total restricted for interest, debt retirement, and construction per trust indentures	2,731,562	2,433,407
Total restricted cash and investments	$ 7,028,241	5,508,453

(5) Accounts Receivable

At June 30, 2018 and 2017, accounts receivable were comprised of the following:

	2018	2017
Gross patient accounts receivable	$ 22,059,942	19,185,023
Less contractual allowances	(6,504,146)	(5,134,186)
Less allowance for doubtful accounts	(5,618,249)	(4,827,053)
Patient accounts receivable, net	9,937,547	9,223,784
Sponsored programs receivables:		
Grants and contracts – federal	7,011,521	5,937,559
Grants and contracts – private	488,052	773,714
Grants and contracts – state	269,065	182,700
Total sponsored programs receivables	7,768,638	6,893,973
Local hospitals, net	3,252,807	2,729,190
Parking	99,205	87,147
U.S. Department of Education	1,002,587	4,397,022
Tuition receivable, net	818,194	520,681
Other, net	732,440	750,661
Total accounts receivable, net	$ 23,611,418	24,602,458

(Continued)

The activity in the patient allowance for doubtful accounts is summarized as follows for the years ended June 30:

		2018	2017
Beginning balance as of July 1	$	4,827,053	4,844,368
Provision for bad debts, net of recoveries		14,080,968	12,475,364
Less write-offs		(13,289,772)	(12,492,679)
Ending balance as of June 30	$	5,618,249	4,827,053

(6) Accounts Receivable from Affiliate

At June 30, 2018 and 2017, accounts receivable from affiliate were due from the EVMS Foundation in the amount of $771,962 and $1,634,597, respectively. This receivable is secured by the EVMS Foundation's investments.

(7) Fair Value Measurements

EVMS uses valuation approaches that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. EVMS determines fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to the reporting entity at the measurement date
- Level 2 Inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability
- Level 3 Inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date.

The following tables present assets and liabilities that are measured at fair value on a recurring basis at June 30, 2018 and 2017:

	Total as of June 30, 2018	Level 1	Level 2	Level 3
Assets:				
Cash and cash equivalents	$ 51,593,037	51,593,037	—	—
Mutual funds – fixed income	4,121,280	4,121,280	—	—
Mutual funds – large cap	725,060	725,060	—	—
Equity securities	491,157	491,157	—	—
U.S. government securities	14,295,432	—	14,295,432	—
Corporate debt	10,384,302	—	10,384,302	—
Asset-backed securities	346,717	—	346,717	—
Certificates of deposit	4,513,081	—	4,513,081	—
Beneficial interest in net assets of affiliate	76,328,078	—	—	76,328,078
Total	$ 162,798,144	56,930,534	29,539,532	76,328,078
Liability:				
Interest rate swaps	$ (363,991)	—	(363,991)	—

	Total as of June 30, 2017	Level 1	Level 2	Level 3
Assets:				
Cash and cash equivalents	$ 41,225,324	41,225,324	—	—
Mutual funds – fixed income	4,088,945	4,088,945	—	—
Mutual funds – large cap	445,640	445,640	—	—
Equity securities	1,251,920	1,251,920	—	—
U.S. government securities	13,496,693	—	13,496,693	—
Corporate debt	7,618,367	—	7,618,367	—
Asset-backed securities	2,594,274	—	2,594,274	—
Certificates of deposit	5,382,668	—	5,382,668	—
Beneficial interest in net assets of affiliate	68,704,398	—	—	68,704,398
Total	$ 144,808,229	47,011,829	29,092,002	68,704,398
Liability:				
Interest rate swaps	$ (1,509,981)	—	(1,509,981)	—

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

- Cash and cash equivalents: Consist of repurchase agreements, cash reserve funds, and short-term money market funds, which are valued at $1 per share, which is the price the shares trade at in an active market
- Mutual funds: Valued at the daily quoted net asset value of shares held, which is based on the quoted market prices of the underlying assets of the funds
- Equity securities: Valued using quoted prices from the exchanges upon which the securities actively trade
- U.S. government securities, corporate debt, asset-backed securities, and certificates of deposit: Valued based upon proprietary valuation models that may consider market characteristics, such as benchmark yield curves, option-adjusted spreads, credit spreads, estimated default rates, coupon rates, anticipated timing of principal repayments, underlying collateral, and other security features in order to estimate relevant cash flows, which are discounted to fair value.
- Beneficial interest in net assets of affiliate: Valued at the net present value of future benefits using an income approach through discounted cash flows.
- Interest rate swaps (note 10): The fair value of the interest rate swaps is determined using pricing models that consider assumptions including time value, interest rates, and yield curves, as well as other relevant economic measures.

