

# Advocate Aurora Health, Inc.

Condensed Consolidated Financial Statements and Other Information

As of and for the Three Months Ended March 31, 2022



**ADVOCATE AURORA HEALTH, INC.**  
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**ADVOCATE AURORA HEALTH, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(in thousands)

	Unaudited	Note 1
	March 31, 2022	December 31, 2021
Assets		
Current assets		
Cash and cash equivalents	\$ 763,163	\$ 703,725
Assets limited as to use	139,740	139,742
Patient accounts receivable	1,885,662	1,816,705
Other current assets	805,876	706,253
Third-party payors receivables	20,845	22,154
Collateral proceeds under securities lending program	13,622	18,550
Total current assets	3,628,908	3,407,129
Assets limited as to use	11,345,829	12,394,605
Property and equipment, net	5,926,824	5,943,011
Other assets		
Goodwill and intangible assets, net	260,796	271,178
Investments in unconsolidated entities	255,689	259,127
Reinsurance receivable	81,100	42,100
Operating lease right-of-use assets	287,762	283,398
Other noncurrent assets	533,406	538,013
Total other assets	1,418,753	1,393,816
<b>Total assets</b>	<b>\$ 22,320,314</b>	<b>\$ 23,138,561</b>

(Continued)

**ADVOCATE AURORA HEALTH, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(in thousands)

	Unaudited	Note 1
	March 31, 2022	December 31, 2021
Current liabilities		
Long-term debt and commercial paper, current portion	\$ 95,257	\$ 96,185
Long-term debt subject to short-term financing arrangements	115,970	166,350
Operating lease liabilities, current portion	73,417	68,247
Accrued salaries and employee benefits	963,277	1,296,458
Accounts payable and other accrued liabilities	1,321,521	1,562,089
Third-party payors payables	355,723	354,186
Accrued insurance and claims costs, current portion	151,230	151,230
Collateral under securities lending program	13,622	18,550
Total current liabilities	3,090,017	3,713,295
Noncurrent liabilities		
Long-term debt, less current portion	3,341,196	3,298,508
Operating lease liabilities, less current portion	246,791	248,062
Accrued insurance and claims cost, less current portion	632,454	615,576
Accrued losses subject to insurance recovery	81,100	42,100
Obligations under swap agreements	67,966	91,217
Other noncurrent liabilities	787,921	798,824
Total noncurrent liabilities	5,157,428	5,094,287
<b>Total liabilities</b>	<b>8,247,445</b>	<b>8,807,582</b>
Net assets		
Without donor restrictions		
Controlling interest	13,669,912	13,911,862
Noncontrolling interests in subsidiaries	157,934	167,440
Total net assets without donor restrictions	13,827,846	14,079,302
With donor restrictions	245,023	251,677
<b>Total net assets</b>	<b>14,072,869</b>	<b>14,330,979</b>
<b>Total liabilities and net assets</b>	<b>\$ 22,320,314</b>	<b>\$ 23,138,561</b>

*Note 1: The financial statement information was derived from and should be read in conjunction with the Advocate Aurora Health, Inc. audited financial statements as of and for the year ended December 31, 2021 and 2020, available on the Electronic Municipal Market Access website ([www.emma.msrb.org](http://www.emma.msrb.org))*

See accompanying notes to condensed consolidated financial statements.

**ADVOCATE AURORA HEALTH, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS**  
(in thousands)

	Unaudited		Note 1
	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
<b>Revenue</b>			
Patient service revenue	\$ 2,991,082	\$ 2,716,852	\$ 11,702,581
Capitation revenue	300,397	304,968	1,196,109
Other revenue	274,366	246,601	1,163,442
Total revenue	3,565,845	3,268,421	14,062,132
<b>Expenses</b>			
Salaries, wages and benefits	2,083,217	1,837,363	7,665,848
Supplies, purchased services and other	1,152,364	1,063,365	4,530,877
Contracted medical services	150,781	135,721	564,586
Depreciation and amortization	142,190	139,885	563,409
Interest	27,408	27,856	106,101
Total expenses	3,555,960	3,204,190	13,430,821
<b>Operating income before nonrecurring expenses</b>	<b>9,885</b>	<b>64,231</b>	<b>631,311</b>
Nonrecurring expenses	7,380	13,284	37,759
<b>Operating income</b>	<b>2,505</b>	<b>50,947</b>	<b>593,552</b>
<b>Nonoperating (loss) income</b>			
Investment (loss) income, net	(265,968)	295,725	1,303,546
Loss on debt refinancing	(33)	—	(14,468)
Change in fair value of interest rate swaps	23,250	27,338	27,403
Other nonoperating (loss) income, net	(2,362)	(4,516)	12,220
Total nonoperating (loss) income, net	(245,113)	318,547	1,328,701
Revenue (less than) in excess of expenses	(242,608)	369,494	1,922,253
Less income attributable to noncontrolling interests	(10,619)	(17,742)	(73,130)
<b>Revenue (less than) in excess of expenses - attributable to controlling interest</b>	<b>\$ (253,227)</b>	<b>\$ 351,752</b>	<b>\$ 1,849,123</b>

(Continued)

**ADVOCATE AURORA HEALTH, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS**  
(in thousands)

	Unaudited		Note 1
	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
<b>Net assets without donor restrictions, controlling interest</b>			
Revenue (less than) in excess of expenses - attributable to controlling interest	\$ (253,227)	\$ 351,752	\$ 1,849,123
Pension-related changes other than net periodic pension costs	1,810	3,301	48,236
Net assets released from restrictions for purchase of property and equipment	1,440	4,088	9,709
Other, net	8,027	320	(7,925)
(Decrease) increase in net assets without donor restrictions, controlling interest	(241,950)	359,461	1,899,143
<b>Net assets without donor restrictions, noncontrolling interests</b>			
Revenues in excess of expenses	10,619	17,742	73,130
Distributions to noncontrolling interests	(20,125)	(23,084)	(60,335)
(Decrease) increase in net assets without donor restrictions, noncontrolling interests	(9,506)	(5,342)	12,795
<b>Net assets with donor restrictions</b>			
Contributions	1,060	3,354	18,693
Investment (loss) income, net	(3,428)	5,042	21,106
Net assets released from restrictions for operations	(2,833)	(2,331)	(11,102)
Net assets released from restrictions for purchase of property and equipment	(1,440)	(4,088)	(9,709)
Other, net	(13)	141	9
(Decrease) increase in net assets with donor restrictions	(6,654)	2,118	18,997
<b>(Decrease) increase in net assets</b>	<b>(258,110)</b>	<b>356,237</b>	<b>1,930,935</b>
Net assets at beginning of period	14,330,979	12,400,044	12,400,044
<b>Net assets at end of period</b>	<b>\$ 14,072,869</b>	<b>\$ 12,756,281</b>	<b>\$ 14,330,979</b>

*Note 1: The financial statement information was derived from and should be read in conjunction with the Advocate Aurora Health, Inc. audited financial statements as of and for the years ended December 31, 2021 and 2020, available on the Electronic Municipal Market Access website ([www.emma.msrb.org](http://www.emma.msrb.org))*

See accompanying notes to condensed consolidated financial statements.

**ADVOCATE AURORA HEALTH, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)

	Unaudited		Note 1
	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
<b>Cash flows from operating activities</b>			
(Decrease) increase in net assets	\$ (258,110)	\$ 356,237	\$ 1,930,935
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Depreciation, amortization and accretion	139,719	137,862	555,983
Amortization of operating lease right-of-use assets	18,921	17,013	79,398
Loss on debt refinancing	33	—	14,468
Loss (gain) on sale of property and equipment	424	105	(13,117)
Change in fair value of swap agreements	(23,250)	(27,338)	(27,403)
Pension-related changes other than net periodic pension cost	(1,810)	(3,301)	(48,236)
Net assets released from restrictions for operations	(2,833)	(2,331)	(11,102)
Distribution to noncontrolling interests	20,125	22,957	60,335
Distributions from unconsolidated entities	16,999	2,724	11,442
Changes in operating assets and liabilities			
Trading securities, net	1,054,312	30,090	(1,330,868)
Accounts receivable, net	(68,957)	18,424	(245,966)
Accounts payable and accrued liabilities	(584,208)	(158,689)	(56,718)
Third-party payors receivable and payable, net	2,846	34,005	30,163
Other assets and liabilities, net	(79,376)	(49,180)	(342,705)
Net cash provided by operating activities	<u>234,835</u>	<u>378,578</u>	<u>606,609</u>
<b>Cash flows from investing activities</b>			
Capital expenditures	(129,581)	(127,070)	(570,166)
Proceeds from sale of property and equipment	658	80	2,019
Purchases of investments designated as non-trading, net	(234)	(221)	4
Investments in unconsolidated entities, net	(17,383)	(13,975)	(38,021)
Acquisition of Senior Helpers, net of cash acquired	—	—	(183,672)
Other	(435)	(164)	(2,879)
Net cash used in investing activities	<u>(146,975)</u>	<u>(141,350)</u>	<u>(792,715)</u>
<b>Cash flows from financing activities</b>			
Proceeds from issuance of debt	—	—	182,157
Repayments of long-term debt	(5,929)	(4,599)	(231,668)
Distribution to noncontrolling interests	(20,125)	(22,957)	(60,335)
Proceeds from restricted contributions and income on investments	(2,368)	8,396	39,799
Net cash used in financing activities	<u>(28,422)</u>	<u>(19,160)</u>	<u>(70,047)</u>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>59,438</b>	<b>218,068</b>	<b>(256,153)</b>
Cash and cash equivalents at beginning of period	703,725	959,878	959,878
<b>Cash and cash equivalents at end of period</b>	<b><u>\$ 763,163</u></b>	<b><u>\$ 1,177,946</u></b>	<b><u>\$ 703,725</u></b>
<b>Supplemental disclosures of noncash information</b>			
Operating lease right-of-use assets in exchange for new operating lease liabilities	\$ 21,885	\$ 634	\$ 46,016

*Note 1: The financial statement information was derived from and should be read in conjunction with the Advocate Aurora Health, Inc. audited financial statements as of and for the years ended December 31, 2021 and 2020, available on the Electronic Municipal Market Access website ([www.emma.msrb.org](http://www.emma.msrb.org)).*

See accompanying notes to condensed consolidated financial statements.

