

**Audited
Consolidated
Financial
Statements**

December 31, 2018

AdventHealth
(formerly Adventist Health System)

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Consolidated Balance Sheets

December 31, 2018
and 2017

(dollars in thousands)

ASSETS

Current Assets

Cash and cash equivalents	\$ 576,390	\$ 338,346
Investments	5,859,138	5,821,745
Current portion of assets whose use is limited	333,888	303,823
Patient accounts receivable, less allowance for uncollectible accounts of \$420,784 in 2017	581,568	478,091
Due from brokers	82,240	338,621
Estimated settlements from third parties	63,732	28,267
Other receivables	516,849	611,295
Inventories	234,253	221,960
Prepaid expenses and other current assets	109,322	121,427
	<u>8,357,380</u>	<u>8,263,575</u>

Property and Equipment

6,506,650 6,061,128

Assets Whose Use is Limited, net of current portion

359,718 398,005

Other Assets

752,942 745,143
\$ 15,976,690 \$ 15,467,851

LIABILITIES AND NET ASSETS

Current Liabilities

Accounts payable and accrued liabilities	\$ 1,216,499	\$ 1,099,159
Estimated settlements to third parties	175,334	189,781
Due to brokers	393,120	696,721
Other current liabilities	311,573	311,460
Short-term financings	104,420	179,420
Current maturities of long-term debt	101,536	104,708
	<u>2,302,482</u>	<u>2,581,249</u>

Long-Term Debt, net of current maturities

2,857,654 2,719,815

Other Noncurrent Liabilities

612,773 598,002
5,772,909 5,899,066

Net Assets

Net assets without donor restrictions	9,984,702	9,349,046
Net assets with donor restrictions	185,946	186,666
	<u>10,170,648</u>	<u>9,535,712</u>
Noncontrolling interests	33,133	33,073
	<u>10,203,781</u>	<u>9,568,785</u>

Commitments and Contingencies

\$ 15,976,690 \$ 15,467,851

Consolidated Statements of Operations and Changes in Net Assets

For the years ended
December 31, 2018
and 2017

(dollars in thousands)

	2018	2017
Revenue		
Patient service revenue		\$ 10,212,644
Provision for bad debts		(568,000)
Net patient service revenue	\$ 10,577,663	9,644,644
Other	396,461	438,481
Total operating revenue	10,974,124	10,083,125
Expenses		
Employee compensation	5,337,918	5,027,882
Supplies	1,809,820	1,671,024
Purchased services	868,384	765,073
Professional fees	650,620	563,299
Other	858,834	699,750
Interest	90,239	89,663
Depreciation and amortization	574,050	533,664
Total operating expenses	10,189,865	9,350,355
Income from Operations	784,259	732,770
Nonoperating (Losses) Gains		
Investment return	(155,564)	392,170
Loss on extinguishment of debt	(10,033)	(1,774)
Total nonoperating (losses) gains, net	(165,597)	390,396
Excess of revenue and gains over expenses and losses	618,662	1,123,166
Noncontrolling interests	(333)	702
Excess of Revenue and Gains over Expenses and Losses Attributable to Controlling Interest	618,329	1,123,868

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

For the years ended
December 31, 2018
and 2017

(dollars in thousands)

CONTROLLING INTEREST

Net Assets Without Donor Restrictions

	2018	2017
Excess of revenue and gains over expenses and losses	\$ 618,329	\$ 1,123,868
Net assets released from restrictions for purchase of property and equipment	25,961	24,669
Change in unrealized gains and losses on investments	(4,457)	8,337
Accumulated derivative losses reclassified into excess of revenue and gains over expenses and losses	—	6,019
Pension-related changes other than net periodic pension cost	26	1,161
Other	(4,203)	18,133
Increase in net assets without donor restrictions	635,656	1,182,187

Net Assets With Donor Restrictions

Investment return	691	2,838
Gifts and grants	37,840	32,476
Net assets released from restrictions for purchase of property and equipment or use in operations	(43,237)	(49,937)
Other	3,986	(168)
Decrease in net assets with donor restrictions	(720)	(14,791)