EVMS' accounting policy is to recognize transfers between levels of the fair value hierarchy on the date of the event or change in circumstances that caused the transfer. There were no transfers into or out of Level 1, Level 2, or Level 3 for the years ended June 30, 2018 and 2017.

(8) Property, Plant, and Equipment

At June 30, 2018 and 2017, property, plant, and equipment consisted of the following:

		2018	2017
Land	$	2,992,314	2,992,315
Land improvements		9,320,940	9,260,954
Buildings and improvements		187,480,589	186,064,823
Equipment		75,299,117	70,374,132
Construction in progress		9,834,563	3,109,928
		284,927,523	271,802,152
Less accumulated depreciation and amortization		(159,471,610)	(150,187,755)
Total property, plant, and equipment, net	$	125,455,913	121,614,397

Depreciation and amortization expenses related to property, plant, and equipment for the years ended June 30, 2018 and 2017 were $10,248,539 and $10,336,371, respectively.

(9) Lines of Credit

EVMS has a $10,000,000 unsecured line-of-credit facility with a bank. Under the terms of the agreement, interest is payable at one-month London Interbank Offered Rate (LIBOR) plus 1.50% (3.57% at June 30, 2018). The line of credit was not utilized during the year ended June 30, 2018 and expires on January 9, 2020.

EVMS MG has a $3,000,000 line-of-credit facility with a bank, which is subject to semi-annual review and expires on May 30, 2019. This facility is collateralized by certain accounts receivable. Interest is payable at the 30-day LIBOR plus 1.50% (3.57% at June 30, 2018). No amounts were outstanding under the line of credit at June 30, 2018 or 2017.

(10) Long-Term Debt

At June 30, 2018 and 2017, long-term debt consisted of bonds payable and related interest rate swap agreements as follows:

	2018	2017	
Bonds (property and equipment fund):			
General Revenue Refunding Bonds, Series 2001	$ 1,200,000	3,265,000	(A)
General Revenue Refunding Bonds, Series 2002	645,000	1,380,000	(B)
General Revenue Bonds, Series 2006	6,450,000	6,910,000	(C)
General Revenue Bonds, Series 2010	12,000,000	12,340,000	(D)
General Revenue Refunding Bonds, Series 2010	8,855,000	9,255,000	(E)
General Revenue Bonds, Series 2011	8,800,000	8,900,000	(F)
	37,950,000	42,050,000	
Interest rate swaps	363,991	1,509,981	(G)
Less bond issuance costs	(277,070)	(303,439)	(H)
Less current portion	(4,500,000)	(4,010,000)	
Noncurrent portion	$ 33,536,921	39,246,542	

(A) On December 5, 2001, EVMS refunded $9,735,000 of the Series 1991A Bonds by issuing the Series 2001 General Revenue Refunding Bonds. The Series 2001 Bonds are secured by a Master Indenture of Trust dated November 15, 1991 between EVMS and U.S. Bank, as trustee, as amended, and supplemented by a Sixth Supplemental Indenture of Trust dated November 15, 2001. The Series 2001 Bonds, maturing on November 18, 2018, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on November 15, 2008 and each November 15 thereafter through 2018. In addition, the bonds are also subject to optional redemption, as described in the Indentures of Trust mentioned above.

Interest is payable semi-annually at a floating rate per annum equal to 64% of 30-day LIBOR plus 50 basis points (1.82% and 1.25% as of June 30, 2018 and 2017, respectively) on each November 15 and May 15, and the entire principal balance is due on November 15, 2018. Mandatory sinking fund payments will be due annually on November 15 as follows:

Fiscal year maturities	Principal amount
2019	$ 1,200,000

(B) On January 15, 2002, EVMS refunded $4,620,000 of the Series 1991A Bonds by issuing the Series 2002 General Revenue Refunding Bonds. The Series 2002 Bonds are secured by a Master Indenture of Trust dated November 15, 1991 between EVMS and U.S. Bank, as trustee, as amended, and supplemented by a Seventh Supplemental Indenture of Trust dated January 15, 2002. The Series 2002 Bonds, maturing on November 18, 2018, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on November 15, 2003 and each November 15 thereafter through 2018. In addition, the bonds are also subject to optional redemption, as described in the Indentures of Trust mentioned above.

