

**Audited
Consolidated
Financial
Statements**

December 31, 2019

AdventHealth

**Table of
Contents**

Consolidated Balance Sheets	2
Consolidated Statements of Operations and Changes in Net Assets	3
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	6
Report of Independent Auditors	38

Consolidated Balance Sheets

December 31, 2019
and 2018

(dollars in thousands)

	2019	2018
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 184,811	\$ 576,390
Investments	7,000,804	5,859,138
Current portion of assets whose use is limited	381,119	333,888
Patient accounts receivable	593,627	581,568
Due from brokers	261,960	82,240
Estimated settlements from third parties	63,066	63,732
Other receivables	749,747	516,849
Inventories	254,760	234,253
Prepaid expenses and other current assets	141,282	109,322
	<u>9,631,176</u>	<u>8,357,380</u>
Property and Equipment	7,205,731	6,506,650
Operating Lease Assets	274,916	—
Assets Whose Use is Limited, net of current portion	445,416	359,718
Other Assets	<u>828,650</u>	<u>752,942</u>
	<u>\$ 18,385,889</u>	<u>\$ 15,976,690</u>
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable and accrued liabilities	\$ 1,453,059	\$ 1,216,499
Estimated settlements to third parties	150,176	175,334
Due to brokers	633,078	393,120
Other current liabilities	463,765	311,573
Short-term financings	104,420	104,420
Current maturities of long-term debt	55,711	101,536
	<u>2,860,209</u>	<u>2,302,482</u>
Long-Term Debt, net of current maturities	2,928,895	2,857,654
Operating Lease Liabilities, net of current portion	220,449	—
Other Noncurrent Liabilities	<u>565,260</u>	<u>612,773</u>
	<u>6,574,813</u>	<u>5,772,909</u>
Net Assets		
Net assets without donor restrictions	11,584,007	9,984,702
Net assets with donor restrictions	187,842	185,946
	<u>11,771,849</u>	<u>10,170,648</u>
Noncontrolling interests	39,227	33,133
	<u>11,811,076</u>	<u>10,203,781</u>
Commitments and Contingencies		
	<u>\$ 18,385,889</u>	<u>\$ 15,976,690</u>

AdventHealth

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

Consolidated Statements of Operations and Changes in Net Assets

For the years ended
December 31, 2019
and 2018

(dollars in thousands)

	2019	2018
Revenue		
Net patient service revenue	\$ 11,435,650	\$ 10,577,663
Other	456,617	396,461
Total operating revenue	11,892,267	10,974,124
Expenses		
Employee compensation	5,787,576	5,337,918
Supplies	1,990,987	1,809,820
Purchased services	973,224	868,384
Professional fees	729,285	635,831
Other	873,775	873,623
Interest	88,376	90,239
Depreciation and amortization	619,655	574,050
Total operating expenses	11,062,878	10,189,865
Income from Operations	829,389	784,259
Nonoperating Gains (Losses)		
Investment return	745,343	(155,564)
Loss on extinguishment of debt	(7,625)	(10,033)
Contribution from business combination	13,675	—
Total nonoperating gains (losses), net	751,393	(165,597)
Excess of revenue and gains over expenses and losses	1,580,782	618,662
Noncontrolling interests	(2,202)	(333)
Excess of Revenue and Gains over Expenses and Losses Attributable to Controlling Interest	1,578,580	618,329

Consolidated Statements of Operations and Changes in Net Assets (continued)

For the years ended
December 31, 2019
and 2018

(dollars in thousands)

CONTROLLING INTEREST

Net Assets Without Donor Restrictions

	2019	2018
Excess of revenue and gains over expenses and losses	\$ 1,578,580	\$ 618,329
Net assets released from restrictions for purchase of property and equipment	26,844	25,961
Change in unrealized gains and losses on investments	2,740	(4,457)
Pension-related changes other than net periodic pension cost	(1,702)	26
Other	(7,157)	(4,203)
Increase in net assets without donor restrictions	1,599,305	635,656

Net Assets With Donor Restrictions

Gifts and grants	27,910	37,840
Net assets released from restrictions for purchase of property and equipment or use in operations	(36,992)	(43,237)
Investment return	3,353	691
Other	7,625	3,986
Increase (decrease) in net assets with donor restrictions	1,896	(720)

NONCONTROLLING INTERESTS

Net Assets Without Donor Restrictions

Excess of revenue and gains over expenses and losses	2,202	333
Distributions	(845)	(1,018)
Other	4,737	745
Increase in noncontrolling interests	6,094	60

Increase in Net Assets

Net assets, beginning of year	10,203,781	9,568,785
Net assets, end of year	<u>\$ 11,811,076</u>	<u>\$ 10,203,781</u>

Consolidated Statements of Cash Flows

For the years ended
December 31, 2019
and 2018

(dollars in thousands)

	2019	2018
Operating Activities		
Increase in net assets	\$ 1,607,295	\$ 634,996
Increase in net assets from business combination	(13,675)	—
Depreciation and amortization	619,655	574,050
Amortization of deferred financing costs and original issue discounts and premiums	(13,127)	(9,161)
Loss on extinguishment of debt	7,625	10,033
Net realized and unrealized (gains) losses on investments	(620,859)	239,391
Restricted gifts and grants and investment return	(31,263)	(38,531)
Income from unconsolidated entities	(64,287)	(59,303)
Distributions from unconsolidated entities	30,092	14,715
Pension-related changes other than net periodic pension cost	1,702	(26)
Changes in operating assets and liabilities:		
Patient accounts receivable	(620,789)	(469,803)
Other receivables	(6,921)	37,462
Other current assets	(9,242)	16,130
Accounts payable and accrued liabilities	226,646	114,570
Estimated settlements to third parties, net	(24,633)	(49,912)
Other current liabilities	71,437	(1,068)
Other noncurrent assets and liabilities	(30,853)	14,797
Net cash provided by operating activities	1,128,803	1,028,340
Investing Activities		
Purchases of property and equipment, net	(1,176,612)	(879,353)
Cash paid for acquisitions, net of cash received	(177,220)	(150,149)
Cash acquired in business combination	3,486	—
Sales and maturities of investments	1,938,981	3,028,615
Purchases of investments	(2,488,744)	(3,304,219)
Due from brokers	(179,720)	256,381
Due to brokers	239,958	(303,601)
Sales, maturities, and uses of assets whose use is limited	265,483	249,204
Purchases of and additions to assets whose use is limited	(159,940)	(220,493)
Return of capital from unconsolidated entities	18,549	10,806
Cash receipts on sold patient accounts receivable	388,712	423,310
(Increase) decrease in other assets	(41,109)	23,610
Net cash used in investing activities	(1,368,176)	(865,889)
Financing Activities		
Repayments of long-term borrowings	(524,249)	(242,341)
Additional long-term borrowings	554,371	379,269
Repayments of short-term borrowings	—	(206,000)
Additional short-term borrowings	—	131,000
Payment of deferred financing costs	(4,075)	(3,197)
Restricted gifts and grants and investment return	31,263	38,531
Net cash provided by financing activities	57,310	97,262
(Decrease) Increase in Cash, Cash Equivalents, Restricted Cash, and Restricted Cash Equivalents	(182,063)	259,713
Cash, cash equivalents, restricted cash, and restricted cash equivalents at beginning of year	685,128	425,415
Cash, Cash Equivalents, Restricted Cash, and Restricted Cash Equivalents at End of Year	<u>\$ 503,065</u>	<u>\$ 685,128</u>
Noncash Investing Activity		
Beneficial interest obtained in exchange for patient accounts receivable	\$ (614,686)	\$ (366,326)

AdventHealth

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

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

1. Significant Accounting Policies

Reporting Entity

Adventist Health System Sunbelt Healthcare Corporation d/b/a AdventHealth (Healthcare Corporation) is a not-for-profit healthcare corporation that owns and/or operates hospitals, nursing homes, physician offices, urgent care centers and other healthcare facilities, and a philanthropic foundation with various informal divisions (collectively referred to herein as the System). The System's affiliated healthcare facilities are operated or controlled through their by-laws, governing board appointments, or operating agreements. The System's 46 hospitals, 11 nursing homes, and philanthropic foundations operate in 9 states – Colorado, Florida, Georgia, Illinois, Kansas, Kentucky, North Carolina, Texas, and Wisconsin.

SunSystem Development Corporation (Foundation) is a charitable foundation operated by Healthcare Corporation for the benefit of many of the hospitals that are divisions or controlled affiliates. Healthcare Corporation is the Foundation's member and appoints its board of managers. The Foundation engages in philanthropic activities.

Healthcare Corporation and the System are collectively controlled by the Lake Union Conference of Seventh-day Adventists, the Mid-America Union Conference of Seventh-day Adventists, the Southern Union Conference of Seventh-day Adventists, and the Southwestern Union Conference of Seventh-day Adventists.