**ADVOCATE AURORA HEALTH, INC.**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2022**  
**(in thousands)**

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**1. ORGANIZATION AND BASIS OF PRESENTATION**

**Description of Business**

Advocate Aurora Health, Inc. is a Delaware nonprofit corporation (the "Parent Corporation"). The Parent Corporation is the sole corporate member of Advocate Health Care Network, an Illinois not-for-profit corporation ("Advocate") and Aurora Health Care, Inc., a Wisconsin nonstock not-for-profit corporation ("Aurora"). The Parent Corporation, Advocate, Aurora and their controlled subsidiaries are collectively referred to herein as the "System." The System was formed in furtherance of the parties' common and unifying charitable health care mission to promote and improve the quality and expand the scope and accessibility of affordable health care and health care-related services for the communities they serve.

The System is comprised of various not-for-profit and for-profit entities, the primary activities are the delivery of health care services or the provision of goods and services ancillary thereto.

The System provides a continuum of care through its 25 acute care hospitals, an integrated children's hospital and a psychiatric hospital, primary and specialty physician services, outpatient centers, physician office buildings, pharmacies, rehabilitation and home health and hospice care in northern Illinois and eastern Wisconsin.

**Basis of Presentation**

The accompanying condensed consolidated financial statements as of and for the three months ended March 31, 2022, have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim reporting. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included in these financial statements. Included in the System's accompanying condensed consolidated financial statements are all of its controlled subsidiaries. All significant intercompany transactions have been eliminated in consolidation. The accompanying condensed consolidated financial statements do not include all the information and footnotes required by GAAP for complete financial statements. As such the accompanying condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements as of and for the year ended December 31, 2021. The audited consolidated financial statements are available from the Municipal Securities Rulemaking Board ("MSRB") on its Electronic Municipal Market Access ("EMMA") system, found at <http://emma.msrb.org>. Additional information can be found in the investor relations section of the System's website at <https://www.advocateaurorahealth.org/investor-relations>.

Operating results for the three months ended March 31, 2022 are not necessarily indicative of the results that may be experienced during the year ending December 31, 2022.

**2. SIGNIFICANT EVENTS**

Due to the COVID-19 pandemic, the behavior of businesses and people globally was altered in a manner that had a negative impact on global and local economies including significant investment market volatility, various temporary business closures resulting in increased unemployment and other



effects which have and could continue to result in supply disruptions, lower collections on patient accounts receivable and/or decisions to defer medical treatments at the System's facilities.

The continuing and total impact of the COVID-19 pandemic on the System is difficult to predict and could adversely impact the business, investment portfolio, financial condition or results of operations and, accordingly, may have a material adverse impact on the financial condition of the System. The System continues to monitor liquidity and cash flow and has taken, and continues to take, steps to protect its fiscal health, including a focus on maintaining liquidity to meet its obligations. In addition, the System applied for certain COVID-19 related resources, including supplies, financial support, payroll tax deferrals and relief and other assistance made available through local, state and federal governments.

The System received \$0 for the three months ended March 31, 2022 and 2021, respectively, and \$34,354 for the year ended December 31, 2021 in grant payments from the U.S. Department of Health and Human Services ("HHS") from the Provider Relief Fund established under the Coronavirus Aid, Relief and Economic Security Act ("CARES Act"), which has been recognized as revenue and included in other operating revenue within the accompanying condensed consolidated statement of operations and changes in net assets. Payments from the Provider Relief Fund are intended to cover unreimbursed healthcare related expenses and lost revenue from patient care attributed to COVID-19 and are not required to be repaid provided the recipient attests to and complies with the terms and conditions of the grant funds. Management of the System believes that the System is in compliance with the terms and conditions of the Provider Relief Fund distributions and will continue to monitor compliance. The CARES Act also entitled eligible employers to an employee retention tax credit designed to encourage employers to keep employees on their payroll. The refundable tax credit is limited to 50% of up to \$10 in qualified wages paid to each employee by an eligible employer whose business had been financially impacted by COVID-19. The System recognized \$0 for the three months ended March 31, 2022 and 2021 and \$37,060 for the year ended December 31, 2021 for the employee retention tax credit, which is included in other operating revenue within the accompanying condensed consolidated statement of operations and changes in net assets and a corresponding receivable that is included in other current assets in the accompanying condensed consolidated balance sheets. The recognition of the COVID-19 support falls under the grant accounting guidance of accounting principles generally accepted in the United States. This guidance requires all significant terms and conditions to have been met for recognition to occur. Management of the System will continue to monitor compliance with the terms and conditions of the CARES Act grant funds and the impact of the pandemic on the System's revenues and expenses.

In addition, the System received \$773,000 for the year ended December 31, 2020 from the Centers for Medicare and Medicaid Services ("CMS") as an advance payment for Medicare services. The funds were provided through the expansion of the Medicare Accelerated and Advance Payment Program to ensure providers and suppliers had the resources needed to combat the COVID-19 pandemic. The advances are being recouped by withholding future Medicare fee-for-service payments for claims until the full accelerated payment has been recouped, unless the System elects to repay the advances prior to full recoupment. Subsequent to the twenty-nine month recoupment period any unpaid remaining balance is subject to an interest charge of 4 percent per annum. For the year ended December 31, 2021, CMS payments of approximately \$257,000 were recouped. During the three months ended March 31, 2022, approximately \$102,000 of additional CMS payments have been recouped. Medicare accelerated and advance payments of approximately \$414,000 and \$516,000 are included in accounts payable and other accrued liabilities within the accompanying condensed consolidated balance sheets at March 31, 2022 and December 31, 2021, respectively. The CARES Act also permitted employers to defer the employer portion of social security taxes through December 31, 2020. Employers are required to remit one-half of the amount deferred by December 31, 2021 and the remaining half by

December 31, 2022. During 2020 the System deferred approximately \$215,000 of these taxes and approximately \$107,500 were remitted during 2021. At March 31, 2022 and December 31, 2021, approximately \$107,500 is included in accrued salaries and employee benefits within the accompanying condensed consolidated balance sheets which will be remitted in 2022 to fulfill this payment obligation.

Additionally, the System was awarded approximately \$17,700 in Federal American Rescue Plan Act funds by the Illinois Department of Healthcare and Family Services. These funds are meant to cover premium pay and payroll and benefit expenses for employees who spent time mitigating or responding to COVID-19 from March 2021 through June 30, 2022. For the three months ended March 31, 2022 and 2021, respectively, approximately \$12,800 and \$0 of these funds were recognized as revenue and for the year ended December 31, 2021, approximately \$4,900 of these funds were recognized as revenue and included in other operating revenue within the accompanying condensed consolidated statement of operations and changes in net assets.

On April 1, 2021, the System purchased the stock of SH Corporate Company, Inc. and SHF Acquisition Company, Inc. (collectively "Senior Helpers") for \$183,672, net of cash acquired, to further the System's strategy. The System acquired the following significant assets: \$101,459 of goodwill and \$96,200 of intangible assets. Total 2021 revenue and operating loss from the date of acquisition of \$26,488 and \$9,543, respectively, were included in the accompanying condensed consolidated statements of operations and changes in net assets. The 2021 related changes in net assets without donor restrictions of \$(9,517) from the date of acquisition is included in the accompanying condensed consolidated balance sheets.

### **3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Use of Estimates**

The preparation of the accompanying condensed consolidated financial statements in conformity with GAAP requires management to make estimates, assumptions and judgments that affect the reported amounts of assets, liabilities and amounts disclosed in the notes to the condensed consolidated financial statements at the date of the condensed consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Although estimates are considered to be fairly stated at the time made, actual results could differ materially from those estimates.

#### **Cash Equivalents**

The System considers all highly liquid investments with a maturity of three months or less when purchased, other than those included in the investment portfolio, to be cash equivalents.

#### **Investments**

The System has designated substantially all of its investments as trading. Investments in debt and equity securities with readily determinable fair values are measured at fair value using quoted market prices or otherwise observable inputs. Investments in private equity limited partnerships and derivative products (hedge funds) are reported at fair value using net asset value as a practical expedient. Commingled funds are carried at fair value based on other observable inputs. Investment income or loss (including realized gains and losses, interest, dividends and unrealized gains and losses) is included in the nonoperating section of the accompanying condensed consolidated statements of operations and changes in net assets, unless the income or loss is restricted by donor or law or is related to assets

designated for self-insurance programs. Investment income or loss on self-insurance trust funds is reported in other revenue in the accompanying condensed consolidated statements of operations and changes in net assets. Investment income or loss that is restricted by donor or law is reported as a change in net assets with donor restrictions.

#### **Assets Limited as to Use**

Assets limited as to use consist of investments set aside by the System for future capital improvements and certain medical education and other health care programs. The System retains control of these investments and may, at its discretion, subsequently use them for other purposes. Additionally, assets limited as to use include investments held by trustees or in trust under debt agreements, self-insurance trusts, assets held in reinsurance trust accounts and donor-restricted funds.

#### **Patient Service Revenue and Accounts Receivable**

Patient service revenue is reported at the amount that reflects the consideration to which the System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including managed care payors and government programs and excludes revenues for services provided to patients under capitated arrangements) and others and include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews and investigations. Generally, patients and third-party payors are billed within days after the services are performed or after discharge. Revenue is recognized as performance obligations are satisfied. Provisions for third-party payor settlements and adjustments are estimated in the period the related services are provided and adjusted in future periods as additional information becomes available and final settlements are determined.

As the System's performance obligations relate to contracts with a duration of less than one year, the System has applied the optional exemption provided in the guidance and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

The System does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component, due to the expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less.