Interest is payable semi-annually at a floating rate per annum equal to 64% of 30-day LIBOR plus 50 basis points (1.82% and 1.25% as of June 30, 2018 and 2017, respectively) on each November 15 and May 15, and the entire principal balance is due on November 15, 2018. Mandatory sinking fund payments will be due annually on November 15 as follows:

Fiscal year maturities	Principal amount
2019	$ 645,000

(C) On June 15, 2006, EVMS issued the Series 2006 General Revenue Bonds. The Series 2006 Bonds are secured by a Master Indenture of Trust dated November 15, 1991 between EVMS and U.S. Bank, as trustee, as amended, and supplemented by an Eighth Supplemental Indenture of Trust dated June 1, 2006. The Series 2006 Bonds, maturing on November 15, 2028, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on November 15, 2009 and each November 15 thereafter through 2028. In addition, the bonds are also subject to optional redemption, as described in the Indentures of Trust mentioned above.

On October 17, 2011, EVMS modified the Series 2006 General Revenue Bonds, in accordance with the Twelfth Supplemental Indenture of Trust, effective November 1, 2011, to reduce the current interest rate payable from 4.00% per annum to 2.95% per annum until the rate reset date, which was also adjusted from June 15, 2021 to November 15, 2021.

Interest is payable semi-annually on each May 15 and November 15 at a rate of 2.95% per annum until the reset date of November 15, 2021. Effective November 15, 2021, the interest rate per annum will reset based on the 10-year average of the 7-year U.S. Treasury bond plus 30 basis points. The entire principal balance is due on November 15, 2028. Mandatory sinking fund payments will be due annually on November 15 as follows:

Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount
2019	$ 475,000	2023	$ 560,000	2027	$ 650,000
2020	500,000	2024	580,000	2028	680,000
2021	520,000	2025	605,000	2029	710,000
2022	540,000	2026	630,000		

(D) On October 29, 2010, EVMS issued the Series 2010A and Series 2010B General Revenue Bonds. The Series 2010 Bonds are secured by a Master Indenture of Trust dated November 15, 1991 between EVMS and U.S. Bank, as trustee, as amended, and supplemented by a Tenth Supplemental Indenture of Trust dated October 1, 2010. The Series 2010A Bonds, maturing on November 15, 2027, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on May 15, 2011 and each May 15 and November 15 thereafter through 2027. The Series 2010B Bonds, maturing on November 15, 2032, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on May 15, 2011 and each May 15 and November 15 thereafter through 2032. In addition, the bonds are also subject to optional redemption, as described in the Indentures of Trust mentioned above.

Interest is payable semi-annually at a floating rate per annum equal to 67% of 30-day LIBOR plus 184 basis points (3.23% and 2.62% as of June 30, 2018 and 2017, respectively) on each November 15 and May 15, and the entire principal balance is due on November 15, 2032.

EVMS made early redemption payments of $90,000 and $310,000 on the Series 2010B Bonds during the years ended June 30, 2018 and 2017, respectively, reducing the total principal of the Series 2010A and 2010B Bonds to $12,000,000 as of June 30, 2018. Mandatory sinking fund payments will be due annually on November 15 as follows:

Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount
2019	$ 1,250,000	2025	$ 1,250,000
2020	1,250,000	2026	1,250,000
2021	1,250,000	2027	1,250,000
2022	1,250,000	2028	750,000
2023	1,250,000		
2024	1,250,000		

(E) On November 15, 2010, EVMS refunded $10,000,000 of the Series 2008 Bonds by issuing the Series 2010 General Revenue Refunding Bonds. The Series 2010 Bonds are secured by a Master Indenture of Trust dated November 15, 1991 between EVMS and U.S. Bank, as trustee, as amended, and supplemented by an Eleventh Supplemental Indenture of Trust dated November 1, 2010. The Series 2010 Bonds, maturing on November 15, 2032, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on May 15, 2011 and each May 15 and November 15 thereafter through 2032. In addition, the bonds are also subject to optional redemption, as described in the Indentures of Trust mentioned above.

Interest is payable semi-annually at a floating rate per annum equal to 67% of 30-day LIBOR plus 169 basis points (3.08% and 2.47% as of June 30, 2018 and 2017, respectively) on each November 15 and May 15, and the entire principal balance is due on November 15, 2032. Mandatory sinking fund payments will be due annually on November 15 as follows:

Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount
2019	$ 430,000	2025	$ 555,000	2031	$ 720,000
2020	445,000	2026	580,000	2032	755,000
2021	465,000	2027	605,000	2033	785,000
2022	490,000	2028	635,000		
2023	510,000	2029	660,000		
2024	530,000	2030	690,000		

(F) On November 17, 2011, EVMS issued the Series 2011 General Revenue Bonds. The Series 2011 Bonds are secured by a Master Indenture of Trust dated November 15, 1991 between EVMS and U.S. Bank, as trustee, as amended, and supplemented by a Thirteenth Supplemental Indenture of

Trust dated November 1, 2011. The Series 2011 Bonds, maturing on November 15, 2032, are subject to mandatory sinking fund redemption by lot at a redemption price of 100% of the principal amount redeemed plus accrued interest on May 15, 2012 and each May 15 and November 15 thereafter through 2032.