Mission

The System exists solely to improve and enhance the local communities that it serves in harmony with Christ's healing ministry. All financial resources and excess of revenue and gains over expenses and losses are used to benefit the communities in the areas of patient care, research, education, community service, and capital reinvestment.

Specifically, the System provides:

Benefit to the underprivileged, by offering services free of charge or deeply discounted to those who cannot pay, and by supplementing the unreimbursed costs of the government's Medicaid assistance program.

Benefit to the elderly, as provided through governmental Medicare funding, by subsidizing the unreimbursed costs associated with this care.

Benefit to the community's overall health and wellness through the cost of providing clinics and primary care services, health education and screenings, in-kind donations, extended education, and research.

Benefit to the faith-based and spiritual needs of the community in accordance with its mission of extending the healing ministry of Christ.

Benefit to the community's infrastructure by investing in capital improvements to ensure the facilities and technology provide the best possible care to the community.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of affiliated organizations that are controlled by Healthcare Corporation. Any subsidiary or other operations owned and controlled by divisions or controlled affiliates of Healthcare Corporation are included in these consolidated financial statements. Investments in entities that Healthcare Corporation does not control are recorded under the equity or cost method of accounting, depending on the ability to exert significant influence. Income from unconsolidated entities is included in other operating revenue or as a reduction to supplies expense (Note 6) in the accompanying consolidated statements of operations and changes in net assets. All significant intercompany accounts and transactions have been eliminated in consolidation. Partial ownership by another entity in the net assets and results of operations of a consolidated subsidiary is reflected as noncontrolling interests in the accompanying consolidated financial statements.

Use of Estimates

The preparation of these consolidated financial statements in conformity with accounting principles generally accepted in the United States (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Recently Adopted Accounting Guidance

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases* (ASU 2016-02). The FASB codified ASU 2016-02 in the FASB Accounting Standards Codification (ASC) as Topic 842 (ASC 842). The standard introduces a lease accounting model that requires an entity to recognize assets and liabilities arising from most leases, including both finance and operating leases. On January 1, 2019, the System adopted the new lease accounting standard using a modified retrospective method of application to all leases existing on January 1, 2019. The System elected the package of practical expedients permitted under the transition guidance within the new standard, which among other things, allowed the System to carry forward the historical lease classification.

The adoption of ASC 842 resulted in the recognition of operating lease assets and operating lease liabilities of approximately \$269,000 and \$285,000 as of January 1, 2019, respectively, while the accounting for finance leases remained substantially unchanged. Lease assets represent the System's right to use an underlying asset for the lease term and lease liabilities represent the System's obligation to make lease payments arising from the lease. The standard did not materially impact the System's consolidated statement of operations and changes in net assets or cash flows for the year ended December 31, 2019. Expanded disclosures required by ASC 842 are included within Note 7.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, which addresses the presentation of certain cash flows with the objective of reducing the existing diversity in practice. The System retrospectively adopted the standard effective for the December 31, 2019 consolidated financial statements. The adoption results in classifying consideration received for beneficial interest obtained in exchange for transferring patient accounts receivable as investing activities instead of operating activities in the consolidated statement of cash flows. The increase in cash flow from investing activities and the corresponding decrease to cash flow from operating

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

activities upon adoption of the standard was approximately \$388,000 and \$423,000 for the fiscal years ended December 31, 2019 and 2018, respectively.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*, which provides guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. Accordingly, restricted cash or restricted cash equivalents should be included with cash and cash equivalents when reconciling the total amounts shown on the statement of cash flows at the beginning and at the end of period. The System retrospectively adopted the standard effective for the December 31, 2019 consolidated financial statements. The adoption changed the presentation and classification of cash and cash equivalents included in assets whose use is limited in the consolidated statements of cash flows. A summary of the major limitations as to the use of assets whose use is limited is disclosed in Note 3.

Recent Accounting Guidance Not Yet Adopted

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. This ASU aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. Management is currently evaluating the potential impact of this guidance, which will be effective for the System beginning in 2021.

In May 2019, the FASB issued ASU No. 2019-06, *Intangibles – Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958): Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities*, which allows not-for-profits to apply accounting alternatives that simplify the subsequent accounting for goodwill and accounting for certain intangible assets that are acquired. Not-for-profits that elect the goodwill accounting alternative must amortize goodwill over a period not greater than 10 years. Additionally, goodwill is only required to be tested for impairment when a triggering event occurs. Not-for-profits that elect the intangible asset accounting alternative may recognize fewer identifiable intangible assets in an acquisition. Management is currently evaluating whether to elect the alternative.

Net Patient Service Revenue

Net patient service revenue is reported at the amount that reflects the consideration the System expects to be due from patients and third-party payors in exchange for providing patient care. Providing patient care services is considered a single performance obligation, satisfied over time, in both the inpatient and outpatient setting. Generally, the System bills the patients and third-party payors several days after services are performed or the patient is discharged from the facility.

Revenue for inpatient acute care services is recognized based on actual charges incurred in relation to total expected, or actual, charges. The System 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.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

As all the System's performance obligations relate to contracts with a duration of less than one year, the System is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially satisfied at the end of the reporting period, which 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.

For patients covered by third-party payors, the System determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to those third-party payors. The System determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience.

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. The System is subject to retroactive revenue adjustments due to future audits, reviews, and investigations. In addition, the contracts the System has with commercial payors also provide for retroactive audit and review of claims. Settlements with third-party payors for retroactive adjustments 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 with the payor, and the System's historical settlement activity, attempting to ensure that a significant revenue reversal will not occur when the final amounts are subsequently determined. Estimated settlements are adjusted in future periods as new information becomes available, or as years are settled or are no longer subject to such audits, reviews, and investigations. Net adjustments for prior-year cost reports and related valuation allowances, principally related to Medicare and Medicaid, resulted in increases to revenue of approximately \$32,000 and \$24,000 for the years ended December 31, 2019 and 2018, respectively.

Generally, patients covered by third-party payors are responsible for related deductibles and coinsurance, which is referred to as the patient portion. The System also provides services to uninsured patients and offers those uninsured patients a discount from standard charges in accordance with its policies.

Consistent with the System's mission, care is provided to patients regardless of their ability to pay. Therefore, the System has determined that it has provided implicit price concessions to uninsured patients and patients with other uninsured balances such as copay and deductibles. The difference between amounts billed to patients and the amounts the System expects to collect based on its collection history with those patients is recorded as implicit price concessions, or as a direct reduction to net patient service revenue. Subsequent adjustments that are determined to be the result of an adverse change in the patient's or payor's ability to pay are recognized as bad debt expense. Bad debt expense for the years ended December 31, 2019 and 2018 was not material for the System, and is included within other expense in the accompanying consolidated statements of operations and changes in net assets, rather than as a deduction to arrive at revenue.

The System estimates the transaction price for the patient portion and 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.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

The composition of net patient service revenue by primary payor is as follows:

	Year Ended December 31,			
	2019		2018	
	Amount	%	Amount	%
Managed Care	\$ 5,999,015	52%	\$ 5,517,497	52%
Medicare	2,349,128	20	2,221,138	21
Managed Medicare	1,562,356	14	1,317,488	12
Medicaid	458,963	4	507,344	5
Managed Medicaid	518,920	5	473,556	5
Self-pay	122,703	1	137,863	1
Other	424,565	4	402,777	4
	<u>\$11,435,650</u>	<u>100%</u>	<u>\$10,577,663</u>	<u>100%</u>

Charity Care

The System's patient acceptance policy is based on its mission statement and its charitable purposes and as such, the System accepts patients in immediate need of care, regardless of their ability to pay. Patients that qualify for charity care are provided services for which no payment is due for all or a portion of the patient's bill. Therefore, charity care is excluded from patient service revenue and the cost of providing such care is recognized within operating expenses.

The System estimates the direct and indirect costs of providing charity care by applying a cost to gross charges ratio to the gross uncompensated charges associated with providing charity care to patients. The System also receives certain funds to offset or subsidize charity care services provided. These funds are primarily received from uncompensated care programs sponsored by various states, whereby healthcare providers within the state pay into an uncompensated care fund and the pooled funds are then redistributed based on state-specific criteria.