The System has entered into payment arrangements with patients that allow for payments over a term in excess of one year. The System has evaluated historical collections in excess of one year and current market interest rates to determine whether a significant financing component exists that would require an adjustment to the promised amount of consideration from patients and third-party payors. The System has determined that the impact of implicit financing arrangements for payment agreements in excess of one year is insignificant to the accompanying condensed consolidated statements of operations and changes in net assets.

The System does not incur significant incremental costs in obtaining contracts with patients. Any costs incurred are expensed in the period of occurrence, as the amortization period of any asset that the System would have recognized is one year or less in duration.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is a possibility that recorded estimates will change by a material amount.

### **Inventories**

Inventories, consisting primarily of medical supplies, pharmaceuticals and durable medical equipment, are stated at the lower of cost or net realizable value.

### **Reinsurance Receivables**

Reinsurance receivables are recognized in a manner consistent with the liabilities relating to the underlying reinsured contracts.

### **Goodwill and Intangible Assets, Net**

Goodwill of \$147,537 and \$151,655 is included in goodwill and intangible assets, net in the accompanying condensed consolidated balance sheets at March 31, 2022 and December 31, 2021, respectively. As described in Note 2. SIGNIFICANT EVENTS, the System recognized \$101,459 of goodwill related to the stock purchase of Senior Helpers. The System has elected to amortize goodwill prospectively using the straight-line method over a 10-year period in accordance with Accounting Standards Update ("ASU") 2019-06. Goodwill amortization is included in depreciation and amortization in the accompanying condensed consolidated statements of operations and changes in net assets. Goodwill amortization expense is as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Goodwill amortization	\$ 4,525	\$ 2,925	\$ 16,483

Intangible assets with expected useful lives are amortized over that period.

### **Asset Impairment**

The System considers whether indicators of impairment are present and, if indicators are present, performs the necessary tests to determine if the carrying value of an asset is recoverable. Impairment write-downs are recognized in the accompanying condensed consolidated statements of operations and changes in net assets as a component of operating expense at the time the impairment is identified. There were no material impairment charges recorded for the three months ended March 31, 2022 and the year ended December 31, 2021.

### **Property and Equipment, Net**

Property and equipment are reported at cost or, if donated, at fair value at the date of the gift. Costs of computer software developed or obtained for internal use, including external and internal direct costs of materials and labor directly associated with internal-use software development projects, are capitalized during the application development stage and included in property and equipment. Internal labor and interest expense incurred during the period of construction of significant capital projects are capitalized as a component of costs of the asset.

Property and equipment capitalized under direct financing leases are recorded at the present value of future lease payments, adding initial direct costs and prepaid lease payments, reduced by any lease incentives. Property and equipment capitalized under direct financing leases are amortized using the

straight-line method over the related lease term. Amortization of property and equipment under financing leases is included in the accompanying condensed consolidated statements of operations and changes in net assets in depreciation and amortization expense.

Property and equipment are depreciated on the straight-line method over a period ranging from 3 years to 80 years.

### **Operating Lease Right-of-use Assets**

The System records an operating lease right-of-use asset (an asset that represents the System's right to use the leased asset for the lease term) for leases that do not meet the criteria as a sales-type lease or a direct financing lease.

The System records operating lease right-of-use assets at the present value of future lease payments, adding initial direct costs and prepaid lease payments, reduced by any lease incentives. Operating lease right-of-use assets are amortized using the straight-line method over the related lease term. Amortization of operating lease right-of-use assets is included in the accompanying condensed consolidated statements of operations and changes in net assets in supplies, purchased services and other expense.

Included within operating lease right-of-use assets are assets that the System previously sold and then leased back. Those sale/leaseback transactions, which related to various administrative and medical support buildings, did not meet the accounting criteria as a sales-type lease or a direct financing lease. The buyer-lessors for such transactions are generally unrelated special-purpose entities.

### **Investments in Unconsolidated Entities**

Investments in unconsolidated entities are accounted for using the equity method or as an equity security without a readily determinable fair value. The System applies the equity method of accounting for investments in unconsolidated entities when its ownership or membership interest is 50% or less and the System has the ability to exercise significant influence over the operating and financial policies of the investee. The income (loss) on these unconsolidated entities is included in other revenue in the accompanying condensed consolidated statements of operations and changes in net assets. All other unconsolidated entities are accounted for as an equity security without a readily determinable fair value. These unconsolidated entities are initially recorded at cost, tested for impairment at least annually and adjusted as market transactions occur that would indicate a fair value adjustment is needed. The income (loss) on these unconsolidated entities is included in nonoperating (loss) income in the accompanying condensed consolidated statements of operations and changes in net assets.

### **Derivative Financial Instruments**

The System enters into transactions to manage its interest rate, credit and market risks. Derivative financial instruments, including exchange-traded and over-the-counter derivative contracts and interest rate swaps, are recorded as either assets or liabilities at fair value. Subsequent changes in a derivative's fair value are recognized in nonoperating (loss) income, net.

### **Bond Issuance Costs, Discounts and Premiums**

Bond issuance costs, discounts and premiums are amortized over the term of the bonds using the effective interest method and are included in long-term debt, less current portion in the accompanying condensed consolidated balance sheets.

## **General and Professional Liability Risks**

The provision for self-insured general and professional liability claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported. The System measures the cost of its unfunded obligations under such programs based upon actuarial calculations and records a liability on a discounted basis.

## **Net Assets With Donor Restrictions**

Net assets with donor restrictions are those assets whose use by the System has been limited by donors to a specific time period or purpose or consist of gifts with corpus values that have been restricted by donors to be maintained in perpetuity. Net assets with donor restrictions are used in accordance with the donor's wishes primarily to purchase property and equipment, to fund medical education or to fund health programs.

Assets released from restrictions to fund purchases of property and equipment are reported in the accompanying condensed consolidated statements of operations and changes in net assets as increases to net assets without donor restrictions. Those assets released from restriction for operating purposes are reported in the accompanying condensed consolidated statements of operations and changes in net assets as other revenue. When restricted, earnings are recorded as net assets with donor restrictions until amounts are expended in accordance with the donor's specifications.

## **Nonrecurring Expenses**

The System has incurred salaries, purchased services and other expenses in connection with the implementation of an enterprise resource planning system in 2022 and 2021, which was placed into service on April 1, 2022. Due to the nature of these expenses, the costs were reported as nonrecurring in the accompanying condensed consolidated statements of operations and changes in net assets.

## **Other Nonoperating (Loss) Income, Net**

Revenues and expenses from delivering health care services and the provision of goods and services ancillary thereto are reported in operations. Income and losses that arise from transactions that are peripheral or incidental to the System's main purpose are included in other nonoperating (loss) income, net. Other nonoperating (loss) income, net primarily consists of fund-raising expenses, contributions to charitable organizations, income taxes and the net non-service components of the periodic benefit expense of the System's pension plans.

## **Revenue (Less Than) in Excess of Expenses and Changes in Net Assets**

The accompanying condensed consolidated statements of operations and changes in net assets includes the revenue (less than) in excess of expenses as the performance indicator. Changes in net assets without donor restrictions, which are excluded from revenue (less than) in excess of expenses, primarily include contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purposes of acquiring such assets), pension-related changes other than net periodic pension costs and distributions to noncontrolling interests.

## **Accounting Pronouncements Adopted**

In August 2018, the Financial Accounting Standards Board ("FASB") issued ASU 2018-14, *Compensation-Retirement Benefits-Defined Benefit Plans-General (Subtopic 715-20)* to improve the effectiveness of disclosures for defined benefit plans under ASC 715-20. The ASU applies to employers that sponsor

defined benefit pension or other postretirement plans. This ASU is effective for non-public business entities for fiscal years ending after December 15, 2021. The amendments in this update remove disclosures that no longer are considered cost beneficial, clarify the specific requirements of disclosures and add disclosure requirements identified as relevant. The System adopted this guidance retrospectively.

In March 2021, the FASB issued updated guidance on goodwill impairment. ASU 2021-03-*Intangibles – Goodwill and Other (Topic 350): Accounting Alternative for Evaluating Triggering Events* attempts to simplify the goodwill triggering event evaluation process for private companies and not-for-profit entities. ASU 2021-03 provides an alternative for private companies and not-for-profit organizations by eliminating the ongoing triggering event analysis and instead allows organizations to evaluate the facts and circumstances as of the end of the reporting period to determine whether goodwill impairment has occurred. For entities who elect this alternative, the assessment is limited to the reporting date only. The scope of the alternative is limited to goodwill that is tested for impairment in accordance with Accounting Standards Codification Subtopic 350-20, *Intangibles—Goodwill and Other—Goodwill*. For private companies and not-for-profit organizations that have elected to amortize goodwill, the adoption of ASU 2021-03 is still applicable. The amendments in this ASU are effective on a prospective basis for fiscal years beginning after December 15, 2019. Early adoption is permitted for both interim and annual financial statements that have not yet been issued as of March 30, 2021. The amendments in the ASU also include an unconditional one-time option for entities to adopt the alternative prospectively after its effective date. No additional disclosures would be required. The System adopted this guidance during 2021.

#### **Accounting Pronouncements Not Yet Adopted**

In March 2020, the FASB issued ASU 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting*. This guidance provides optional expedients and exceptions for applying current GAAP to contracts, hedging relationships and other transactions affected by the transition from the use of London Interbank Offered Rate ("LIBOR") to an alternative reference rate. In response to concerns about structural risks of interbank offered rates ("IBORs"), and, particularly, the risk of cessation of LIBOR, regulators in several jurisdictions around the world have undertaken reference rate reform initiatives to identify alternative reference rates that are more observable or transaction based and less susceptible to manipulation. This guidance provides companies the option to ease the potential accounting burden associated with transitioning away from reference rates that are expected to be discontinued. In January 2021, the FASB issued ASU 2021-01, *Reference Rate Reform (Topic 848): Scope*, which adds implementation guidance to ASU 2020-04 to clarify certain optional expedients in Topic 848. The guidance has to be adopted no later than December 1, 2022 with early adoption permitted. Management is currently evaluating the impact of this guidance.