Interest is payable semi-annually at a floating rate per annum equal to 65% of 30-day LIBOR plus 170 basis points (3.04% and 2.46% as of June 30, 2018 and 2017, respectively) on each November 15 and May 15, and the entire principal balance is due on November 15, 2032. Mandatory sinking fund payments will be due annually on November 15 as follows:

Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount	Fiscal year maturities	Principal amount
2019	$ 500,000	2025	$ 550,000	2031	$ 700,000
2020	500,000	2026	550,000	2032	700,000
2021	500,000	2027	600,000	2033	750,000
2022	500,000	2028	600,000		
2023	500,000	2029	650,000		
2024	550,000	2030	650,000		

(G) The Series 2001 and 2002 General Revenue Refunding Bonds bear interest at 64% of 30-day LIBOR plus 50 basis points (1.82% and 1.25% as of June 30, 2018 and 2017, respectively). To minimize the effect of changes in LIBOR, EVMS entered into an interest rate swap contract with a current notional principal amount of $1,800,000, under which it pays interest at 5.635% and receives interest at 64% of 30-day LIBOR plus 50 basis points. The swap will expire on November 15, 2018. The cumulative unrealized loss of $28,469 and $159,706 as of June 30, 2018 and 2017, respectively, from the changes in the swap contract’s fair value is included in long-term debt.

The Series 2010 General Revenue Refunding Bonds bear interest at 67% of 30-day LIBOR plus 169 basis points (3.08% and 2.47% as of June 30, 2018 and 2017, respectively). To minimize the effect of changes in LIBOR, EVMS entered into an interest rate swap contract with a current notional principal amount of $8,855,000, under which it pays interest at 3.31% and receives interest at 67% of 30-day LIBOR plus 169 basis points. The swap will expire on November 15, 2032. The cumulative unrealized loss of $200,735 and $548,615 as of June 30, 2018 and 2017, respectively, from the changes in the swap contract’s fair value is included in long-term debt.

The Series 2010 General Revenue Bonds bear interest at 67% of 30-day LIBOR plus 184 basis points (3.23% and 2.62% as of June 30, 2018 and 2017, respectively). To minimize the effect of changes in LIBOR, EVMS entered into an interest rate swap contract with a current notional principal amount of $12,000,000, under which it pays interest at 3.28% and receives interest at 67% of 30-day LIBOR plus 184 basis points. The swap will expire on November 15, 2027. The cumulative unrealized loss of $118,411 and $483,090 as of June 30, 2018 and 2017, respectively, from the changes in the swap contract’s fair value is included in long-term debt.

The Series 2011 General Revenue Bonds bear interest at 65% of 30-day LIBOR plus 170 basis points (3.04% and 2.46% as of June 30, 2018 and 2017, respectively). To minimize the effect of changes in LIBOR, EVMS entered into an interest rate swap contract with a current notional principal amount of $8,800,000, under which it pays interest at 2.94% and receives interest at 65% of 30-day LIBOR plus 170 basis points. The swap will expire on November 15, 2032. The cumulative unrealized loss of $16,376 and $318,570 as of June 20, 2018 and 2017, respectively, from the changes in the swap contract’s fair value are included in long-term debt.

Annual changes in the swap contracts’ fair value are included in nonoperating items in the accompanying consolidated statement of activities.

(H) Pursuant to the terms of the Indentures of Trust, EVMS is required to comply with certain covenants regarding payment of bonds, pledging of revenues, the operations of EVMS, insurance, accounting and financial statements, limitations on liens and the incurrence of additional indebtedness, and the sale, lease, or other disposition of assets. EVMS was in compliance with its covenants for the fiscal years ended June 30, 2018 and 2017. The bonds are equally and ratably secured by an unconditional guaranty of EVMS Foundation and by security interest in revenue granted by EVMS.