NONCONTROLLING INTERESTS

Net Assets Without Donor Restrictions

Excess (deficiency) of revenue and gains over expenses and losses	333	(702)
Distributions	(1,018)	(462)
Other	745	1,392
Increase in noncontrolling interests	60	228

Increase in Net Assets

Net assets, beginning of year	9,568,785	8,401,161
Net assets, end of year	<u>\$ 10,203,781</u>	<u>\$ 9,568,785</u>

Consolidated Statements of Cash Flows

For the years ended
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and 2017

(dollars in thousands)

	2018	2017
Operating Activities		
Increase in net assets	\$ 634,996	\$ 1,167,624
Provision for bad debts	—	568,000
Depreciation	569,465	529,232
Amortization of intangible assets	4,585	4,432
Amortization of deferred financing costs and original issue discounts and premiums	(9,161)	(9,417)
Loss on extinguishment of debt	10,033	1,774
Change in unrealized gains and losses on investments	239,391	(182,846)
Restricted gifts and grants and investment return	(38,531)	(35,314)
Income from unconsolidated entities	(59,303)	(57,682)
Distributions from unconsolidated entities	25,521	23,124
Pension-related changes other than net periodic pension cost	(26)	(1,161)
Changes in operating assets and liabilities:		
Patient accounts receivable	(103,477)	(548,464)
Other receivables	94,446	(49,566)
Other current assets	16,130	(38,536)
Accounts payable and accrued liabilities	114,570	108,057
Estimated settlements to third parties, net	(49,912)	4,863
Other current liabilities	(1,068)	(5,407)
Other noncurrent liabilities	14,797	(5,130)
Net cash provided by operating activities	1,462,456	1,473,583
Investing Activities		
Purchases of property and equipment, net	(879,353)	(792,974)
Cash paid for acquisitions, net of cash received	(150,149)	—
Sales and maturities of investments	3,028,615	5,603,674
Purchases of investments	(3,304,219)	(6,361,655)
Due from brokers	256,381	(97,868)
Due to brokers	(303,601)	53,482
Sales, maturities and uses of assets whose use is limited	256,484	633,060
Purchases of and additions to assets whose use is limited	(249,442)	(722,812)
Decrease (increase) in other assets	23,610	(21,499)
Net cash used in investing activities	(1,321,674)	(1,706,592)
Financing Activities		
Repayments of long-term borrowings	(242,341)	(338,905)
Additional long-term borrowings	379,269	239,471
Repayments of short-term borrowings	(206,000)	(76,580)
Additional short-term borrowings	131,000	75,000
Payment of deferred financing costs	(3,197)	(1,414)
Restricted gifts and grants and investment return	38,531	35,314
Net cash provided by (used in) financing activities	97,262	(67,114)
Increase (Decrease) in Cash and Cash Equivalents	238,044	(300,123)
Cash and cash equivalents at beginning of year	338,346	638,469
Cash and Cash Equivalents at End of Year	<u>\$ 576,390</u>	<u>\$ 338,346</u>

Notes to Consolidated Financial Statements

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1. Significant Accounting Policies

Reporting Entity

Adventist Health System Sunbelt Healthcare Corporation (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 was formerly known as Adventist Health System and, on January 2, 2019, as a part of a systemwide brand transformation, began operating as AdventHealth. No changes were made to the System's governance structure, ownership or not-for-profit status. The System's 43 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.

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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 balance sheets.

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 May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09). The FASB codified ASU 2014-09 in the FASB Accounting Standards Codification (ASC) as Topic 606 (ASC 606). The standard is a single, comprehensive revenue recognition model that requires revenue to be recognized in a manner depicting the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services. On January 1, 2018, the System adopted the new revenue recognition standard using a modified retrospective method of application to all contracts existing on January 1, 2018. The adoption of ASC 606 resulted in changes to the presentation for revenue related to uninsured or underinsured patients. Prior to the adoption of ASC 606, a significant portion of the System's provision for bad debts related to self-pay patients, as well as co-pay and deductibles owed by patients with insurance. Under ASC 606, the estimated uncollectable amounts due from these patients are generally considered implicit price concessions that are a direct reduction to net patient service revenue, rather than as a provision for bad debts. For the year ended December 31, 2018, the System recorded approximately \$575,000 of implicit price concessions as a direct reduction of net patient service revenue that would have been recorded as provision for bad debts prior to adoption of ASC 606. At December 31, 2018, the System recorded approximately \$467,000 as a direct reduction of patient accounts receivable that would have been reflected as allowance for uncollectable accounts prior to the adoption of ASC 606. Other than these changes in presentation, the adoption of ASC 606 did not have a material impact on the consolidated balance sheet or statement of operations and changes in net assets as of and for the year ended December 31, 2018. Expanded disclosures required by ASC 606 are included within Note 1.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities* (ASU 2016-14), which changes the presentation and disclosure requirements of not-for-profit entities. The System adopted the standard effective for the December 31, 2018 consolidated