## **4. REVENUE AND RECEIVABLES**

### **Patient Service Revenue**

Patient service revenue is reported at the amount that reflects the consideration to which the System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including managed care payors and government programs and excludes revenues for services provided to patients under capitated arrangements) and others and include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews and investigations. Generally, patients and third-party payors are billed shortly after discharge. Revenue is recognized as performance obligations are satisfied.

Performance obligations are identified based on the nature of the services provided. Revenue associated with performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. Performance obligations satisfied over time relate to patients receiving inpatient acute care services. The System measures the performance obligation from admission into the hospital to the point when there are no further services required for the patient, which is generally the time of discharge. For outpatient services, the performance obligation is satisfied as the patient simultaneously receives and consumes the benefits provided as the services are performed. In the case of these outpatient services, recognition of the obligation over time yields the same result as recognizing the obligation at a point in time. Management believes this method provides a faithful depiction of the transfer of services over the term of performance obligations based on the inputs needed to satisfy the obligations.

The System uses a portfolio approach to account for categories of patient contracts as a collective group rather than recognizing revenue on an individual contract basis. The portfolios consist of major payor classes for inpatient revenue and major payor classes and types of services provided for outpatient revenue. Based on the historical collection trends and other analyses, the System believes that revenue recognized by utilizing the portfolio approach approximates the revenue that would have been recognized if an individual contract approach were used.

The System determines the transaction price, which involves significant estimates and judgment, based on standard charges for goods and services provided, reduced by explicit and implicit price concessions, including contractual adjustments provided to third-party payors, discounts provided to uninsured and underinsured patients in accordance with policy and/or implicit price concessions based on the historical collection experience of patient accounts. The System determines the transaction price associated with services provided to patients who have third-party payor coverage based on reimbursement terms per contractual agreements, discount policies and historical experience. For uninsured patients who do not qualify for charity care, the System determines the transaction price associated with services based on charges reduced by implicit price concessions. Implicit price concessions included in the estimate of the transaction price are based on historical collection experience for applicable patient portfolios. Patients who meet the System's criteria for charity care are provided care without charge; such amounts are not reported as revenue. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. Settlements with third-party payors for retroactive adjustments due to audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care using the most likely outcome method. These settlements are estimated based on the terms of the payment agreements with the payor, correspondence from the payor and historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as new information becomes available or as years are settled or are no longer subject to such audits, reviews and investigations.

For the three months ended March 31, 2022 and March 31, 2021 and the year ended December 31, 2021, changes in the System's estimates of implicit price concessions, discounts and contractual adjustments or other reductions to expected payments for performance obligations related to prior years were not significant.

In the normal course of business, the System does receive payments in advance for certain services provided and would consider these amounts to represent contract liabilities. The amounts received in the normal course of business at March 31, 2022 and December 31, 2021 were not material. In 2020



the CMS accelerated and advance payments received in relation to the COVID-19 pandemic for Medicare services are deemed contract liabilities at March 31, 2022 and December 31, 2021. See Note 2. SIGNIFICANT EVENTS.

Currently, the State of Illinois utilizes supplemental reimbursement programs to increase reimbursement to providers to offset a portion of the cost of providing care to Medicaid and indigent patients. These programs are designed with input from the CMS and are funded with a combination of state and federal resources, including assessments levied on the providers. Under these supplemental programs, the System recognizes revenue and related expenses in the period in which amounts are estimable and collection is reasonably assured. Reimbursement and the assessment under these programs are reflected in the accompanying condensed consolidated statements of operations and changes in net assets are as follows:

	<b>Classification</b>	<b>Three Months Ended March 31, 2022</b>	<b>Three Months Ended March 31, 2021</b>	<b>Year Ended December 31, 2021</b>
Reimbursement	Patient service revenue	\$ 70,250	\$ 73,819	\$ 321,123
Assessment	Supplies, purchased services and other expense	45,546	45,148	181,784

The State of Wisconsin assesses a fee or tax on gross patient service revenue. The revenues from this assessment are used to increase payments made to hospitals for services provided to Medicaid and other medically indigent patients. The System's patient service revenue reflects this increase in payment for services to Medicaid and other medically indigent patients and hospital tax assessment expense reflects the fees assessed by the State. Reimbursement and the assessment under these programs is reflected in the accompanying condensed consolidated statements of operations and changes in net assets are as follows:

	<b>Classification</b>	<b>Three Months Ended March 31, 2022</b>	<b>Three Months Ended March 31, 2021</b>	<b>Year Ended December 31, 2021</b>
Reimbursement	Patient service revenue	\$ 33,403	\$ 36,895	\$ 136,679
Assessment	Supplies, purchased services and other expense	24,614	25,320	99,140

Management has determined that the nature, amount, timing and uncertainty of revenue and cash flows are affected by the payor's geographical location, the line of business that renders services to patients and the timing of when revenue is recognized and billed.

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

<b>Three Months Ended March 31</b>	<b>2022</b>		<b>2021</b>	
Managed care	\$ 1,663,548	56 %	\$ 1,539,597	57 %
Medicare	894,429	29	804,301	29
Medicaid - Illinois	210,600	7	178,325	7
Medicaid - Wisconsin	137,310	5	135,399	5
Self-pay and other	85,195	3	59,230	2
	<u>\$ 2,991,082</u>	<u>100 %</u>	<u>\$ 2,716,852</u>	<u>100 %</u>

**Year Ended December 31**

	<b>2021</b>	
Managed care	\$ 6,534,404	55 %
Medicare	3,371,753	29
Medicaid - Illinois	825,834	7
Medicaid - Wisconsin	539,922	5
Self-pay and other	430,668	4
	<u>\$ 11,702,581</u>	<u>100 %</u>

Deductibles, copayments and coinsurance under third-party payment programs, which are the patient's responsibility, are included within the primary payor category in the tables above.

**Capitation Revenue**

The System has agreements with various managed care organizations under which the System provides or arranges for medical care to members of the organizations in return for a monthly payment per member. Revenue is earned each month as a result of the System agreeing to provide or arrange for the members' medical care.

**Other Revenue**

Other revenue is recognized at an amount that reflects the consideration to which the System expects to be entitled in exchange for providing goods and services. The amounts recognized reflect consideration due from customers, third-party payors and others. Primary categories of other revenue include grant revenues from the CARES Act, income from joint ventures, retail pharmacy revenue, grant revenue, cafeteria revenue, rent revenue and other miscellaneous revenue.

Revenue disaggregation by state and business line are as follows:

	<b>Three Months Ended March 31, 2022</b>	<b>Three Months Ended March 31, 2021</b>	<b>Year Ended December 31, 2021</b>
Illinois	\$ 1,641,228	\$ 1,481,514	\$ 6,388,560
Wisconsin	1,650,251	1,540,306	6,510,130
Total patient service revenue and capitation	<u>3,291,479</u>	<u>3,021,820</u>	<u>12,898,690</u>
Other revenue	274,366	246,601	1,163,442
Total revenue	<u>\$ 3,565,845</u>	<u>\$ 3,268,421</u>	<u>\$ 14,062,132</u>
Hospital	\$ 2,211,726	\$ 2,003,734	\$ 8,640,613
Clinic	679,088	626,552	2,711,468
Home Care	64,057	61,030	259,692
Other	36,211	25,536	90,808
Total patient service revenue	<u>2,991,082</u>	<u>2,716,852</u>	<u>11,702,581</u>
Capitation revenue	300,397	304,968	1,196,109
Other revenue	274,366	246,601	1,163,442
Total revenue	<u>\$ 3,565,845</u>	<u>\$ 3,268,421</u>	<u>\$ 14,062,132</u>

**Patient Accounts Receivable**

The System's patient accounts receivable is reported at the amount that reflects the consideration to which it expects to be entitled, in exchange for providing patient care. Patient accounts receivable are reported at net realizable value based on certain assumptions. For third-party payors including

Medicare, Medicaid and Managed Care, the net realizable value is based on the estimated contractual reimbursement percentage, which is based on current contract prices or historical paid claims data by payor. For self-pay, the net realizable value is determined using estimates of historical collection experience including an analysis by aging category. These estimates are adjusted for expected recoveries and any anticipated changes in trends including significant changes in payor mix and economic conditions or trends in federal and state governmental health care coverage.

The composition of patient accounts receivable is summarized as follows:

	<b>March 31, 2022</b>		<b>December 31, 2021</b>	
Managed care	\$ 989,148	52 %	\$ 935,709	52 %
Medicare	350,226	19	356,959	20
Medicaid - Wisconsin	42,994	2	50,111	3
Medicaid - Illinois	150,549	8	177,188	10
Self-pay and other	352,745	19	296,738	15
	<u>\$ 1,885,662</u>	<u>100 %</u>	<u>\$ 1,816,705</u>	<u>100 %</u>

The self-pay patient accounts receivable above includes amounts due from patients for co-insurance, deductibles, installment payment plans and amounts due from patients without insurance.

## 5. INVESTMENTS

The System invests in a diversified portfolio of investments, including alternative investments, such as real asset funds, hedge funds and private equity limited partnerships, whose fair value was \$5,836,834 and \$5,856,960 at March 31, 2022 and December 31, 2021, respectively. Collectively, these funds have liquidity terms ranging from daily to annual with notice periods typically ranging from 1 to 90 days. Certain of these investments have redemption restrictions that may restrict redemption for up to 11 years. However, the potential for the System to sell its interest in these funds in a secondary market prior to the end of the fund term does exist for prices at or other than the carrying value.

At March 31, 2022, the System had additional commitments to fund alternative investments, including callable distributions of \$1,889,276 over the next seven years.

In the normal course of operations and within established investment policy guidelines, the System may enter into various exchange-traded and over-the-counter derivative contracts for trading purposes, including futures, options and forward contracts. These instruments are used primarily to maintain the System's strategic asset allocation and hedge security price movements. These instruments require the System to deposit cash or securities collateral with the broker or custodian. Collateral provided was \$10,470 and \$16,589 at March 31, 2022 and December 31, 2021, respectively. The gross notional value of the derivatives outstanding was \$258,829 and \$282,289 at March 31, 2022 and December 31, 2021, respectively.