Payment requirements on EVMS’ bonds payable for the next five years ending June 30 and thereafter are as follows:

2019	$ 4,500,000
2020	2,695,000
2021	2,735,000
2022	2,780,000
2023	2,820,000
Thereafter	22,420,000
	$ 37,950,000

(11) Leases

EVMS has several noncancelable operating leases, primarily for buildings and medical and office equipment, which expire over the next six years. These leases generally contain renewal options for periods ranging from one to five years. Total rental expense for operating leases for the years ended June 30, 2018 and 2017 amounted to $2,690,871 and $2,819,924, respectively.

Future minimum lease payments under noncancelable operating leases (with initial or remaining lease terms in excess of one year) as of June 30, 2018 were approximately as follows:

Year ending June 30:		
2019	$	2,361,756
2020		2,160,055
2021		2,055,988
2022		2,084,304
2023		1,817,103
Thereafter		2,304,318
Total minimum operating lease payments	$	12,783,524

(12) Grant Deposits

At June 30, 2018 and 2017, grant deposits for sponsored research consisted of the following:

		2018	2017
Federal grants	$	624,045	532,004
State and local grants		281,597	383,706
Private gifts and grants:			
Bill and Melinda Gates Foundation		868,339	1,588,082
Obici Healthcare Foundation		15,609	302,515
Varian		82,213	62,845
Sanofi		116,465	—
Illumina		44,676	3,446
Others		600,495	486,924
Total private gifts and grants		1,727,797	2,443,812
Total grant deposits	$	2,633,439	3,359,522

Grant deposits represent amounts received for various grants and contracts that have not been expended at June 30, 2018 and 2017. If amounts are not expended per agreement, they will be refunded to the grantors, as required.

(13) Assets Held for Affiliate

Various donors contributed funds to the EVMS Foundation for the purpose of establishing loan funds for EVMS students. EVMS manages the award and subsequent collection of these loans from EVMS students on behalf of the EVMS Foundation. The amount of loan funds held for the EVMS Foundation at June 30, 2018 and 2017 was $910,855 and $891,406, respectively.

(14) State Appropriations

EVMS receives state appropriations funds annually. A summary of the programs supported for the years ended June 30, 2018 and 2017 is as follows:

		2018	2017
Education	$	17,024,048	16,947,539
Indigent care		6,158,108	6,158,108
Family medicine		665,164	661,026
Medical modeling and simulation		510,600	417,507
Higher education equipment trust fund		524,429	553,387
Capital maintenance reserve		317,353	176,220
Capital projects		527,239	—
Virginia Area Health Education Center		60,620	63,146
	$	25,787,561	24,976,933

(15) Operating Expenses

Operating expenses by natural category for the years ended June 30, 2018 and 2017 were as follows:

		2018	2017
Salaries and wages	$	132,882,593	129,847,355
Contractual services		26,218,498	29,383,656
General expenses		29,451,819	27,174,034
Fringe benefits		26,568,818	25,343,603
Operating supplies and minor equipment		10,785,576	9,904,773
Depreciation and amortization		10,248,539	10,336,371
Interest expense		1,368,224	1,536,753
Indigent care – institutional component		80,000	80,000
Total operating expenses	$	237,604,067	233,606,545

(Continued)

(16) Retirement Plan

Substantially all of the salaried personnel of EVMS are eligible after specified periods of employment to participate in qualified tax-deferred annuity plans under Sections 403(b) and 401(a) of the IRC. EVMS' contributions to the plans are based on percentages of qualified employee earnings. EVMS contributions to this program were $5,155,922 and $4,869,378 for the fiscal years ended June 30, 2018 and 2017, respectively.

(17) Commitments and Contingencies

Amounts received and expended by EVMS under various federal and state programs are subject to audit by various federal and state agencies. In the opinion of management, audit adjustments, if any, will not have a significant effect on the consolidated financial position of the School.

EVMS is subject to various legal proceedings and claims, which arise in the ordinary course of its business. Appropriate provision has been made for possible losses, and in the opinion of management, the ultimate resolution of these matters will not have a material adverse effect on the consolidated financial position, results of activities, or liquidity of the School.

KPMG LLP
Suite 1900
440 Monticello Avenue
Norfolk, VA 23510

Independent Auditors' 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*

The Board of Visitors
Eastern Virginia Medical School:

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 consolidated financial statements of Eastern Virginia Medical School and Affiliated Organization (EVMS), which comprise the consolidated balance sheet as of June 30, 2018, and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated October 29, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered EVMS' 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 consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of EVMS' internal control. Accordingly, we do not express an opinion on the effectiveness of EVMS' 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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's consolidated financial statements will not be prevented, or detected, and corrected on a timely basis. 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 EVMS' consolidated 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 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 EVMS' internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering EVMS' internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Norfolk, Virginia
October 29, 2018