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financial statements. The adoption results in the presentation of two classes of net assets, without donor restrictions and with donor restrictions, which were previously presented as unrestricted and temporarily restricted net assets, respectively. Additionally, ASU 2016-14 requires additional disclosures around liquidity, which have been included within Note 4.

Recent Accounting Guidance Not Yet Adopted

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows – 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. Management is currently evaluating the potential impact of this guidance, which will be effective for the System beginning in 2019.

In February 2016, the FASB issued ASU No. 2016-02, *Leases* (ASU 2016-02), its new standard on accounting for leases. ASU 2016-02 introduces a lease accounting model that requires an entity to recognize assets and liabilities arising from most leases, including both finance and operating leases. The recognition, measurement and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease and will be in a manner similar to the current accounting guidance. ASU 2016-02 will also require additional qualitative and quantitative lease disclosures. Upon adoption, the primary effect will be to record right-of-use assets and obligations for leases currently classified as operating leases. This guidance will be effective for the System beginning in 2019.

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 when 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.

As all the System's performance obligations relate to contracts with a duration of less than one year, the System elected to apply the optional exemption provided in ASC 606 and, therefore, 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.

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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 \$24,000 and \$9,000 for the years ended December 31, 2018 and 2017, 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 expected to be collected based on the System's 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 or payor's ability to pay are recognized as bad debt expense. With the adoption of ASC 606, bad debt expense is included within other expense in the accompanying consolidated statement of operations and changes in net assets, rather than as a deduction to arrive at revenue. Bad debt expense for the year ended December 31, 2018 was not material for the System.

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.

The composition of net patient service revenue by primary payor for the year ended December 31 is as follows:

	Year Ended December 31			
	2018		2017	
	Amount	%	Amount	%
Managed Care	\$ 5,408,252	51%	\$ 4,927,857	51%
Medicare	2,221,138	21	2,118,785	22
Managed Medicare	1,317,488	12	1,117,924	11
Medicaid	507,344	5	384,113	4
Managed Medicaid	473,556	5	456,363	5
Self-pay	137,863	1	168,828	2
Other	512,022	5	470,774	5
	<u>\$10,577,663</u>	<u>100%</u>	<u>\$ 9,644,644</u>	<u>100%</u>

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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	
	2018	2017
Charity Care Cost		
Cost of providing charity care services	<u>\$ 364,078</u>	<u>\$ 335,179</u>
Charity Care Funding		
Funds received to offset or subsidize charity care services (included in patient service revenue)	\$ 314,154	\$ 146,590
Funds paid into trusts (included in other expenses)	<u>(244,125)</u>	<u>(186,257)</u>
Net charity care funding received (paid)	<u>\$ 70,029</u>	<u>\$ (39,667)</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.

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. At December 31, 2018 and 2017, the System had \$185,946 and \$186,666, respectively, of net assets with donor restrictions that will become available for various programs and capital expenditures at the System's hospitals when time or purpose restrictions are met.

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Functional Expenses

The System does not present expense information by functional classification, because its resources and activities are primarily related to providing healthcare services. Further, since the System receives substantially all of its resources from providing healthcare services in a manner similar to a business enterprise, other indicators contained in the accompanying consolidated financial statements are considered important in evaluating how well management has discharged its stewardship responsibilities.

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.

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, 2018 or 2017.