The cost of providing charity care services, amounts paid by the System into uncompensated care funds, and amounts received by the System to offset or subsidize charity care services are as follows:

	Year Ended December 31,	
	2019	2018
Charity Care Cost		
Cost of providing charity care services	<u>\$ 438,090</u>	<u>\$ 364,078</u>
Charity Care Funding		
Funds received to offset or subsidize charity care services (included in patient service revenue)	\$ 266,916	\$ 314,154
Funds paid into trusts (included in other expenses)	<u>(223,153)</u>	<u>(244,125)</u>
Net charity care funding received	<u>\$ 43,763</u>	<u>\$ 70,029</u>

Excess of Revenue and Gains over Expenses and Losses

The consolidated statements of operations and changes in net assets include excess of revenue and gains over expenses and losses as the performance indicator, which is analogous to net income of a for-profit enterprise. Changes in net assets without donor restrictions that are excluded from the performance indicator may include transfers of net assets released from restrictions for the purpose of acquiring long-lived assets, change in unrealized gains and losses on certain investments, certain qualifying derivative activity, pension-related changes other than net periodic pension cost and other changes in net assets.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Contributed Resources

Resources restricted by donors for specific operating purposes or a specified time period are held as net assets with donor restrictions until expended for the intended purpose or until the specified time restrictions are met, at which time they are reported as other revenue. Resources restricted by donors for additions to property and equipment are held as net assets with donor restrictions until the assets are placed in service, at which time they are reported as transfers to net assets without donor restrictions. Gifts, grants, and bequests not restricted by donors are reported as other revenue.

Cash Equivalents

Cash equivalents represent all highly liquid investments, including certificates of deposit and commercial paper with maturities not in excess of three months when purchased. Interest income on cash equivalents is included in investment return.

The following table provides a reconciliation of cash, cash equivalents, restricted cash, and restricted cash equivalents reported within the statement of financial position that sum to the total of the same such amounts shown in the statements of cash flows.

	December 31,	
	2019	2018
Cash and cash equivalents	\$ 184,811	\$ 576,390
Restricted cash and restricted cash equivalents included in current portion of assets whose use is limited	318,254	108,738
Total cash, cash equivalents, restricted cash, and restricted cash equivalents shown in the statement of cash flows	\$ 503,065	\$ 685,128

Investments

Investments include marketable securities and other investments. Investments in debt and equity securities with readily determinable fair values are reported at fair value, based on quoted market prices and are primarily designated as trading securities. The cost of securities sold is based on the average cost method.

Other investments include alternative investments, which are primarily hedge funds, commingled funds, and various exchange-traded and over-the-counter derivative instruments. Hedge funds are accounted for under the equity method, which approximates fair value as determined by the net asset value (NAV). The System's hedge funds are primarily invested in funds of hedge funds, and those hedge funds may have underlying investments that may not have quoted market values. The value of such investments is estimated, and those estimates may change in the near term. The System's risk is limited to its investment in the hedge fund. The financial statements and internal controls of the funds of hedge funds are audited annually by independent auditors.

Commingled funds are used to obtain the desired exposure targets within the investment portfolio. The fair value of the System's investments in commingled funds is estimated using NAV as a practical expedient, as determined by the fund's administrator. These commingled funds have daily redemption terms. There were no unfunded commitments relating to commingled funds as of December 31, 2019 or 2018.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Other investments may also include exchange-traded and over-the-counter derivative instruments that are held for trading purposes and to act as economic hedges to manage the risk of the investment portfolio. These instruments, which primarily include futures, options, and swaps, are used to gain broad market exposure and additional exposure to equity markets, adjust the fixed-income portfolio duration, provide an economic hedge against fluctuations in foreign exchange rates, and generate investment returns. These derivative instruments are not designated as hedging instruments.

Investment return includes realized gains and losses, interest, dividends, and net change in unrealized gains and losses. The investment return on investments restricted by donor or law is recorded as increases or decreases to net assets with donor restrictions. Investment return earned on the System's self-insurance trust funds and employee benefits funds is recorded in other operating revenue.

Assets Whose Use is Limited

Certain of the System's investments are limited as to use through the terms of trust agreements, internal designation, under the terms of bond indentures, or the provisions of other contractual arrangements. These investments are classified as assets whose use is limited in the accompanying consolidated balance sheets.

Sale of Patient Accounts Receivable

The System and certain of its member affiliates maintain a program for the continuous sale of certain patient accounts receivable to the Highlands County, Florida, Health Facilities Authority (Highlands) on a nonrecourse basis. Highlands has partially financed the purchase of the patient accounts receivable through the issuance of private placement, tax-exempt, variable-rate bonds (Bonds). Highlands had Bonds outstanding of \$320,000 and \$360,000 as of December 31, 2019 and 2018, respectively. The Bonds have a put date of December 2022 and a final maturity date of November 2027. The System is the servicer of the receivables under this arrangement and is responsible for performing all accounts receivable administrative functions.

As of December 31, 2019 and 2018, the estimated net realizable value, as defined in the underlying agreements, of patient accounts receivable sold by the System and removed from the accompanying consolidated balance sheets was \$983,537 and \$797,383, respectively. The patient accounts receivable sold consist primarily of amounts due from government programs and commercial insurers. The proceeds received from Highlands consist of cash from the Bonds, a note on a subordinated basis with the Bonds, and a note on a parity basis with the Bonds. The note on a subordinated basis with the Bonds is in an amount to provide the required over-collateralization of the Bonds and was \$80,000 and \$90,000 at December 31, 2019 and 2018, respectively. The note on a parity basis with the Bonds is the excess of eligible accounts receivable sold over the sum of cash received and the subordinated note and was \$583,537 and \$347,383 at December 31, 2019 and 2018, respectively. These notes are included in other receivables in the accompanying consolidated balance sheets. Due to the nature of the patient accounts receivable sold, collectability of the subordinated and parity notes is not significantly impacted by credit risk.

The notes on a parity and subordinated basis represent the System's beneficial interest in the receivables subsequent to the sale. Cash received at the time of sale is recognized within the consolidated statement of cash flows as part of operating activities. Any subsequent cash received on the beneficial interest is recognized within the consolidated statement of cash flows as part of investing activities.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Inventories

Inventories (primarily pharmaceuticals and medical supplies) are stated at the lower of cost or net realizable value using the first-in, first-out method of valuation.

Property and Equipment

Property and equipment are reported on the basis of cost, except for those assets donated, impaired, or acquired under a business combination, which are recorded at fair value. Expenditures that materially increase values, change capacities, or extend useful lives are capitalized. Depreciation is computed primarily utilizing the straight-line method over the expected useful lives of the assets. Amortization of capitalized leased assets is included in depreciation expense and allowances for depreciation.

Goodwill

Goodwill represents the excess of the purchase price and related costs over the value assigned to the net tangible and identifiable intangible assets of the businesses acquired. These amounts are included in other assets (noncurrent) in the accompanying consolidated balance sheets and are evaluated annually for impairment or when there is an indicator of impairment.

During 2019 and 2018, the System performed a qualitative assessment of goodwill and determined that the impairment test under the Intangibles – Goodwill and Other Topic of the ASC was not required.

Interest in the Net Assets of Unconsolidated Foundations

Interest in the net assets of unconsolidated foundations represents contributions received on behalf of the System or its member affiliates by independent fund-raising foundations. As the System cannot influence the foundations to the extent that it can determine the timing and amount of distributions, the System's interest in the net assets of the foundations is included in other assets and changes in that interest are included in net assets with donor restrictions.

Impairment of Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or business conditions indicate the carrying amount of such assets may not be fully recoverable. Initial assessments of recoverability are based on estimates of undiscounted future net cash flows associated with an asset or group of assets. Where impairment is indicated, the carrying amount of these long-lived assets is reduced to fair value based on discounted net cash flows or other estimates of fair value.

Deferred Financing Costs

Direct financing costs are included as a reduction to the carrying amount of the related debt liability and are deferred and amortized over the remaining lives of the financings using the effective interest method.

Bond Discounts and Premiums

Bonds payable, including related original issue discounts and/or premiums, are included in long-term debt. Discounts and premiums are being amortized over the life of the bonds using the effective interest method.

Income Taxes

Healthcare Corporation and its affiliated organizations, other than North American Health Services, Inc. and its subsidiary (NAHS), are exempt from state and federal income taxes. Accordingly, Healthcare Corporation and its tax-exempt affiliates are

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

not subject to federal, state, or local income taxes except for any net unrelated business taxable income.

NAHS is a wholly owned, for-profit subsidiary of Healthcare Corporation. NAHS and its subsidiary are subject to federal and state income taxes. NAHS files a consolidated federal income tax return and, where appropriate, consolidated state income tax returns. All taxable income was fully offset by net operating loss carryforwards for federal income tax purposes; as such, there is no provision for current federal or state income tax for the years ended December 31, 2019 and 2018.