By using derivative financial instruments, the System exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contracts. When the fair value of a derivative contract is positive, the counterparty owes the System, which creates credit risk for the System. When the fair value of a derivative contract is negative, the System owes the counterparty and, therefore, it does not possess credit risk. The System minimizes the credit risk in derivative instruments by entering into transactions that may require the counterparty to post collateral for the benefit of the System based on the credit rating of the counterparty and the fair value of the derivative contract. Market risk is the adverse effect on the value of a financial instrument that results from a change in the underlying reference security. The market risk associated with market

changes is managed by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

Receivables and payables for investment trades not settled are presented within other current assets and accounts payable and other accrued liabilities in the accompanying condensed consolidated balance sheets. Unsettled sales resulted in receivables to brokers of \$54,400 and \$25,384 at March 31, 2022 and December 31, 2021, respectively. Unsettled purchases resulted in payables due to brokers of \$144,797 and \$135,997 at March 31, 2022 and December 31, 2021, respectively.

Investment returns for assets limited as to use and cash and cash equivalents are composed of the following:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Interest income and dividends	\$ 7,501	\$ 19,828	\$ 99,332
Income from alternative investments	163,987	190,754	926,066
Net realized gains	124,999	51,940	273,325
Net unrealized (losses) gains	(552,698)	51,565	79,580
Total	<u>\$ (256,211)</u>	<u>\$ 314,087</u>	<u>\$ 1,378,303</u>

Investment returns are included in the accompanying condensed consolidated statements of operations and changes in net assets as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Other revenue	\$ 18,185	\$ 13,320	\$ 53,651
Investment (loss) income, net	(265,968)	295,725	1,303,546
Net assets with donor restrictions	(3,428)	5,042	21,106
Total	<u>\$ (251,211)</u>	<u>\$ 314,087</u>	<u>\$ 1,378,303</u>

The cash and cash equivalents and assets limited as to use presented within the accompanying condensed consolidated balance sheets are comprised of the following:

	March 31, 2022	December 31, 2021
Internally designated for capital and other	\$ 10,523,856	\$ 11,572,323
Held for self-insurance	657,477	649,513
Donor restricted	151,512	155,009
Investments under securities lending program	12,984	17,760
Total noncurrent assets limited as to use	<u>11,345,829</u>	<u>12,394,605</u>
Cash and cash equivalents	763,163	703,725
Current assets limited as to use	139,740	139,742
Total cash and cash equivalents and assets limited as to use	<u>\$ 12,248,732</u>	<u>\$ 13,238,072</u>

## 6. FAIR VALUE

The System accounts for certain assets and liabilities at fair value and categorizes assets and liabilities measured at fair value in the accompanying condensed consolidated financial statements based upon whether the inputs used to determine their fair values are observable or unobservable. Observable inputs are inputs that are based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about pricing the asset or liability, based on the best information available under the circumstances.

The fair value of all assets and liabilities recognized or disclosed at fair value is classified based on the lowest level of significant inputs. Assets and liabilities that are measured at fair value are disclosed and classified in one of three categories. Category inputs are defined as follows:

Level 1 — Quoted prices (unadjusted) in active markets for identical assets or liabilities on the reporting date.

Level 2 — Inputs other than quoted market prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 — Inputs that are unobservable for the asset or liability for which there is little or no market data.

The following section describes the valuation methodologies used by the System to measure financial assets and liabilities at fair value. In general, where applicable, the System uses quoted prices in active markets for identical assets and liabilities to determine fair value. This pricing methodology applies to Level 1 investments, such as domestic and international equities, exchange-traded funds and agency securities.

If quoted prices in active markets for identical assets and liabilities are not available to determine the fair value, then quoted prices for similar assets and liabilities or inputs other than quoted prices that are observable either directly or indirectly are used. These investments are included in Level 2 and consist primarily of corporate notes and bonds, foreign government bonds, mortgage-backed securities, fixed-income securities, including fixed-income government obligations, commercial paper and certain agency, United States and international equities, which are not traded on an active exchange. The fair value for the obligations under swap agreements included in Level 2 is estimated using industry-standard valuation models. These models project future cash flows and discount the future amounts to a present value using market-based observable inputs, including interest rate curves. The fair values of the obligation under swap agreements include adjustments related to the System's credit risk.

Investments owned by the System are exposed to various kinds and levels of risk. Equity securities and equity funds expose the System to market risk, performance risk and liquidity risk for both domestic and international investments. Market risk is the risk associated with major movements of the equity markets. Performance risk is the risk associated with a company's operating performance. Fixed-income securities and fixed-income mutual funds expose the System to interest rate risk, credit risk and liquidity risk. As interest rates change, the value of many fixed-income securities is affected, including those with fixed interest rates. Credit risk is the risk that the obligor of the security will not fulfill its obligations. Liquidity risk is affected by the willingness of market participants to buy and sell particular securities. Liquidity risk tends to be higher for equities related to small capitalization companies and certain alternative investments. Due to the volatility in the capital markets, there is a reasonable possibility of subsequent changes in fair value, resulting in additional gains and losses in the near term.

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

The fair values of financial assets and liabilities that are measured at fair value on a recurring basis are as follows:

	March 31, 2022	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
<b>Investments</b>				
Cash and short-term investments	\$ 1,140,788	\$ 920,387	\$ 220,401	\$ —
Corporate bonds and other debt securities	767,089	—	767,089	—
United States government bonds	635,299	—	635,299	—
Bond and other debt security funds	510,998	103,492	407,506	—
Non-government fixed-income obligations	34,788	—	34,788	—
Equity securities	952,531	930,170	22,361	—
Equity funds	2,341,077	136,702	2,204,375	—
	<u>6,382,570</u>	<u>\$ 2,090,751</u>	<u>\$ 4,291,819</u>	<u>\$ —</u>
<b>Investments at net asset value</b>				
Alternative investments	<u>5,866,162</u>			
<b>Total investments</b>	<u>\$ 12,248,732</u>			
<b>Collateral proceeds received under securities lending program</b>				
	<u>\$ 13,622</u>		<u>\$ 13,622</u>	
<b>Liabilities</b>				
<b>Obligations under swap agreements</b>	<u>\$ (67,966)</u>		<u>\$ (67,966)</u>	
<b>Obligations to return capital under securities lending program</b>	<u>\$ (13,622)</u>		<u>\$ (13,622)</u>	

	December 31, 2021	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
<b>Investments</b>				
Cash and short-term investments	\$ 1,251,915	\$ 895,856	\$ 356,059	\$ —
Corporate bonds and other debt securities	816,147	—	816,147	—
United States government bonds	667,877	—	667,877	—
Bond and other debt security funds	559,769	99,237	460,532	—
Non-government fixed-income obligations	34,374	—	34,374	—
Equity securities	1,202,388	1,174,214	28,174	—
Equity funds	2,819,140	147,118	2,672,022	—
	<u>7,351,610</u>	<u>\$ 2,316,425</u>	<u>\$ 5,035,185</u>	<u>—</u>
<b>Investments at net asset value</b>				
Alternative investments	<u>5,886,462</u>			
<b>Total investments</b>	<u>\$ 13,238,072</u>			
<b>Collateral proceeds received under securities lending program</b>				
	<u>\$ 18,550</u>		<u>\$ 18,550</u>	
<b>Liabilities</b>				
<b>Obligations under swap agreements</b>	<u>\$ (91,217)</u>		<u>\$ (91,217)</u>	
<b>Obligations to return capital under securities lending program</b>	<u>\$ (18,550)</u>		<u>\$ (18,550)</u>	

## 7. PROPERTY AND EQUIPMENT, NET

The components of property and equipment, net are summarized as follows:

	March 31, 2022	December 31, 2021
Land and improvements	\$ 471,199	\$ 470,257
Buildings and fixed equipment	8,044,318	7,819,014
Movable equipment and computer software	2,605,202	2,554,215
Construction-in-progress	471,057	629,941
	<u>11,591,776</u>	<u>11,473,427</u>
Accumulated depreciation and amortization	<u>(5,664,952)</u>	<u>(5,530,416)</u>
Property and equipment, net	<u>\$ 5,926,824</u>	<u>\$ 5,943,011</u>

Property and equipment, net include assets recorded as finance leases and under other financing arrangements. See additional disclosure in Note 8. LEASES.

Depreciation expense is as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Depreciation expense	<u>\$ 134,550</u>	<u>\$ 136,305</u>	<u>\$ 536,567</u>

## 8. LEASES

The System leases office and clinical space, land and equipment. Leases with an initial term of 12 months or less are not recorded on the accompanying condensed consolidated balance sheets. The System combines lease and non-lease components except for medical equipment leases.

The depreciable lives of assets are limited by the expected lease terms. Most leases include options to renew. The majority of leases do not provide an implicit rate; therefore, the System has elected to use its incremental borrowing rate, which is the interest rate the System would borrow on a collateralized basis over a similar term, as the discount rate. The System used its incremental borrowing rate on January 1, 2019 for operating leases that commenced prior to that date.

Operating and finance leases are classified as follows within the accompanying condensed consolidated balance sheets:

Leases	Classification	March 31, 2022	December 31, 2021
<b>Assets</b>			
Operating	Operating lease right-of-use assets	\$ 287,762	\$ 283,398
Finance	Property and equipment, net	221,504	226,766
Total lease assets		<u>\$ 509,266</u>	<u>\$ 510,164</u>
<b>Liabilities</b>			
<b>Current</b>			
Operating	Operating lease liabilities, current portion	\$ 73,417	\$ 68,247
Finance	Long-term debt and commercial paper, current portion	15,745	16,669
<b>Noncurrent</b>			
Operating	Operating lease liabilities, less current portion	246,791	248,062
Finance	Long-term debt, less current portion	243,789	248,069
Total lease liabilities		<u>\$ 579,742</u>	<u>\$ 581,047</u>

Finance lease assets are recorded net of accumulated amortization of \$75,123 and \$69,861 as of March 31, 2022 and December 31, 2021, respectively.