Other investments may also include exchange-traded and over-the-counter derivative instruments 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 are 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

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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 \$360,000 and \$400,000 as of December 31, 2018 and 2017, respectively. The Bonds have a put date of December 2022 and a final maturity date of November 2027.

As of December 31, 2018 and 2017, 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 \$797,383 and \$894,366, 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 \$90,000 and \$100,000 at December 31, 2018 and 2017, 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 \$347,383 and \$394,366 at December 31, 2018 and 2017, respectively. These notes are included in other receivables in the accompanying consolidated balance sheets. Due to the nature of the patient accounts receivable sold, collectibility of the subordinated and parity notes is not significantly impacted by credit risk.

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 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. During 2017, the System performed a quantitative assessment of each reporting unit and, as a result, no impairment was recognized.

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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 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, 2018 and 2017.

NAHS also has temporary deductible differences of approximately \$53,000 and \$55,700 at December 31, 2018 and 2017, respectively, primarily as a result of net operating loss carryforwards. At December 31, 2018, NAHS had net operating loss carryforwards of approximately \$54,500, expiring beginning in 2022 through 2026. Deferred taxes have been provided for these amounts, resulting in a net deferred tax asset of approximately \$13,400 and \$14,100 at December 31, 2018 and 2017, 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, 2018 and 2017 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.

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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, 2018 and 2017.

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 will impact tax-exempt organizations, including revisions to taxes on unrelated business activities, excise taxes on compensation of certain employees, and various other provisions. The regulations necessary to implement the law have not yet been promulgated, and the ultimate outcome of these regulations and the impact to the System cannot be determined presently. The System will continue to review and assess the impact of the legislation to the consolidated financial statements, but does not expect that the impact will be significant.

Reclassifications

Certain reclassifications were made to the 2017 consolidated financial statements to conform to the classifications used in 2018. 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. Acquisitions

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.

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.

AdventHealth Ocala

On August 1, 2018, the System entered into an asset purchase agreement (the 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 Agreement 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.

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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
	<hr/> 144,268
Liabilities	
Accounts payable and accrued liabilities	\$ 2,421
Other current liabilities	1,110
Long-term debt	64
	<hr/> 3,595
Fair Value of Net Assets Acquired	<hr/> \$ 140,673 <hr/>

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 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.

The following pro forma combined results of operations present the acquisition as if it had occurred on January 1, 2017. 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 Ocala into the System and to incur certain one-time costs. The pro forma combined results of operations do not reflect these benefits or costs.

These combined results reflect the impact of amortizing the fair value adjustments to property and equipment as of January 1, 2017.

	Year Ended December 31	
	2018	2017
Pro forma revenue	\$ 11,137,328	\$ 10,343,986
Pro forma excess of revenue and gains over expenses and losses	614,397	1,099,758
Pro forma change in net assets without donor restrictions	628,201	1,153,940
Pro forma change in net assets with donor restrictions	(720)	(14,791)

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3. Investments and Assets Whose Use is Limited

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

	December 31	
	2018	2017
Debt securities		
U.S. government agencies and sponsored entities	\$ 2,574,221	\$ 2,610,430
Foreign government agencies and sponsored entities	5,944	5,082
Corporate bonds	745,545	779,207
Mortgage backed	44,018	43,253
Other asset backed	55,439	31,186
Short-term investments	130,315	242,184
Accrued interest	15,134	13,430
	<u>3,570,616</u>	<u>3,724,772</u>
Exchange traded and mutual funds		
Domestic equity	687,644	748,754
Foreign equity	532,048	543,951
Fixed income	549,195	289,740
Real estate	17,408	—
	<u>1,786,295</u>	<u>1,582,445</u>
Investments at NAV		
Alternative investments	837,274	824,827
Commingled funds	249,821	304,460
	<u>1,087,095</u>	<u>1,129,287</u>
Cash and cash equivalents – assets whose use is limited		
	<u>108,738</u>	<u>87,069</u>
	<u>6,552,744</u>	<u>6,523,573</u>
Less: assets whose use is limited	<u>(693,606)</u>	<u>(701,828)</u>
Investments	<u>\$ 5,859,138</u>	<u>\$ 5,821,745</u>