NAHS also has temporary deductible differences of approximately \$46,500 and \$53,000 at December 31, 2019 and 2018, respectively, primarily as a result of net operating loss carryforwards. At December 31, 2019, NAHS had net operating loss carryforwards of approximately \$47,500, expiring beginning in 2022 through 2026. Deferred taxes have been provided for these amounts, resulting in a net deferred tax asset of approximately \$11,400 and \$13,400 at December 31, 2019 and 2018, respectively. NAHS remeasured its deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future, which is generally 21%. A full valuation allowance has been provided at December 31, 2019 and 2018 to offset the deferred tax asset, since Healthcare Corporation has determined that it is more likely than not that the benefit of the net operating loss carryforwards will not be realized in future years.

The Income Taxes Topic of the ASC (ASC 740) prescribes the accounting for uncertainty in income tax positions recognized in financial statements. ASC 740 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken, or expected to be taken, in a tax return. There were no material uncertain tax positions as of December 31, 2019 and 2018.

On December 22, 2017, the United States enacted tax reform legislation commonly known as the Tax Cuts and Jobs Act (Act), resulting in significant modifications to existing law. Certain provisions impact tax-exempt organizations, including revisions to taxes on unrelated business activities, excise taxes on compensation of certain employees, and various other provisions. While final regulations on these provisions have not yet been promulgated, the impact of these provisions on the consolidated financial statements is not expected to be significant.

Reclassifications

Certain reclassifications were made to the 2018 consolidated financial statements to conform to the classifications used in 2019. These reclassifications had no impact on the consolidated excess of revenue and gains over expenses and losses, changes in net assets, or cash flows previously reported.

2. Organizational Changes

Business Combinations

The System accounts for transactions that represent business combinations in accordance with the Not-for-Profit Entities, Business Combinations Topic of the ASC (ASC 958-805), where the assets acquired and liabilities assumed are recognized and measured at their fair values on the acquisition date. Fair values that are not finalized are estimated and reported as provisional amounts.

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

AdventHealth Ottawa

On May 1, 2019, the System entered into an agreement to lease Ransom Memorial Health (RMH), a 44-bed hospital and its related outpatient locations in Ottawa, Kansas, for an initial term of 25 years. As a part of this transaction, RMH was renamed AdventHealth Ottawa (AH Ottawa). The non-cash business combination was recorded under the acquisition method of accounting. The System recorded the fair value of the assets acquired of \$23,598 and the liabilities assumed of \$9,923 as of May 1, 2019. The fair value of AH Ottawa's net assets of \$13,675 was recognized in the consolidated statement of operations and changes in net assets as a contribution from business combination and is included in nonoperating gains.

The results of operations and changes in net assets for AH Ottawa were included in the System's consolidated financial statements beginning May 1, 2019. AH Ottawa had total operating revenue of \$30,052 and a deficiency of revenue and gains over expenses and losses of \$3,638 for the period from May 1, 2019 through December 31, 2019.

AdventHealth Heart of Florida and AdventHealth Lake Wales

On September 1, 2019, the System entered into an asset purchase agreement under which, the System acquired certain assets related to Heart of Florida Regional Medical Center, a 193-bed hospital in Davenport, Florida, which was renamed AdventHealth Heart of Florida (AH HOF), and a 160-bed hospital in Lake Wales, Florida, which was renamed AdventHealth Lake Wales (AH Lake Wales). The acquisition included the purchase of substantially all the property and equipment of the hospitals, the related outpatient services, and certain working capital.

The assets acquired and liabilities assumed were recorded based on their acquisition date fair values. Cash consideration was \$177,371, which primarily represented the payment for the real and personal property. The provisional amounts recognized as of the acquisition date for each major class of assets acquired and liabilities assumed are as follows:

Assets

Cash and cash equivalents	\$	151
Patient accounts receivable		801
Inventories		7,487
Prepaid expenses and other current assets		1,824
Property and equipment		155,649
Operating lease assets		17,318
Other assets		24,934
		<hr/> 208,164

Liabilities

Accounts payable and accrued liabilities	\$	6,507
Other current liabilities		205
Current maturities of long-term debt		548
Long-term debt, net of current maturities		2,992
Operating lease liabilities, net of current portion		20,541
		<hr/> 30,793

Fair Value of Net Assets Acquired

\$ 177,371

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

The assessment of fair value is preliminary and is based on information that was available at the time the consolidated financial statements were prepared. The System has not finalized its review of certain assets and liabilities recorded in the acquisition, however management does not anticipate that adjustments to provisional amounts will be significant.

The goodwill acquired represents the excess of the purchase price and related costs over the value assigned to the net tangible and identifiable intangible assets of the business acquired. Goodwill is included in other assets (noncurrent) in the accompanying balance sheets.

The results of operations and changes in net assets for AH HOF and AH Lake Wales were included in the System's consolidated financial statements beginning September 1, 2019. AH HOF and AH Lake Wales had total operating revenue of \$63,907 and a deficiency of revenue and gains over expenses and losses of \$10,870 for the period from September 1, 2019 through December 31, 2019.

The following pro forma combined results of operations present the acquisition as if it had occurred on January 1, 2018 and, as such, reflect the impact of amortizing the fair value adjustments to property and equipment as of January 1, 2018. The pro forma combined results of operations do not necessarily represent the System's consolidated results of operations had the acquisition occurred on the date assumed, nor are these results necessarily indicative of the System's future consolidated results of operations. The System expects to realize certain benefits from integrating AH HOF and AH Lake Wales into the System and to incur certain one-time costs. The pro forma combined results of operations do not reflect these benefits or costs.

	Year Ended December 31,	
	2019	2018
Pro forma revenue	\$ 12,036,365	\$ 11,187,578
Pro forma excess of revenue and gains over expenses and losses	1,575,237	618,205
Pro forma change in net assets without donor restrictions	1,590,393	630,228

AdventHealth Dade City

On April 1, 2018, the System acquired a 120-bed hospital located in Dade City, Florida, which was renamed AdventHealth Dade City (Dade City). The acquisition included the purchase of substantially all the property and equipment of the hospital and its related outpatient services and certain working capital.

The results of operations and changes in net assets for Dade City were included in the System's consolidated financial statements beginning April 1, 2018. Dade City had total operating revenue of \$22,172 and a deficiency of revenue and gains over expenses and losses of \$12,427 for the period from April 1, 2018 through December 31, 2018.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

AdventHealth Ocala

On August 1, 2018, the System entered into an asset purchase agreement under which, the System acquired certain assets related to Munroe Regional Medical Center, a 425-bed hospital located in Ocala, Florida, which was renamed AdventHealth Ocala (Ocala). The acquisition includes the purchase of certain major moveable equipment and the assumption of a lease agreement for the hospital and related land, with a remaining term of approximately 36 years.

Cash consideration was \$140,673, which primarily represented the prepayment of the assumed lease obligation. The provisional amounts for the assets acquired and liabilities assumed were recorded based on the acquisition-date fair values recognized as of the acquisition date as follows:

Assets

Cash and cash equivalents	\$	5
Inventories		12,048
Prepaid expenses and other current assets		2,215
Property and equipment		127,788
Other assets		2,212
		<u>144,268</u>

Liabilities

Accounts payable and accrued liabilities	\$	2,421
Other current liabilities		1,110
Long-term debt		64
		<u>3,595</u>

Fair Value of Net Assets Acquired

<u>\$</u>	<u>140,673</u>
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The results of operations and changes in net assets for Ocala were included in the System's consolidated financial statements beginning August 1, 2018. Ocala had total operating revenue of \$100,595 and a deficiency of revenue and gains over expenses and losses of \$22,747 for the period from August 1, 2018 through December 31, 2018.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

3. Investments and Assets Whose Use is Limited

Investments and assets whose use is limited are comprised of the following:

	December 31,	
	2019	2018
Debt securities		
U.S. government agencies and sponsored entities	\$ 2,995,833	\$ 2,574,221
Foreign government agencies and sponsored entities	6,600	5,944
Corporate bonds	774,629	745,545
Mortgage backed	19,937	44,018
Other asset backed	35,719	55,439
Short-term investments	139,871	130,315
Accrued interest	13,369	15,134
	<u>3,985,958</u>	<u>3,570,616</u>
Exchange traded and mutual funds		
Domestic equity	784,563	687,644
Foreign equity	587,907	532,048
Fixed income	790,303	549,195
Real estate	18,560	17,408
	<u>2,181,333</u>	<u>1,786,295</u>
Investments at NAV		
Alternative investments	1,020,101	837,274
Commingled funds	321,693	249,821
	<u>1,341,794</u>	<u>1,087,095</u>
Cash and cash equivalents – assets whose use is limited		
	<u>318,254</u>	<u>108,738</u>
	<u>7,827,339</u>	<u>6,552,744</u>
Less: assets whose use is limited	<u>(826,535)</u>	<u>(693,606)</u>
Investments	<u>\$ 7,000,804</u>	<u>\$ 5,859,138</u>

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Investment Derivatives

The fair value of investment derivative instruments and the associated notional amounts, presented gross, were as follows:

	December 31, 2019			
	Notional		Fair Value	
	Long	Short	Assets	Liabilities
Equity options	\$ —	\$ (4)	\$ —	\$ (4)
Interest rate swaps	217	(103)	217	(103)
Futures	1,209,215	(225,557)	—	—
Total derivative instruments, gross	<u>\$ 1,209,432</u>	<u>\$ (225,664)</u>	<u>\$ 217</u>	<u>\$ (107)</u>

	December 31, 2018			
	Notional		Fair Value	
	Long	Short	Assets	Liabilities
Equity options	\$ 158	\$ (177)	\$ 158	\$ (177)
Interest rate swaps	768	(581)	768	(581)
Futures	347,020	(132,377)	—	—
Total derivative instruments, gross	<u>\$ 347,946</u>	<u>\$ (133,135)</u>	<u>\$ 926</u>	<u>\$ (758)</u>

The System posted collateral related to investment derivative instruments totaling \$38,239 and \$18,731 as of December 31, 2019 and 2018, respectively. Collateral is included in either cash and cash equivalents or investments in the accompanying consolidated balance sheets, depending on the type of collateral posted.