Lease costs are classified as follows within the accompanying condensed consolidated statements of operations and changes in net assets:

Lease cost	Classification	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Operating lease cost	Supplies, purchased services and other	\$ 19,274	\$ 22,271	\$ 82,822
Short term lease cost	Supplies, purchased services and other	2,848	2,714	13,956
Variable lease cost	Supplies, purchased services and other	10,339	8,040	36,358
<b>Finance lease cost</b>				
Amortization of lease assets	Depreciation and amortization	5,261	2,997	11,998
Interest on lease liabilities	Interest	4,665	2,914	11,482
Sublease income	Other revenue	(652)	(613)	(2,503)
Net lease cost		<u>\$ 41,735</u>	<u>\$ 38,323</u>	<u>\$ 154,113</u>



Lease terms, discount rates and other supplemental information are as follows:

	As of March 31, 2022	As of March 31, 2021	As of December 31, 2021
Weighted average remaining lease term (in years)			
Operating	5.5	4.9	5.2
Finance	10.2	11.4	10.4
Weighted average discount rate			
Operating	1.98 %	2.23 %	2.05 %
Finance	8.52 %	7.55 %	8.52 %

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Cash paid for amounts included in the measurement of lease liabilities			
Operating cash flows from operating leases	\$ 20,416	\$ 21,982	\$ 86,743
Operating cash flows from finance leases	4,665	2,914	11,482
Financing cash flows from finance leases	5,204	2,359	9,246

Future maturities of lease liabilities at March 31, 2022 are as follows:

	Operating Leases	Finance Leases	Total
2022	\$ 60,582	\$ 23,442	\$ 84,024
2023	71,666	34,803	106,469
2024	57,334	35,638	92,972
2025	49,573	35,472	85,045
2026	41,708	35,440	77,148
Thereafter	57,474	226,454	283,928
Future minimum lease payments	338,337	391,249	729,586
Less remaining imputed interest	18,129	131,715	149,844
Total	\$ 320,208	\$ 259,534	\$ 579,742

## 9. INTEREST IN MASONIC FAMILY HEALTH FOUNDATION

The System has an interest in the net assets of the Masonic Family Health Foundation ("MFHF"), an independent organization, under the terms of an asset purchase agreement (the "Agreement"). Substantially all of MFHF's net assets are designated to support the operations and/or capital needs of one of the System's medical facilities. Additionally, 90% of MFHF's investment yield, net of expenses, on substantially all of MFHF's investments is designated for the support of one of the System's medical facilities. MFHF must pay the System, annually, 90% of the investment yield or an agreed-upon percentage of the beginning of the year net assets.

The interest in the net assets of MFHF amounted to \$112,795 and \$122,793 at March 31, 2022 and December 31, 2021, respectively, and is presented within investments in unconsolidated entities in the accompanying condensed consolidated balance sheets. The System's interest in the investment income is reflected in the accompanying condensed consolidated statements of operations and changes in net assets and amounted to the following:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Interest in the investment (loss) income	\$ (8,852)	\$ 2,069	\$ 17,853

Cash distributions were received by the System from MFHF under terms of the Agreement as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Cash distributions	\$ —	\$ 3,584	\$ 3,584

In addition, MFHF made the following contributions to the System for program support:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Contributions	\$ —	\$ —	\$ 694

The summarized financial position and results of operations for MFHF accounted for under the equity method as of and for the periods ended is outlined below:

	March 31, 2022	December 31, 2021
Total assets	\$ 118,974	\$ 127,838
Total liabilities	5,598	4,440
Net assets	113,376	123,398

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Total revenue	\$ (8,660)	\$ 2,305	\$ 19,867
Revenue (less than) in excess of expenses	(10,022)	1,108	14,014

## 10. LONG-TERM DEBT

The System's outstanding bonds are secured by obligations issued under the Second Amended and Restated Master Trust Indenture dated as of August 1, 2018, as the same may be amended from time to time, between Advocate Aurora Health, Inc., the other affiliates identified therein as the Members of the Obligated Group and U.S. Bank National Association, as master trustee ("the System Master Indenture"). Under the terms of the bond indentures and other arrangements, various amounts are to be on deposit with trustees, and certain specified payments are required for bond redemption and interest payments. The System Master Indenture and other debt agreements, including bank agreements, also place restrictions on the System and require the System to maintain certain financial ratios.

The System's unsecured variable rate revenue bonds, Series 2011B of \$69,660 and Series 2018B-2 of \$46,310, while subject to a long-term amortization period, may be put to the System at the option of the bondholders in connection with certain remarketing dates. To the extent that bondholders may, under the terms of the debt, put their bonds within 12 months after March 31, 2022, the principal amount of such bonds has been classified as a current obligation as long-term debt subject to short-term financing arrangements in the accompanying condensed consolidated balance sheets. Management believes the likelihood of a material amount of bonds being put to the System is remote. However, to address this possibility, the System has taken steps to provide various sources of liquidity, including assessing alternate sources of financing, including lines of credit and/or net assets without donor restrictions as a source of self-liquidity.

The System has standby bond purchase agreements with banks to provide liquidity support for the Series 2008C Bonds. In the event of a failed remarketing of a Series 2008C Bond upon its tender by an existing holder and subject to compliance with the terms of the standby bond purchase agreement, the standby bank would provide the funds for the purchase of such tendered bonds, and the System would be obligated to repay the bank for the funds it provided for such bond purchase (if such bond is not subsequently remarketed), with the first installment of such repayment commencing on the date one year and one day after the bank purchases the bond. As of March 31, 2022, there were no bank-purchased bonds outstanding. To the extent that the standby bond purchase agreement expiration date is within 12 months after March 31, 2022, the principal amount of such bonds would be classified as a current obligation in the accompanying condensed consolidated balance sheets. The standby bond purchase agreements expire as follows: \$129,456 in January 2024, \$87,694 in September 2024 and \$58,225 in September 2025.

In April 2021, the System issued additional Series 2018 Taxable Bonds in the principal amount of \$85,000 and additional Series 2019 Taxable Bonds in the principal amount of \$85,210 ("Additional Taxable Bonds"). The proceeds of the Additional Taxable Bonds were used to refinance a portion of the Series 2012, Series 2013A, Series 2014, Series 2015 Bonds and to pay certain financing costs. In connection with this transaction, the System recognized a loss on refinancing in the amount of \$14,421.

As of March 31, 2022, the System is authorized to issue up to \$1,000,000 in commercial paper aggregate principal outstanding. As of March 31, 2022, \$50,000 of commercial paper notes was outstanding, with maturities ranging from 60 to 90 days. As of December 31, 2021, \$50,000 of commercial paper was outstanding, with maturities ranging from 120 to 149 days.

At March 31, 2022, the System had lines of credit with banks aggregating to \$1,250,000 in available commitments. These lines of credit provide for various interest rates and payment terms and as of March 31, 2022 expire as follows: \$100,000 in December 2022, \$350,000 in December 2023, \$150,000 in August 2024, \$325,000 in December 2024 and \$325,000 in December 2025. These lines of credit may be used to redeem bonded indebtedness, to pay costs related to such redemptions, for capital expenditures, for general working capital purposes or to provide for certain letters of credit. As of March 31, 2022, letters of credit totaling \$69,802 have been issued under one of these lines. At March 31, 2022, no amounts were outstanding on these lines or drawn on the letters of credit.

The System maintains an interest rate swap program on certain of its variable rate debt, as described in Note 11. INTEREST RATE SWAP PROGRAM.

The System's interest paid amount includes all debt agreements including revenue bonds and revenue refunding bonds, taxable bonds, finance lease obligations, commercial paper, financing arrangements and interest rate swaps.

The System's interest paid, net of capitalized interest and capitalized interest are as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Interest paid, net of capitalized interest	\$ 32,497	\$ 29,670	\$ 113,633
Capitalized interest	2,789	2,806	13,027

## 11. INTEREST RATE SWAP PROGRAM

The System has interest rate-related derivative instruments to manage the exposure of its variable rate debt instruments. By using derivative financial instruments to manage the risk of changes in interest rates, the System exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contracts. When the fair value of a derivative contract is positive, the counterparty owes the System, which creates credit risk for the System. When the fair value of a derivative contract is negative, the System owes the counterparty and, therefore, it does not possess credit risk. The System minimizes the credit risk in derivative instruments by entering into transactions that may require the counterparty to post collateral for the benefit of the System based on the credit rating of the counterparty and the fair value of the derivative contract. Market risk is the adverse effect on the value of a derivative financial instrument that results from a change in interest rates. The market risk associated with interest rate changes is managed by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken. The System also mitigates risk through periodic reviews of its derivative positions in the context of its total blended cost of capital.

At March 31, 2022, the System maintains an interest rate swap program on its Series 2008C variable rate demand revenue bonds. These bonds expose the System to variability in interest payments due to changes in interest rates. The System believes that it is prudent to limit the variability of its interest payments. To meet this objective and to take advantage of low interest rates, the System entered into various interest rate swap agreements to manage fluctuations in cash flows resulting from interest rate risk. These swaps convert the variable rate cash flow exposure on the variable rate demand revenue bonds to synthetically fixed cash flows. The notional amount under each interest rate swap agreement is reduced over the term of the respective agreement to correspond with reductions in the principal outstanding under various bond series.

The System has two swaps that are being held as a swap portfolio as the related debt is no longer outstanding.