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Investment Derivatives

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

	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>

	December 31, 2017			
	Notional		Fair Value	
	Long	Short	Assets	Liabilities
Equity options	\$ 172	\$ (166)	\$ 172	\$ (166)
Interest rate swaps	991	(314)	991	(314)
Futures	307,724	(88,171)	—	—
Total derivative instruments, gross	<u>\$ 308,887</u>	<u>\$ (88,651)</u>	<u>\$ 1,163</u>	<u>\$ (480)</u>

The System posted collateral related to investment derivative instruments totaling \$18,731 and \$8,889 as of December 31, 2018 and 2017, 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, 2018 includes investments held under trust agreements, internally designated investments for employee retirement plans, and investments held by bond trustees to fund debt service. Amounts to be used for the payment of current liabilities are classified as current assets.

Indenture requirements of tax-exempt financings by the System provide for the establishment and maintenance of various accounts with trustees. These arrangements require the trustee to control the expenditure of debt proceeds, as well as the payment of interest and the repayment of debt to bondholders. Self-insurance trust funds are set aside to provide funds for settling payments under the professional and general liability program.

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

	December 31	
	2018	2017
Self-insurance trust funds	\$ 379,843	\$ 408,353
Employee benefits funds	213,629	200,505
Required bond funds held by bond trustees	2,695	2,846
Other	97,439	90,124
	<u>693,606</u>	<u>701,828</u>
Less: amounts to pay current liabilities	<u>(333,888)</u>	<u>(303,823)</u>
	<u>\$ 359,718</u>	<u>\$ 398,005</u>

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Investment Return and Unrealized Gains and Losses

Investment return from cash and cash equivalents, investments, and assets whose use is limited amounted to \$(155,564) and \$392,170 in the accompanying consolidated statements of operations and changes in net assets for the years ended December 31, 2018 and 2017, respectively, and consisted of the following:

	Year Ended December 31	
	2018	2017
Interest and dividend income	\$ 137,391	\$ 103,520
Net realized (losses) gains	(58,021)	114,141
Net change in unrealized gains and losses	(234,934)	174,509
	<u>\$ (155,564)</u>	<u>\$ 392,170</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 7.

The System had 232 and 240 days cash on hand at December 31, 2018 and 2017, 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	
	2018	2017
Cash and cash equivalents	\$ 576,390	\$ 338,346
Investments	5,859,138	5,821,745
Due to brokers, net	(310,880)	(358,100)
	<u>\$ 6,124,648</u>	<u>\$ 5,801,991</u>
Unrestricted days cash and investments on hand	<u>232</u>	<u>240</u>

The System's financial assets also consist of patient accounts receivable totaling \$581,568 and \$478,091 as of December 31, 2018 and 2017, respectively. Other receivables, totaling \$516,849 and \$611,295 as of December 31, 2018 and 2017, 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, employee benefit funds and required bond funds and are more fully described in Note 3.

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5. Property and Equipment

Property and equipment consists of the following:

	December 31	
	2018	2017
Land and improvements	\$ 846,989	\$ 801,473
Buildings and improvements	5,655,951	5,212,371
Equipment	5,243,306	4,901,130
	<u>11,746,246</u>	<u>10,914,974</u>
Less: allowances for depreciation	<u>(5,762,370)</u>	<u>(5,411,723)</u>
	5,983,876	5,503,251
Construction in progress	<u>522,774</u>	<u>557,877</u>
	<u>\$ 6,506,650</u>	<u>\$ 6,061,128</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 \$288,400 at December 31, 2018.

During periods of construction, interest costs are capitalized to the respective property accounts. Interest capitalized approximated \$7,400 and \$10,000 for the years ended December 31, 2018 and 2017, 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 \$9,900 and \$4,800 at December 31, 2018 and 2017, 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	
	2018	2017
Capitalized software costs	\$ 280,758	\$ 319,689
Less: accumulated amortization	<u>(167,792)</u>	<u>(195,799)</u>
Capitalized software costs, net	<u>\$ 112,966</u>	<u>\$ 123,890</u>

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

2019	\$ 15,963
2020	13,120
2021	11,584
2022	10,524
2023	9,413
Thereafter	52,362

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6. Other Assets

Other assets consisted of the following:

	December 31	
	2018	2017
Goodwill	\$ 182,177	\$ 178,358
Notes and other receivables	71,894	70,566
Interests in net assets of unconsolidated foundations	64,954	64,150
Investments in unconsolidated entities	370,622	336,226
Other noncurrent assets	63,295	95,843
	<u>\$ 752,942</u>	<u>\$ 745,143</u>

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

	Ownership Interest	December 31	
		2018	2017
Texas Health Huguley, Inc.	49%	\$ 93,696	\$ 84,256
Centura Health Corporation	35%	90,712	89,674
Premier Healthcare Alliance, LP	5%	129,887	104,486
Other	5% – 50%	56,327	57,810
		<u>\$ 370,622</u>	<u>\$ 336,226</u>

Income from unconsolidated entities, excluding Premier Healthcare Alliance, LP (Premier LP), totaled \$30,229 and \$33,152 for 2018 and 2017, 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 \$16,586 and \$11,296 for the years ended December 31, 2018 and 2017, respectively. Additionally, Premier LP equity method earnings totaled \$12,488 and \$13,234 and were recognized as a reduction to supplies expense for the years ended December 31, 2018 and 2017, respectively.

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7. Debt Obligations

Long-term debt consisted of the following:

	December 31	
	2018	2017
Fixed-rate hospital revenue bonds, interest rates from 1.90% to 7.25%, payable through 2048	\$ 2,344,000	\$ 2,212,222
Variable-rate hospital revenue bonds, payable through 2039	462,240	478,755
Capitalized leases payable	53,182	56,880
Unamortized original issue premium, net	115,738	92,422
Deferred financing costs	(15,970)	(15,756)
	2,959,190	2,824,523
Less: current maturities	(101,536)	(104,708)
	<u>\$ 2,857,654</u>	<u>\$ 2,719,815</u>

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). 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, 2018 and 2017, the Obligated Group had total net assets of approximately \$9,061,000 and \$8,494,000, 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 2018, with annual interest rates ranging from 0.93% to 1.81%. Additionally, the System paid fees, such as remarketing fees, on variable-rate bonds during 2018.

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 2024, 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, 2018 and 2017. At December 31, 2018, the System had approximately \$1,100 committed to letters of credit under the Revolving Note.

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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, 2018. As of December 31, 2017, the System had \$75,000 of CP Notes outstanding with an interest rate of 1.30% and maturities of less than 90 days.

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 (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 (Put Bonds) at a premium with par amounts totaling \$86,340. The 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 Put Bonds is 2.62% through the mandatory redemption date. The Fixed-Rate Bonds and 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.

2017 Debt Transactions

During the third quarter of 2017, the System issued variable-rate bonds with par amounts totaling \$238,500, mandatory redemption dates ranging from 2022 to 2024 and final maturity dates ranging from 2036 to 2039. The System used \$232,500 of the bond proceeds for the repayment of existing fixed-rate bonds, which resulted in a loss on extinguishment of debt totaling \$1,774 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.

Debt Maturities

The following represents the maturities of long-term debt for the next five years and thereafter:

2019	\$ 101,536
2020	109,404
2021	109,233
2022	116,067
2023	119,231
Thereafter	2,303,951

Cash paid for interest, net of amounts capitalized, approximated \$98,000 and \$94,000 during the years ended December 31, 2018 and 2017, respectively.

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8. 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 for the Plan are included in employee compensation in the accompanying consolidated statements of operations and changes in net assets in the amount of \$150,829 and \$138,896 for the years ended December 31, 2018 and 2017, respectively.

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, 2017 and is as follows:

Total plan assets	\$ 653,469
Actuarial present value of accumulated plan benefits	632,334
Funded status	103.3%

The System did not make contributions to the Old Plan for the years ended December 31, 2018 or 2017.