Assets Whose Use is Limited

Assets whose use is limited as of December 31, 2019 includes investments held under trust agreements for settling payments under the professional and general liability program, and internally designated investments for employee retirement plans. Amounts to be used for the payment of current liabilities are classified as current assets.

A summary of the major limitations as to the use of assets whose use is limited consists of the following:

	December 31,	
	2019	2018
Self-insurance trust funds	\$ 459,451	\$ 379,843
Employee benefits funds	230,524	213,629
Other	136,560	100,134
	826,535	693,606
Less: amounts to pay current liabilities	(381,119)	(333,888)
	<u>\$ 445,416</u>	<u>\$ 359,718</u>

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Investment Return and Unrealized Gains and Losses

Investment return from cash and cash equivalents, investments, and assets whose use is limited amounted to \$745,343 and \$(155,564) in the accompanying consolidated statements of operations and changes in net assets for the years ended December 31, 2019 and 2018, respectively, and consisted of the following:

	Year Ended December 31,	
	2019	2018
Interest and dividend income	\$ 153,440	\$ 137,391
Net realized gains (losses)	82,185	(58,021)
Net change in unrealized gains and losses	509,718	(234,934)
	<u>\$ 745,343</u>	<u>\$ (155,564)</u>

4. Liquidity and Available Resources

The System's primary cash requirements are paying operating expenses, servicing debt, capital expenditures related to the expansion and renovation of existing facilities, and acquisitions. Cash in excess of near-term working capital needs is invested as described in Notes 1 and 3. Primary cash sources are cash flows from operating and investing activities. Additionally, the System has access to public and private debt markets and maintains a revolving credit agreement and commercial paper program, as described in Note 8.

The System had 238 and 232 days cash on hand at December 31, 2019 and 2018, respectively. Days cash on hand is calculated as unrestricted cash and cash equivalents, investments, and due to brokers, net, divided by daily operating expenses (excluding depreciation and amortization expense). Unrestricted cash and cash equivalents, investments, and due to brokers, net consist of the following:

	December 31,	
	2019	2018
Cash and cash equivalents	\$ 184,811	\$ 576,390
Investments	7,000,804	5,859,138
Due to brokers, net	(371,118)	(310,880)
	<u>\$ 6,814,497</u>	<u>\$ 6,124,648</u>
Unrestricted days cash and investments on hand	<u>238</u>	<u>232</u>

The System's financial assets also consist of patient accounts receivable totaling \$593,627 and \$581,568 as of December 31, 2019 and 2018, respectively. Other receivables, totaling \$749,747 and \$516,849 as of December 31, 2019 and 2018, are primarily comprised of the notes associated with the System's sale of patient accounts receivable, which is more fully described in Note 1. The System's financial assets are available as its general expenditures, liabilities, and other obligations come due.

Certain assets whose use is limited are to be used for current liabilities for self-insured programs and employee benefit funds and are more fully described in Note 3.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

5. Property and Equipment

Property and equipment consist of the following:

	December 31,	
	2019	2018
Land and improvements	\$ 914,768	\$ 846,989
Buildings and improvements	6,246,371	5,655,951
Equipment	5,372,503	5,243,306
	<u>12,533,642</u>	<u>11,746,246</u>
Less: allowances for depreciation	<u>(5,967,345)</u>	<u>(5,762,370)</u>
	6,566,297	5,983,876
Construction in progress	639,434	522,774
	<u>\$ 7,205,731</u>	<u>\$ 6,506,650</u>

Certain hospitals have entered into construction contracts or other commitments for which costs have been incurred and included in construction in progress. These and other committed projects will be financed through operations and proceeds of borrowings. The estimated costs to complete these projects approximated \$498,000 at December 31, 2019.

During periods of construction, interest costs are capitalized to the respective property accounts. Interest capitalized approximated \$6,500 and \$7,400 for the years ended December 31, 2019 and 2018, respectively.

The System capitalizes the cost of acquired software for internal use. Any internal costs incurred in the process of developing and implementing software are expensed or capitalized, depending primarily on whether they are incurred in the preliminary project stage, application development stage, or post-implementation stage. Capitalized software costs and estimated amortization expense in the table below exclude software in progress of approximately \$17,000 and \$9,900 at December 31, 2019 and 2018, respectively. Capitalized software costs and accumulated amortization expense, which are included in property and equipment in the accompanying consolidated balance sheets, were as follows:

	December 31,	
	2019	2018
Capitalized software costs	\$ 333,592	\$ 280,758
Less: accumulated amortization	<u>(204,799)</u>	<u>(167,792)</u>
Capitalized software costs, net	<u>\$ 128,793</u>	<u>\$ 112,966</u>

Estimated amortization expense related to capitalized software costs for the next five years and thereafter is as follows:

2020	\$ 34,458
2021	30,251
2022	24,211
2023	6,412
2024	5,632
Thereafter	27,829

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

6. Other Assets

Other assets consisted of the following:

	December 31,	
	2019	2018
Goodwill	\$ 223,365	\$ 182,177
Notes and other receivables	60,355	71,894
Interests in net assets of unconsolidated foundations	71,302	64,954
Investments in unconsolidated entities	419,492	370,622
Other noncurrent assets	54,136	63,295
	<u>\$ 828,650</u>	<u>\$ 752,942</u>

The System's ownership interest and carrying amounts of investments in unconsolidated entities consist of the following:

	Ownership Interest	December 31,	
		2019	2018
Texas Health Huguley, Inc.	49%	\$ 139,301	\$ 93,696
Centura Health Corporation	35%	93,749	90,712
Premier Healthcare Alliance, LP	6%	124,133	129,887
Other	5% – 50%	62,309	56,327
		<u>\$ 419,492</u>	<u>\$ 370,622</u>

Income from unconsolidated entities, excluding Premier Healthcare Alliance, LP (Premier LP), totaled \$48,282 and \$30,229 for 2019 and 2018, respectively, and is included in other operating revenue in the accompanying consolidated statements of operations and changes in net assets.

The System holds membership units in Premier LP, which is a group purchasing organization. In 2013, the general partner, Premier, Inc., restructured from a privately held to a publicly traded company in an initial public offering. In connection with the restructuring, the System's membership units in Premier LP have vesting rights over a seven-year period and, upon vesting, become eligible for exchange into the common stock of Premier, Inc. The increase in estimated value of the membership units as they vest is considered a vendor incentive under GAAP, which increases the System's investment in Premier LP and reduces supplies expense over the vesting period. The System recognized a vendor incentive for the stock vesting of \$6,167 and \$16,586 for the years ended December 31, 2019 and 2018, respectively. Additionally, Premier LP equity method earnings totaled \$9,838 and \$12,488 and were recognized as a reduction to supplies expense for the years ended December 31, 2019 and 2018, respectively.

7. Leases

The System's leases primarily consist of real estate and medical equipment. The System determines if an arrangement is a lease at contract inception. Lease assets and lease liabilities are recognized based on the present value of the lease payments over the lease term at the commencement date. Because most of the System's leases do not provide an implicit rate of return, the System uses a risk-free rate based on the daily treasury yield curve at lease commencement in determining the present value of lease payments. Lease assets exclude lease incentives received.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Most leases include one or more options to renew, with renewal terms that can extend the lease term from one month to thirty years. The exercise of such lease renewal options is at the System's sole discretion. For purposes of calculating lease liabilities, lease terms include options to extend or terminate the lease when it is reasonably certain that the System will exercise that option. Certain leases also include options to purchase the leased asset. The depreciable life of assets and leasehold improvements is limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise.

The System does not separate lease and non-lease components except for certain medical equipment leases. Leases with a lease term of 12 months or less at commencement are not recorded on the consolidated balance sheets. Lease expense for these arrangements is recognized on a straight-line basis over the lease term.