The following is a summary of the outstanding positions under these interest rate swap agreements at March 31, 2022:

Bond Series	Notional Amount	Maturity Date	Rate Received	Rate Paid
2008C-1	\$ 129,900	November 1, 2038	61.7% of LIBOR + 26bps	3.605 %
2008C-2B	58,425	November 1, 2038	61.7% of LIBOR + 26bps	3.605 %
2008C-3A	88,000	November 1, 2038	61.7% of LIBOR + 26bps	3.605 %
Swap portfolio	50,000	November 1, 2038	61.7% of LIBOR + 26bps	3.605 %
Swap portfolio	24,265	February 1, 2038	70.0% of LIBOR	3.314 %

The swaps are not designated as hedging instruments and, therefore, hedge accounting has not been applied. As such, unrealized changes in fair value of the swaps are classified as changes in fair value of swaps in the accompanying condensed consolidated statements of operations and changes in net assets. The net cash settlement payments, representing the realized changes in fair value of the swaps, are included as interest expense in the accompanying condensed consolidated statements of operations and changes in net assets.

The fair value of the interest rate swap agreements was a liability of \$67,966 and \$91,217 as of March 31, 2022 and December 31, 2021, respectively. No collateral was posted under these swap agreements as of March 31, 2022 and December 31, 2021.

Amounts recorded in the accompanying condensed consolidated statements of operations and changes in net assets are as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Net cash payments on interest rate swap agreements (interest expense)	\$ 2,903	\$ 2,901	\$ 11,487
Change in fair value of interest rate swaps	\$ 23,250	\$ 27,338	\$ 27,403

The interest rate swap instruments contain provisions that require the System to maintain an investment grade credit rating on its bonds from certain major credit rating agencies. If the System's bonds were to fall below investment grade, it would be in violation of these provisions and the counterparties to the swap instruments could request immediate payment or demand immediate and ongoing full overnight collateralization on interest rate swap instruments in net liability positions.

## 12. RETIREMENT PLANS

The System maintains various employee retirement benefit plans available to qualifying employees and retirees.

The Advocate Aurora Health Pension Plan ("AAH Plan") created through a merger of the Condell Health Network Retirement Plan (frozen effective January 1, 2008) and the Aurora Health Care, Inc. Pension Plan (frozen effective December 31, 2012). The accompanying condensed consolidated balance sheets contain an other noncurrent liability related to the AAH Plan of \$55,534 and \$57,617 at March 31, 2022 and December 31, 2021, respectively. During the three months ended March 31, 2022 and the year ended December 31, 2021, no contributions were made to the AAH Plan.

The Advocate Health Care Network Pension Plan ("Advocate Plan") was frozen effective December 31, 2019 to new participants and participants ceased accruing additional pension benefits. The accompanying condensed consolidated balance sheets contain an other noncurrent liability related to the Advocate Plan totaling \$71,683 and \$75,012 at March 31, 2022 and December 31, 2021, respectively. During the three months ended March 31, 2022 and the year ended December 31, 2021, \$0 and \$30,000, respectively, in cash contributions were made to the Advocate Plan.

Pension plan expense included in the accompanying condensed consolidated statements of operations and changes in net assets is as follows:

### Three Months Ended March 31, 2022

	Advocate	AAH	Total
Interest cost	\$ 7,306	\$ 10,962	\$ 18,268
Expected return on plan assets	(10,637)	(13,045)	(23,682)
Amortization of:			
Actuarial loss	896	1,509	2,405
Prior service cost	—	1	1
Net pension income	\$ (2,435)	\$ (573)	\$ (3,008)

**Three Months Ended March 31, 2021**

	<b>Advocate</b>	<b>AAH</b>	<b>Total</b>
Interest cost	\$ 6,579	\$ 10,412	\$ 16,991
Expected return on plan assets	(10,280)	(10,872)	(21,152)
Amortization of:			
Actuarial loss	1,148	2,603	3,751
Prior service cost	—	1	1
Net pension (income) expense	<u>\$ (2,553)</u>	<u>\$ 2,144</u>	<u>\$ (409)</u>

**Year Ended December 31, 2021**

	<b>Advocate</b>	<b>AAH</b>	<b>Total</b>
Interest cost	\$ 28,119	\$ 41,650	\$ 69,769
Expected return on plan assets	(42,421)	(43,487)	(85,908)
Amortization of:			
Actuarial loss	4,477	10,410	14,887
Prior service cost	—	3	3
Settlement	12,102	—	12,102
Net pension expense	<u>\$ 2,277</u>	<u>\$ 8,576</u>	<u>\$ 10,853</u>

The components of net periodic benefit costs other than the service cost component are included in other nonoperating (loss) income, net in the accompanying condensed consolidated statements of operations and changes in net assets.

The expected employee benefit payments to be paid from the pension plans are as follows:

	<b>Advocate</b>	<b>AAH</b>	<b>Total</b>
2022	\$ 63,891	\$ 51,638	\$ 115,529
2023	60,825	54,806	115,631
2024	61,364	58,001	119,365
2025	62,050	61,627	123,677
2026	62,199	64,417	126,616
2027-2031	291,885	356,338	648,223
Total	<u>\$ 602,214</u>	<u>\$ 646,827</u>	<u>\$ 1,249,041</u>

The System's asset allocation and investment strategies are designed to earn returns on plan assets consistent with a reasonable and prudent level of risk. Investments are diversified across classes, economic sectors and manager style to minimize the risk of loss. The System utilizes investment managers specializing in each asset category and, where appropriate, provides the investment manager with specific guidelines that include allowable and/or prohibited investment types. The System regularly monitors manager performance and compliance with investment guidelines.

The System's target and actual pension asset allocations for the plans are as follows:

<b>Asset Category - Advocate Plan</b>	<b>March 31, 2022</b>		<b>December 31, 2021</b>	
	<b>Target</b>	<b>Actual</b>	<b>Target</b>	<b>Actual</b>
De-risking portfolio	70 %	69 %	70 %	70 %
Domestic and international equity securities	21	21	21	21
Alternative investments	6	7	6	6
Fixed-income securities	3	3	3	3
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

Asset Category - AAH	March 31, 2022		December 31, 2021	
	Target	Actual	Target	Actual
De-risking portfolio	85 %	83 %	85 %	83 %
Domestic and international equity securities	12	14	12	14
Alternative investments	1	1	1	1
Fixed-income securities	2	2	2	2
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

Assumptions used to determine benefit obligations are as follows:

	December 31, 2022
Discount rate - Advocate Plan	2.85 %
Discount rate - AAH Plan	3.05 %
Assumed rate of return on assets - Advocate Plan	4.50 %
Assumed rate of return on assets - AAH Plan	3.80 %
Interest crediting rate - Advocate Plan	1.80 %

The assumed rate of return on each of the Plan's assets is based on historical and projected rates of return for asset classes in which the portfolio is invested. The de-risking portfolio is comprised of cash and fixed-income instruments designed to hedge Plan liabilities.

In addition to these plans, the System sponsors a defined contribution plan for its employees. Expense related to the plan, is included in salaries, wages and benefits expense in the accompanying condensed consolidated statements of operations and changes in net assets as follows:

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Year Ended December 31, 2021
Defined contribution plan expense	<u>\$ 87,791</u>	<u>\$ 78,965</u>	<u>\$ 296,894</u>

### 13. FUNCTIONAL EXPENSES

For the three months ended March 31, 2022 and March 31, 2021, the majority of the System's expenses were directly attributable to the provision of health care services. The remaining expenses, primarily legal, finance, purchasing and human resources were attributable to general and administrative functions. Health care services require the benefit of and the expense of general and administrative services; therefore, these costs would be further allocated to health care services. Fundraising expense are primarily reported within other nonoperating (loss) income, net in the accompanying condensed consolidated statements of operations and changes in net assets.

## 14. LIQUIDITY

The System's financial assets available within one year of the accompanying condensed consolidated balance sheets date for general expenditures are as follows:

	March 31, 2022	December 31, 2021
Current assets		
Cash and cash equivalents	\$ 763,163	\$ 703,725
Assets limited as to use	139,740	139,742
Patient accounts receivable	1,885,662	1,816,705
Third-party payors receivables	20,845	22,154
Collateral proceeds under securities lending program	13,622	18,550
Total current assets	2,823,032	2,700,876
Assets limited as to use		
Internally designated for capital and other	10,523,856	11,572,323
Held for self-insurance	657,477	649,513
Donor restricted	151,512	155,009
Investments under securities lending program	12,984	17,760
Total assets limited as to use	11,345,829	12,394,605
Total financial assets	14,168,861	15,095,481
Less		
Amounts unavailable for general expenditures		
Alternative investments	(2,832,323)	(2,727,059)
Total amounts unavailable for general expenditure	(2,832,323)	(2,727,059)
Amounts unavailable to management without approval		
Held for self-insurance	(797,217)	(789,255)
Donor restricted	(151,512)	(155,009)
Investments under securities lending program	(12,984)	(17,760)
Total amounts unavailable to management without approval	(961,713)	(962,024)
Total financial assets available to management for general expenditure within one year	\$ 10,374,825	\$ 11,406,398

## 15. GENERAL AND PROFESSIONAL LIABILITY RISKS

The System is self-insured for substantially all general and professional liability risks. The self-insurance programs combine various levels of self-insured retention with excess commercial insurance coverage. In addition, various umbrella insurance policies have been purchased to provide coverage in excess of the self-insured limits. Revocable trust funds, administered by a trustee and captive insurance companies, have been established for the self-insurance programs. Actuarial consultants have been retained to determine the estimated cost of claims, as well as to determine the amount to fund into the irrevocable trust and captive insurance companies.

The System's hospitals, clinics, surgery centers, physicians and certified registered nurse anesthetist providers that provide health care in Wisconsin are qualified health care providers that are fully covered for losses in excess of statutory limits through mandatory participation in the State of Wisconsin Injured Patients and Families Compensation Fund.

The estimated cost of claims is actuarially determined based on past experience, as well as other considerations, including the nature of each claim or incident and relevant trend factors. Accrued



insurance liabilities and contributions to the trust were determined using a discount rate of 3.00% as of March 31, 2022 and December 31, 2021.

The System entities are defendants in certain litigation related to professional and general liability risks, and other matters. Although the outcome of the litigation cannot be determined with certainty, management believes, after consultation with legal counsel, that the ultimate resolution of the litigations will not have a material adverse effect on the System's operations or financial condition.