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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, 2018 and 2017, 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	
	2018	2017
Accumulated benefit obligation, end of year	<u>\$ 137,726</u>	<u>\$ 170,731</u>
Change in projected benefit obligation:		
Projected benefit obligation, beginning of year	\$ 170,731	\$ 163,649
Interest cost	6,299	6,988
Benefits paid	(6,953)	(10,348)
Actuarial (gains) losses	(14,675)	10,442
Settlements	<u>(17,676)</u>	<u>—</u>
Projected benefit obligation, end of year	137,726	170,731
Change in plan assets:		
Fair value of plan assets, beginning of year	152,376	134,404
Actual return on plan assets	(10,104)	18,020
Employer contributions	—	10,300
Benefits paid	(6,953)	(10,348)
Settlements	<u>(17,676)</u>	<u>—</u>
Fair value of plan assets, end of year	117,643	152,376
Deficiency of fair value of plan assets over projected benefit obligation, included in other noncurrent liabilities	<u>\$ (20,083)</u>	<u>\$ (18,355)</u>

No plan assets are expected to be returned to the System during the fiscal year ending December 31, 2019.

Included in net assets without donor restrictions at December 31, 2018 and 2017 are unrecognized actuarial losses of \$23,733 and \$23,759, 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, 2019.

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

	Year Ended December 31	
	2018	2017
Net actuarial (losses) gains	\$ (2,774)	\$ 892
Amortization of net actuarial losses	190	269
Impact of settlement	2,610	—
Total increase recognized in net assets without donor restrictions	\$ 26	\$ 1,161

The components of net periodic pension cost were as follows:

	Year Ended December 31	
	2018	2017
Interest cost	\$ 6,299	\$ 6,988
Expected return on plan assets	(7,345)	(6,686)
Recognized net actuarial losses	190	269
Net periodic pension (income) cost	\$ (856)	\$ 571

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	
	2018	2017
Used to determine projected benefit obligation		
Weighted-average discount rate	4.50%	3.80%
Used to determine pension cost		
Weighted-average discount rate	3.80%	4.40%
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 2018 and 2017 was 70% debt securities, 27% equity securities and 3% alternative investments.

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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 11:

	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>

The following table presents the Pension Plans' financial instruments as of December 31, 2017, measured at fair value on a recurring basis by the valuation hierarchy defined in Note 11:

	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 3,000	\$ 3,000	\$ —	\$ —
Debt securities				
U.S. government agencies and sponsored entities	27,675	—	27,675	—
Corporate bonds	76,730	—	76,730	—
Equity securities				
Domestic equities	3,114	3,114	—	—
Foreign equities	2,269	2,269	—	—
Exchange traded funds				
Domestic equity	22,972	22,972	—	—
Foreign equity	9,649	9,649	—	—
Alternative strategy mutual funds	6,967	6,967	—	—
Total plan assets	<u>\$ 152,376</u>	<u>\$ 47,971</u>	<u>\$ 104,405</u>	<u>\$ —</u>

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

2019	\$ 6,431
2020	6,760
2021	7,083
2022	7,404
2023	7,691
2024-2028	42,206

9. 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, 2018. 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 \$379,843 and \$408,353 at December 31, 2018 and 2017, respectively. The related accrued claims are recorded in the accompanying consolidated balance sheets as other current liabilities in the amount of \$103,799 and \$95,174 and as other noncurrent liabilities in the amount of \$360,608 and \$334,309 at December 31, 2018 and 2017, respectively. These liabilities are based upon actuarially determined estimates using a discount rate of 3.75% at December 31, 2018 and 2017. The related estimated insurance recoveries are recorded as other assets in the amount of \$13,629 and \$13,213 in the accompanying consolidated balance sheets at December 31, 2018 and 2017, respectively.

10. Commitments and Contingencies

Operating Leases

The System leases certain property and equipment under operating leases. Lease and rental expense was approximately \$135,300 and \$129,400 for the years ended December 31, 2018 and 2017, respectively, and is included in other expenses in the accompanying consolidated statements of operations and changes in net assets.

The following represents the net future minimum lease payments under noncancelable operating leases for the next five years and thereafter:

2019	\$ 60,509
2020	47,214
2021	37,813
2022	26,350
2023	16,426
Thereafter	25,297

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*For the years ended
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Compliance with Laws and Regulations

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.