Operating and finance leases consist of the following as of December 31, 2019:

Operating Leases

Operating lease assets	\$ 274,916
Other current liabilities	\$ 80,550
Operating lease liabilities, net of current portion	220,449
Total operating lease liabilities	<u>\$ 300,999</u>

Finance Leases

Property and equipment	\$ 49,837
Current maturities of long-term debt	\$ 6,935
Long-term debt, net of current maturities	41,623
Total finance lease liabilities	<u>\$ 48,558</u>

Lease expense for lease payments is recognized on a straight-line basis over the lease term. The components of lease expense for the year ended December 31, 2019 are as follows:

Operating lease expense	\$ 94,641
Variable lease expense	25,329
Short-term lease expense	20,254
Finance lease expense	
Amortization of lease assets	8,762
Interest on lease liabilities	3,703
Total lease expense	<u>\$ 152,689</u>

Lease term and discount rate as of December 31, 2019 are as follows:

Weighted-average remaining lease term:	
Operating leases	6.0 years
Finance leases	11.4 years
Weighted-average discount rate:	
Operating leases	2.5%
Finance leases	5.6%

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

The following table summarizes the maturity of lease liabilities under finance and operating leases for the next five years and the years thereafter, as of December 31, 2019:

	Operating Leases	Finance Leases	Total
2020	\$ 86,474	\$ 9,561	\$ 96,035
2021	68,674	9,031	77,705
2022	51,375	8,744	60,119
2023	35,873	7,430	43,303
2024	20,241	7,201	27,442
Thereafter	66,254	18,213	84,467
Total lease payments	328,891	60,180	\$ 389,071
Less: imputed interest	27,892	11,622	
Total lease liabilities	\$ 300,999	\$ 48,558	

Supplemental cash flow information related to leases for the year ended December 31, 2019 is as follows:

Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	\$ 92,318
Operating cash flows from finance leases	3,353
Financing cash flows from finance leases	9,765
Lease assets obtained in exchange for new operating lease liabilities	75,267
Lease assets obtained in exchange for new finance lease liabilities	5,732

8. Debt Obligations

Long-term debt consisted of the following:

	December 31, 2019	2018
Fixed-rate hospital revenue bonds, interest rates from 1.90% to 5.00%, payable through 2049	\$ 2,344,587	\$ 2,344,000
Variable-rate hospital revenue bonds, payable through 2039	437,670	462,240
Finance leases payable	48,558	53,182
Unamortized original issue premium, net	171,296	115,738
Deferred financing costs	(17,505)	(15,970)
	2,984,606	2,959,190
Less: current maturities	(55,711)	(101,536)
	\$ 2,928,895	\$ 2,857,654

Master Trust Indenture

Long-term debt has been issued primarily on a tax-exempt basis. Substantially all bonds are secured under a Master Trust Indenture (MTI), which provides for, among other things, the deposit of revenue with the master trustee in the event of certain defaults, pledges of accounts receivable, pledges not to encumber property, and limitations on additional borrowings. Certain affiliates controlled by Healthcare Corporation comprise the AdventHealth Obligated Group (Obligated Group).

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Members of the Obligated Group are jointly and severally liable under the MTI to make all payments required with respect to obligations under the MTI. The MTI requires certain covenants and reporting requirements be met by the System and the Obligated Group. At December 31, 2019 and 2018, the Obligated Group had total net assets of approximately \$10,536,000 and \$9,061,000, respectively.

Variable-Rate Bonds and Sources of Liquidity

Certain variable-rate bonds, including \$104,420 classified as short-term financings in the accompanying consolidated balance sheets, may be put to the System at the option of the bondholder. The variable-rate bond indentures generally provide the System the option to remarket the obligations at the then prevailing market rates for periods ranging from one day to the maturity dates. The obligations have been primarily marketed for seven-day periods during 2019, with annual interest rates ranging from 1.05% to 2.32%. Additionally, the System paid fees, such as remarketing fees, on variable-rate bonds during 2019.

The System has various sources of liquidity, including a \$500,000 revolving credit agreement (Revolving Note) with a syndicate of banks and a \$500,000 commercial paper program (CP Program). In the event any variable-rate bonds are put and not remarketed, the Revolving Note is available for liquidity and the System's obligation to the banks would be payable upon expiration of the Revolving Note. The Revolving Note, which expires in December 2023, is also available for letters of credit, liquidity facilities, and general corporate needs, including working capital, capital expenditures, and acquisitions and has certain prime rate and LIBOR-based pricing options. No amounts were outstanding under the Revolving Note as of December 31, 2019 and 2018. At December 31, 2019, the System had approximately \$1,100 committed to letters of credit under the Revolving Note. The System's CP Program allows for up to \$500,000 of taxable, commercial paper notes (CP Notes) to be issued for general corporate purposes at an interest rate to be determined at the time of issuance. No amounts were outstanding under the CP Program as of December 31, 2019 and 2018.

2019 Debt Transactions

During the third quarter of 2019, the System issued fixed-rate bonds (Fixed-Rate Bonds) at a net premium with par amounts totaling \$359,440, maturity dates ranging from 2037 to 2046, stated interest rates ranging from 3.00% to 5.00%, and effective interest rates ranging from 2.33% to 3.08% through the call date of 2029. The System also issued mandatory tender put bonds (Put Bonds) at a premium with par amounts totaling \$122,085. The Put Bonds have a stated interest rate of 5.00% through a mandatory redemption date of 2026 and a final maturity of 2049. The effective interest rate on the Put Bonds is 1.64% through the mandatory redemption date. The Fixed-Rate Bonds and Put Bonds were issued with premiums totaling \$68,487, which resulted in total proceeds of \$550,012. The System used \$403,646 of bond proceeds for repayment of fixed-rate bonds, which resulted in a loss on extinguishment of debt totaling \$7,625 in the accompanying consolidated statement of operations and changes in net assets. The System used the remaining bond proceeds to finance or refinance certain costs of the acquisition, construction, and equipping of certain facilities.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

2018 Debt Transactions

During the second quarter of 2018, the System deposited \$137,593 into irrevocable trusts for the advance repayments of existing fixed-rate bonds and the related interest obligations through the call dates. In accordance with GAAP, these bonds, along with the related trust assets, were excluded from the System's accompanying consolidated balance sheet as of December 31, 2018. These advance repayments resulted in a loss on extinguishment of debt totaling \$10,033 in the accompanying consolidated statement of operations and changes in net assets.

During the third quarter of 2018, the System issued fixed-rate bonds (2018 Fixed-Rate Bonds) at a premium with par amounts totaling \$257,055, a maturity date of 2048, stated interest rates ranging from 4.00% to 5.00%, and effective interest rates ranging from 3.41% to 3.78% through the call date of 2028. The System also issued mandatory tender put bonds (2018 Put Bonds) at a premium with par amounts totaling \$86,340. The 2018 Put Bonds have a stated interest rate of 5.00% through a mandatory redemption of 2025 and a final maturity date of 2048. The effective interest rate on the 2018 Put Bonds is 2.62% through the mandatory redemption date. The 2018 Fixed-Rate Bonds and 2018 Put Bonds were issued with premiums totaling \$31,614. The System used the bond proceeds to finance or refinance certain costs of the acquisition, construction, and equipping of certain facilities.

Debt Maturities

The following represents the maturities of long-term debt, excluding finance leases disclosed in Note 7, for the next five years and the years thereafter:

2020	\$	48,776
2021		62,668
2022		76,842
2023		77,973
2024		94,038
Thereafter		2,421,960

Cash paid for interest, net of amounts capitalized, approximated \$102,000 and \$98,000 during the years ended December 31, 2019 and 2018, respectively.

9. Retirement Plans

Defined Contribution Plans

The System participates with other Seventh-day Adventist healthcare entities in a defined contribution retirement plan (Plan) that covers substantially all full-time employees who are at least 18 years of age. The Plan is exempt from the Employee Retirement Income Security Act of 1974 (ERISA). The Plan provides, among other things, that the employer contribute 2.6% of wages, plus additional amounts for highly compensated employees. Additionally, the Plan provides that the employer match 50% of an employee's contributions up to 4% of the contributing employee's wages, resulting in a maximum available match of 2% of the contributing employee's wages each year.

Contributions to the Plan are included in employee compensation in the accompanying consolidated statements of operations and changes in net assets in the amount of \$152,850 and \$150,829 for the years ended December 31, 2019 and 2018, respectively.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Defined Benefit Plan – Multiemployer Plan

Prior to January 1, 1992, certain of the System's entities participated in a multiemployer, noncontributory, defined benefit retirement plan, the Seventh-day Adventist Hospital Retirement Plan Trust (Old Plan) administered by the General Conference of Seventh-day Adventists that is exempt from ERISA. The risks of participating in multiemployer plans are different from single-employer plans in the following aspects:

Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers.