The System is involved in litigation regarding certain related professional liability claims. Based on the information available to date, management believes that the System has adequately provided for the most likely outcome of this professional liability matter after considering applicable insurance coverage. However, as more information becomes known, it is possible that the estimate could change. As such, assurance cannot be given that the resolution of these matters will not affect the consolidated financial position, results of operations or cash flows of the System, taken as a whole.

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.

11. 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

Notes to Consolidated Financial Statements

For the years ended
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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.

Recurring Fair Value Measurements

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>

Notes to Consolidated Financial Statements

For the years ended
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The fair value of financial instruments measured at fair value on a recurring basis at December 31, 2017 was as follows:

	Total	Level 1	Level 2	Level 3
ASSETS				
<i>CASH AND CASH EQUIVALENTS</i>	\$ 338,346	\$ 318,071	\$ 20,275	\$ —
<i>INVESTMENTS AND ASSETS WHOSE USE IS LIMITED</i>				
Cash and cash equivalents	87,069	86,895	174	—
Debt securities				
U.S. government agencies and sponsored entities	2,610,430	—	2,610,430	—
Foreign government agencies and sponsored entities	5,082	—	5,082	—
Corporate bonds	779,207	—	779,207	—
Mortgage backed	43,253	—	43,253	—
Other asset backed	31,186	—	31,186	—
Short-term investments	242,184	—	242,184	—
Exchange traded funds				
Domestic equity	748,754	748,754	—	—
Foreign equity	543,951	543,951	—	—
Fixed income	289,740	289,740	—	—
	<u>5,380,856</u>	<u>1,669,340</u>	<u>3,711,516</u>	<u>—</u>
Total	<u>\$ 5,719,202</u>	<u>\$ 1,987,411</u>	<u>\$ 3,731,791</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	
	2018	2017
Investments and assets whose use is limited measured at fair value	\$ 5,450,515	\$ 5,380,856
Alternative investments	837,274	824,827
Commingled funds	249,821	304,460
Accrued interest	15,134	13,430
Total	<u>\$ 6,552,744</u>	<u>\$ 6,523,573</u>
Investments	\$ 5,859,138	\$ 5,821,745
Assets whose use is limited:		
Current	333,888	303,823
Noncurrent	359,718	398,005
Total	<u>\$ 6,552,744</u>	<u>\$ 6,523,573</u>

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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:

Cash equivalents, 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 \$2,440,000 and \$2,360,000 as of December 31, 2018 and 2017, respectively. The carrying value of the fixed-rate bonds was approximately \$2,344,000 and \$2,212,000 as of December 31, 2018 and 2017, respectively. The carrying amount approximates fair value for all other long-term debt (Note 7).

12. Subsequent Events

The System evaluated events and transactions occurring subsequent to December 31, 2018 through March 1, 2019, the date the accompanying consolidated financial statements were issued. During this period, there were no subsequent events that required recognition in the accompanying consolidated financial statements. Additionally, there were no nonrecognized subsequent events that required disclosure.

Notes to Consolidated Financial Statements

*For the years ended
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(dollars in thousands)*

13. Fourth Quarter Results of Operations (Unaudited)

The System's operating results for the three months ended December 31, 2018 are presented below:

Revenue	
Net patient service revenue	\$ 2,750,721
Other	98,995
Total operating revenue	<u>2,849,716</u>
Expenses	
Employee compensation	1,377,730
Supplies	475,816
Purchased services	278,756
Professional fees	138,697
Other	243,079
Interest	23,072
Depreciation and amortization	151,642
Total operating expenses	<u>2,688,792</u>
Income from Operations	160,924
Nonoperating Losses	
Investment return	(169,672)
Loss on extinguishment of debt	(241)
Total nonoperating losses	<u>(169,913)</u>
Deficiency of revenue and gains over expenses and losses	(8,989)
Noncontrolling interests	<u>(104)</u>
Deficiency of Revenue and Gains over Expenses and Losses	
Attributable to Controlling Interest	(9,093)
Other changes in net assets without donor restrictions, net	21,013
Decrease in net assets with donor restrictions, net	(17,918)
Decrease in Net Assets	<u><u>\$ (5,998)</u></u>

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, 2018 and 2017, 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, 2018 and 2017, 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
March 1, 2019