If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.

If an entity chooses to stop participating in the multiemployer plan, it may be required to pay the plan an amount based on the underfunded status of the plan, referred to as withdrawal liability.

During 1992, the Old Plan was suspended, and the Plan was established. The System, along with the other participants in the Old Plan, may be required to make future contributions to the Old Plan to fund any difference between the present value of the Old Plan benefits and the fair value of the Old Plan assets. Future funding amounts and the funding time periods have not been determined by the Old Plan administrators; however, management believes the impact of any such future decisions will not have a material adverse effect on the System's consolidated financial statements

The most recent available plan asset and benefit obligation data for the Old Plan is as of December 31, 2018 and is as follows:

Total plan assets	\$ 552,021
Actuarial present value of accumulated plan benefits	599,672
Funded status	92.1%

The System did not make contributions to the Old Plan for the years ended December 31, 2019 or 2018.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

Defined Benefit Plan – Frozen Pension Plans

Certain of the System's entities sponsored noncontributory, defined benefit pension plans (Pension Plans) that have been frozen such that no new benefits accrue. The following table sets forth the remaining combined projected and accumulated benefit obligations and the assets of the Pension Plans at December 31, 2019 and 2018, the components of net periodic pension cost for the years then ended, and a reconciliation of the amounts recognized in the accompanying consolidated financial statements:

	Year Ended December 31,	
	2019	2018
Accumulated benefit obligation, end of year	<u>\$ 154,354</u>	<u>\$ 137,726</u>
Change in projected benefit obligation:		
Projected benefit obligation, beginning of year	\$ 137,726	\$ 170,731
Interest cost	6,021	6,299
Benefits paid	(7,635)	(6,953)
Actuarial losses (gains)	18,242	(14,675)
Settlements	—	(17,676)
Projected benefit obligation, end of year	<u>154,354</u>	<u>137,726</u>
Change in plan assets:		
Fair value of plan assets, beginning of year	117,643	152,376
Actual return on plan assets	21,945	(10,104)
Benefits paid	(7,635)	(6,953)
Settlements	—	(17,676)
Fair value of plan assets, end of year	<u>131,953</u>	<u>117,643</u>
Deficiency of fair value of plan assets over projected benefit obligation, included in other noncurrent liabilities	<u>\$ (22,401)</u>	<u>\$ (20,083)</u>

No plan assets are expected to be returned to the System during the fiscal year ending December 31, 2020.

Included in net assets without donor restrictions at December 31, 2019 and 2018 are unrecognized actuarial losses of \$25,435 and \$23,733, respectively, which have not yet been recognized in net periodic pension cost. None of the actuarial losses included in net assets without donor restrictions are expected to be recognized in net periodic pension cost during the year ending December 31, 2020.

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

Changes in plan assets and benefit obligations recognized in net assets without donor restrictions include:

	Year Ended December 31,	
	2019	2018
Net actuarial losses	\$ (2,021)	\$ (2,774)
Amortization of net actuarial losses	319	190
Impact of settlement	—	2,610
Total increase recognized in net assets without donor restrictions	<u>\$ (1,702)</u>	<u>\$ 26</u>

The components of net periodic pension cost were as follows:

	Year Ended December 31,	
	2019	2018
Interest cost	\$ 6,021	\$ 6,299
Expected return on plan assets	(5,724)	(7,345)
Recognized net actuarial losses	319	190
Net periodic pension cost (income)	<u>\$ 616</u>	<u>\$ (856)</u>

The assumptions used to determine the benefit obligation and net periodic pension cost for the Pension Plans are set forth below:

	Year Ended December 31,	
	2019	2018
Used to determine projected benefit obligation		
Weighted-average discount rate	3.35%	4.50%
Used to determine pension cost		
Weighted-average discount rate	4.50%	3.80%
Weighted-average expected long-term rate of return on plan assets	5.00%	5.00%

The Pension Plans' assets are invested in a portfolio designed to protect principal and obtain competitive investment returns and long-term investment growth, consistent with actuarial assumptions, with a reasonable and prudent level of risk. The Pension Plans' assets are managed solely in the interest of the participants and their beneficiaries. Diversification is achieved by allocating funds to various asset classes and investment styles and by retaining multiple investment managers with complementary styles, philosophies, and approaches.

The expected long-term rate of return on the Pension Plans' assets is based on historical and projected rates of return for current and planned asset categories and the target allocation in the investment portfolio. The target investment allocation for the Pension Plans during 2019 and 2018 was 70% debt securities, 27% equity securities, and 3% alternative investments.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

The following table presents the Pension Plans' financial instruments as of December 31, 2019, measured at fair value on a recurring basis by the valuation hierarchy defined in Note 12:

	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 2,479	\$ 2,479	\$ —	\$ —
Debt securities				
U.S. government agencies and sponsored entities	38,041	—	38,041	—
Corporate bonds	52,846	—	52,846	—
Equity securities				
Domestic equities	4,015	4,015	—	—
Foreign equities	2,516	2,516	—	—
Exchange traded funds				
Domestic equity	22,388	22,388	—	—
Foreign equity	4,398	4,398	—	—
Alternative strategy mutual funds	5,270	5,270	—	—
Total plan assets	<u>\$ 131,953</u>	<u>\$ 41,066</u>	<u>\$ 90,887</u>	<u>\$ —</u>

The following table presents the Pension Plans' financial instruments as of December 31, 2018, measured at fair value on a recurring basis by the valuation hierarchy defined in Note 12:

	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 2,937	\$ 2,937	\$ —	\$ —
Debt securities				
U.S. government agencies and sponsored entities	22,494	—	22,494	—
Corporate bonds	60,139	—	60,139	—
Equity securities				
Domestic equities	2,800	2,800	—	—
Foreign equities	2,889	2,889	—	—
Exchange traded funds				
Domestic equity	16,107	16,107	—	—
Foreign equity	5,548	5,548	—	—
Alternative strategy mutual funds	4,729	4,729	—	—
Total plan assets	<u>\$ 117,643</u>	<u>\$ 35,010</u>	<u>\$ 82,633</u>	<u>\$ —</u>

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

The following represents the expected benefit plan payments for the next five years and the five years thereafter:

2020	\$ 6,729
2021	7,045
2022	7,354
2023	7,728
2024	7,963
2025-2029	42,926

10. General and Professional Liability Program

The System has a self-insured revocable trust that covers its subsidiaries and their respective employees for professional and general liability claims within a specified level. A self-insured retention of \$2,000 was established for the year ended December 31, 2001 was increased to \$7,500 and \$15,000 effective January 1, 2002 and 2003, respectively, and has remained at \$15,000 through December 31, 2019. Claims above the self-insured retention are insured by claims-made coverage that is placed with Adhealth Limited (Adhealth), a Bermuda company. Adhealth has purchased reinsurance through commercial insurers for the excess limits of coverage.

The professional and general liability trust funds are recorded in the accompanying consolidated balance sheets as assets whose use is limited in the amount of \$459,451 and \$379,843 at December 31, 2019 and 2018, respectively. The related accrued claims are recorded in the accompanying consolidated balance sheets as other current liabilities in the amount of \$100,904 and \$103,799 and as other noncurrent liabilities in the amount of \$334,815 and \$347,512 at December 31, 2019 and 2018, respectively. These liabilities are based upon actuarially determined estimates using a discount rate of 3.75% at December 31, 2019 and 2018. The related estimated insurance recoveries are recorded as other assets in the amount of \$11,866 and \$13,629 in the accompanying consolidated balance sheets at December 31, 2019 and 2018, respectively.

11. Commitments and Contingencies

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. There is significant government activity within the healthcare industry with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Compliance with such laws and regulations can be subject to future review and interpretation, as well as regulatory actions unknown or unasserted at this time. Management assesses the probable outcome of unresolved litigation and investigations and records contingent liabilities reflecting estimated liability exposure.

In addition, certain of the System's affiliated organizations are involved in litigation and other regulatory investigations arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, these matters will be resolved without material adverse effect to the System's consolidated financial statements, taken as a whole.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

12. Fair Value Measurements

The System categorizes, for disclosure purposes, assets and liabilities measured at fair value, on a recurring basis, into a three-tier fair value hierarchy. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement, which should be determined based on assumptions that would be made by market participants.

In accordance with the Fair Value Measurement Topic of the ASC (ASC 820), investments that are valued using NAV as a practical expedient are excluded from this three-tier hierarchy. For all other investments measured at fair value, the hierarchy prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). Level inputs are defined as follows:

Level 1 – based on unadjusted quoted prices for identical assets or liabilities in an active market that the System has the ability to access.

Level 2 – based on pricing inputs that are either directly observable or that can be derived or supported from observable data as of the reporting date. Level 2 inputs may include quoted prices for similar assets or liabilities in non-active markets or pricing models whose inputs are observable for substantially the full term of the asset or liability.

Level 3 – based on prices or valuation techniques that require inputs that are both significant to the fair value of the financial asset or liability and are generally less observable from objective sources. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value. The System has no financial assets or financial liabilities with significant Level 3 inputs.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

Recurring Fair Value Measurements

The fair value of financial instruments measured at fair value on a recurring basis at December 31, 2019 was as follows:

	Total	Level 1	Level 2	Level 3
ASSETS				
<i>CASH AND CASH EQUIVALENTS</i>	\$ 184,811	\$ 184,811	\$ —	\$ —
<i>INVESTMENTS AND ASSETS WHOSE USE IS LIMITED</i>				
Cash and cash equivalents	318,254	318,254	—	—
Debt securities				
U.S. government agencies and sponsored entities	2,995,833	—	2,995,833	—
Foreign government agencies and sponsored entities	6,600	—	6,600	—
Corporate bonds	774,629	—	774,629	—
Mortgage backed	19,937	—	19,937	—
Other asset backed	35,719	—	35,719	—
Short-term investments	139,871	—	139,871	—
Exchange traded and mutual funds				
Domestic equity	784,563	784,563	—	—
Foreign equity	587,907	587,907	—	—
Fixed income	790,303	790,303	—	—
Real estate	18,560	18,560	—	—
	<u>6,472,176</u>	<u>2,499,587</u>	<u>3,972,589</u>	<u>—</u>
Total	<u>\$ 6,656,987</u>	<u>\$ 2,684,398</u>	<u>\$ 3,972,589</u>	<u>\$ —</u>

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

The fair value of financial instruments measured at fair value on a recurring basis at December 31, 2018 was as follows:

	Total	Level 1	Level 2	Level 3
ASSETS				
<i>CASH AND CASH EQUIVALENTS</i>	\$ 576,390	\$ 576,390	\$ —	\$ —
<i>INVESTMENTS AND ASSETS WHOSE USE IS LIMITED</i>				
Cash and cash equivalents	108,738	108,738	—	—
Debt securities				
U.S. government agencies and sponsored entities	2,574,221	—	2,574,221	—
Foreign government agencies and sponsored entities	5,944	—	5,944	—
Corporate bonds	745,545	—	745,545	—
Mortgage backed	44,018	—	44,018	—
Other asset backed	55,439	—	55,439	—
Short-term investments	130,315	—	130,315	—
Exchange traded and mutual funds				
Domestic equity	687,644	687,644	—	—
Foreign equity	532,048	532,048	—	—
Fixed income	549,195	549,195	—	—
Real estate	17,408	17,408	—	—
	<u>5,450,515</u>	<u>1,895,033</u>	<u>3,555,482</u>	<u>—</u>
Total	<u>\$ 6,026,905</u>	<u>\$ 2,471,423</u>	<u>\$ 3,555,482</u>	<u>\$ —</u>

The following tables represent a reconciliation of financial instruments at fair value to the accompanying consolidated balance sheets as follows:

	December 31,	
	2019	2018
Investments and assets whose use is limited measured at fair value	\$ 6,472,176	\$ 5,450,515
Alternative investments	1,020,101	837,274
Commingled funds	321,693	249,821
Accrued interest	13,369	15,134
Total	<u>\$ 7,827,339</u>	<u>\$ 6,552,744</u>
Investments	\$ 7,000,804	\$ 5,859,138
Assets whose use is limited:		
Current	381,119	333,888
Noncurrent	445,416	359,718
Total	<u>\$ 7,827,339</u>	<u>\$ 6,552,744</u>

Notes to Consolidated Financial Statements

For the years ended
December 31, 2019
and 2018
(dollars in thousands)

The fair values of the securities included in Level 1 were determined through quoted market prices. The fair values of Level 2 financial assets were determined as follows:

U.S. and foreign government agencies and sponsored entities, corporate bonds, mortgage backed, other asset backed, and short-term investments – These Level 2 securities were valued through the use of third-party pricing services that use evaluated bid prices adjusted for specific bond characteristics and market sentiment.

Other Fair Value Disclosures

The carrying values of accounts receivable, accounts payable, and accrued liabilities are reasonable estimates of their fair values, due to the short-term nature of these financial instruments.

The fair values of the System's fixed-rate bonds are estimated using Level 2 inputs based on quoted market prices for those or similar instruments. The estimated fair value of the fixed-rate bonds was approximately \$2,631,000 and \$2,440,000 as of December 31, 2019 and 2018, respectively. The carrying value of the fixed-rate bonds was approximately \$2,345,000 and \$2,344,000 as of December 31, 2019 and 2018, respectively. The carrying amount approximates fair value for all other long-term debt (Note 8).

13. Functional Expenses

The System's resources and activities are primarily related to providing healthcare services. Corporate services include certain administration, finance and accounting, human resources, legal, information technology, and other functions.

Expenses by functional classification for the year ended December 31, 2019 consist of the following:

	Healthcare Services	Corporate Services	Total
Employee compensation	\$ 5,426,611	\$ 360,965	\$ 5,787,576
Purchased services and professional fees	1,550,410	152,099	1,702,509
Supplies	1,985,342	5,645	1,990,987
Other	1,496,288	85,518	1,581,806
Total	<u>\$ 10,458,651</u>	<u>\$ 604,227</u>	<u>\$ 11,062,878</u>

Expenses by functional classification for the year ended December 31, 2018 consist of the following:

	Healthcare Services	Corporate Services	Total
Employee compensation	\$ 5,015,001	\$ 322,917	\$ 5,337,918
Purchased services and professional fees	1,375,479	128,736	1,504,215
Supplies	1,803,980	5,840	1,809,820
Other	1,461,385	76,527	1,537,912
Total	<u>\$ 9,655,845</u>	<u>\$ 534,020</u>	<u>\$ 10,189,865</u>

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

14. Subsequent Events

The System evaluated events and transactions occurring subsequent to December 31, 2019 through February 28, 2020, the date the accompanying consolidated financial statements were issued. During this period, other than those events noted below, there were no subsequent events that required recognition in the accompanying consolidated financial statements nor were there any additional nonrecognized subsequent events that required disclosure.

On January 3, 2020, the System acquired a minority interest in Health First, Inc. (Health First). Health First is a community based not-for-profit healthcare system located in Brevard County, Florida and includes hospitals, insurance plans, a multi-specialty medical group, and outpatient and wellness services. The fair value of the minority interest acquired totaled \$350,000. The System paid \$125,000 at closing and two remaining installments will be paid in 2021 and 2023.

On February 2, 2020, the System and CHRISTUS Santa Rosa Healthcare (CHRISTUS), a faith-based health system headquartered in Irving, Texas, signed an agreement whereby CHRISTUS would purchase substantially all of the assets of Central Texas Medical Center together with certain other affiliated assets (CTMC). The sale is expected to close in the first quarter of 2020. CTMC provides healthcare services to the San Marcos, Texas community and surrounding areas. Assets held for sale at December 31, 2019 were approximately \$32,500 and are included in other current assets in the accompanying consolidated balance sheet.

Notes to Consolidated Financial Statements

*For the years ended
December 31, 2019
and 2018
(dollars in thousands)*

15. Fourth Quarter Results of Operations (Unaudited)

The System's operating results for the three months ended December 31, 2019 are presented below:

Revenue	
Net patient service revenue	\$ 3,003,627
Other	115,577
Total operating revenue	<u>3,119,204</u>
Expenses	
Employee compensation	1,484,404
Supplies	521,317
Purchased services	256,884
Professional fees	190,111
Other	202,307
Interest	19,522
Depreciation and amortization	169,494
Total operating expenses	<u>2,844,039</u>
Income from Operations	275,165
Nonoperating Gain – Investment Return	<u>183,517</u>
Excess of revenue and gains over expenses	458,682
Noncontrolling interests	<u>(299)</u>
Excess of Revenue and Gains over Expenses Attributable to Controlling Interest	458,383
Other changes in net assets without donor restrictions, net	14,156
Decrease in net assets with donor restrictions, net	(10,121)
Increase in Net Assets	<u><u>\$ 462,418</u></u>

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Report of Independent Auditors

The Board of Directors
Adventist Health System Sunbelt Healthcare Corporation
d/b/a AdventHealth

We have audited the accompanying consolidated financial statements of Adventist Health System Sunbelt Healthcare Corporation (the System), which comprise the consolidated balance sheets as of December 31, 2019 and 2018, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity 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 financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the System at December 31, 2019 and 2018, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Orlando, Florida
February 28, 2020