## **16. LEGAL, REGULATORY AND OTHER CONTINGENCIES**

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. During the last few years, due to nationwide investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties, exclusion from the Medicare and Medicaid programs and revocation of federal or state tax-exempt status. Moreover, the System expects that the level of review and audit to which it and other health care providers are subject will increase.

Various federal and state agencies have initiated investigations, which are in various stages of discovery, relating to reimbursement, billing practices and other matters of the System. There can be no assurance that regulatory authorities will not challenge the System's compliance with these laws and regulations, and it is not possible to determine the impact, if any, such claims or penalties would have on the System. To foster compliance with applicable laws and regulations, the System maintains a compliance program designed to detect and correct potential violations of laws and regulations related to its programs.

## **17 SUBSEQUENT EVENTS**

The System evaluated events and transactions subsequent to March 31, 2022 through May 16, 2022, the date of consolidated financial statement issuance.

In May 2022, the System and Atrium Health, Inc. entered into a definitive agreement to come together to create a leading health and wellness delivery system to best meet patients' needs by redefining how, when and where care is delivered (the "Proposed Combination"). The completion of the Proposed Combination is contingent upon the satisfaction of certain conditions precedent, including the completion of a federal antitrust filing under the Hart-Scott-Rodino Act. Through the System can provide no assurances the Proposed Combination will occur, the System anticipates closing the transaction during 2022.

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## MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL POSITION

This quarterly report includes the condensed consolidated financial statements and analysis for Advocate Aurora Health, Inc., a Delaware nonprofit corporation (the "Parent Corporation"), and its subsidiaries. References to "the System", "we", "our" or "us" in this document are to the Parent Corporation and all of the subsidiaries consolidated with it pursuant to accounting principles generally accepted in the United States of America ("GAAP"). References to the Parent Corporation are references only to the Parent Corporation and should not be read to include any of the Parent Corporation's and subsidiaries.

The financial information should be read together with our condensed consolidated financial statements and related notes included elsewhere in this quarterly report, as well as the audited consolidated financial statements of the System as of and for the year ended December 31, 2021, which is available from the Municipal Securities Rulemaking Board (the MSRB) on its Electronic Municipal Market Access ("EMMA") system, found at <http://emma.msrb.org>. Additional information can be found on the investor relations section of the System's website at <https://www.advocateaurorahealth.org/investor-relations>.

Certain statements included in this quarterly report constitute forward-looking statements that involve risks and uncertainties. Actual results may differ significantly from the results discussed in the forward-looking statements as a result of known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. We do not plan to issue any updates or revisions to those forward-looking statements if or when the expectations, or events, conditions or circumstances on which such statements are based occur.

The information included herein is being provided solely to comply with contractual commitments. This filing does not purport to contain all information that may be material to an investor's decision to buy, sell or hold bonds issued by or for the benefit of the System ("Related Bonds"), and does not constitute or imply any representation that no other information exists that may have a bearing on the financial condition of the System, the security for any Related Bonds or an investor's decision to buy, sell or hold any Related Bonds. This report includes information only as of and for the three months ended March 31, 2022, and such information should not be relied upon as indicative of future financial performance. The COVID-19 pandemic described herein has and may adversely affect the System's future financial performance to an extent that could be material.

**ADVOCATE AURORA HEALTH, INC.**  
**KEY FINANCIAL RATIOS**

	<b>Three Months Ended,</b>	
	<b>March 31, 2022</b>	<b>March 31, 2021</b>
<b>Profitability</b>		
Operating margin <sup>(1)</sup>	0.3%	2.0%
Operating cash flow margin <sup>(2)</sup>	5.0%	7.1%
Excess margin <sup>(3)</sup>	(7.3)%	10.3%
EBIDA margin <sup>(4)</sup>	(2.0)%	16.4%
	<b>As of March 31, 2022</b>	<b>As of December 31, 2021</b>
<b>Leverage and Liquidity</b>		
Debt to capitalization <sup>(5)</sup>	20.4%	20.2%
Cash to debt <sup>(6)</sup>	318%	345%
Days cash on hand <sup>(7)</sup>	297	348
Historical debt service coverage ratio	8.8x	8.9x

<sup>(1)</sup> Operating income before nonrecurring expenses/Total revenue

<sup>(2)</sup> (Operating income before nonrecurring expenses + Interest + Depreciation and amortization)/Total revenue

<sup>(3)</sup> Revenue in excess of expenses/(Total revenue + Total nonoperating income (loss), net)

<sup>(4)</sup> (Revenue in excess of expenses + Interest + Depreciation and amortization)/Total revenue

<sup>(5)</sup> (Current portion of long-term debt and commercial paper + Long-term debt subject to short-term financing arrangements + Long-term debt, less current portion)/(Current portion of long-term debt and commercial paper + Long-term debt subject to short-term financing arrangements + Long-term debt, less current portion + Total net assets without donor restrictions)

<sup>(6)</sup> Unrestricted cash and investments/(Current portion of long-term debt and commercial paper + Long-term debt subject to short-term financing arrangements + Long-term debt, less current portion)

<sup>(7)</sup> Unrestricted cash and investments/(Total expenses before nonrecurring expenses - Depreciation and amortization + Nonrecurring expenses (less estimated loss on sale of property)/days in period). The days cash on hand ratio is calculated from expenses for the three months ended March 31, 2022 and the year ended December 31, 2021.

**ADVOCATE AURORA HEALTH, INC.**  
**KEY FINANCIAL RATIOS**  
(in thousands)

**Trailing twelve-month debt service coverage as of March 31, 2022**

Revenue less than expenses- attributable to controlling interest	\$	1,244,144
Adjustments:		
Depreciation and amortization expense		565,714
Interest expense		105,653
Unrealized gain on investments		(366,951)
Unrealized gain on interest rate swap obligation		(23,315)
Loss on early extinguishment of debt		14,501
Asset impairment charges		1,017
Nonrecurring expenses		31,855
Total income available for debt service		1,572,618
Debt service requirement		177,727
Historical debt service coverage ratio		8.8

This ratio is being presented for information purposes only and is not indicative of future results. This ratio is calculated in the same manner as that presented in the Management, Discussion and Analysis of the condensed consolidated financial statements as of and for the year ended December 31, 2021.

**ADVOCATE AURORA HEALTH, INC.**  
**HISTORICAL UTILIZATION**

	Three Months Ended March 31, 2022	Three Months Ended March 31, 2021	Change	% Change
Discharges	56,961	59,321	(2,360)	(4.0)%
Observation Cases	26,398	23,711	2,687	11.3 %
Hospital Outpatient Visits	1,036,399	975,193	61,206	6.3 %
Physician Visits <sup>(2)</sup>	2,398,534	2,247,868	150,666	6.7 %
Home Care Visits	189,248	201,171	(11,923)	(5.9)%
Capitated Member Lives <sup>(1)</sup>	234,935	247,143	(12,208)	(4.9)%

<sup>(1)</sup> As of the date set forth in the column header

<sup>(2)</sup> 2021 visits were updated to reflect the current year count methodology.

**MANAGEMENT DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS**  
**(in thousands)**

The management discussion and analysis section refers to the accompanying condensed consolidated financial statements.

Results of Operations – Three Months Ended March 31, 2022 Compared to Three Months Ended March 31, 2021

Operating income before nonrecurring expenses was \$9,885 for the three months ended March 31, 2022, resulting in an operating margin of 0.3%, compared to \$64,231 for the three months ended March 31, 2021, for an operating margin of 2.0%. This represented a period-over-period decrease of \$54,346.

Total revenue for the three months ended March 31, 2022 was \$3,565,845, which was \$297,424 (9.1%) higher than the comparative period of 2021.

Patient service revenue increased \$274,230 (10.1%), in the three months ended March 31, 2022 compared to the same period in the prior year. The increase is due to an increase in outpatient visits and physician visits compared to the same period in the prior year.

Capitation revenue decreased \$4,571 (1.5%) in the three months ended March 31, 2022, compared to the same period in the prior year due to a shift in the overall membership mix and a decrease in capitated lives of 4.9%.

Other operating revenue of \$274,366 decreased \$27,765 or 11.3% in the three months ended March 31, 2022, compared to the same period in the prior year. The decrease is due to lower shared savings revenue for the three months ended March 31, 2022.

Total expenses (excluding nonrecurring expenses) for the three months ended March 31, 2022 were \$3,555,960, which was \$351,770 (11.0%) higher than the comparative period of 2021.

Salaries, wages and benefits expenses increased \$245,854 (13.4%) in the three months ended March 31, 2022, compared to the same period in the prior year. The increase is primarily due to an increase in nurse agency costs and an increase in full-time equivalent employees of 1.0% due to higher patient volumes period-over-period.

Supplies, purchased services and other expenses increased \$88,999 (8.4%) in the three months ended March 31, 2022, compared to the same period in the prior year. The increase is primarily due an increase in patient volumes period-over-period and an increase in supply purchases in anticipation of the system-wide implementation of the new enterprise resource planning system ("ERP") on April 1, 2022.

Nonrecurring expenses were \$7,380 and \$13,284 for the three months ended March 31, 2022 and March 31, 2021, respectively. Nonrecurring expenses consist of costs incurred in connection with the ERP implementation.

Nonoperating loss of \$(245,113) for the three months ended March 31, 2022 compares unfavorably to the nonoperating income of \$318,547 for the three months ended March 31, 2021 primarily due to investment (loss) income, net which decreased \$561,693 over the comparative period. See disclosure of the composition of investment income, net within Note 5. INVESTMENTS of the accompanying condensed consolidated financial statements. The decrease is due to the decline in financial market yields over the

comparative period. The change in fair value of interest rate swaps is attributable to an increase in interest rates.

Overall, the System reported revenue (less than) in excess of expenses - attributable to controlling interest of \$(253,227) for the three months ended March 31, 2022 compared to \$351,752 for the three months ended March 31, 2021 due primarily to decreased investment yields in 2022.

## **Liquidity**

The System holds substantially all its investments in a single investment portfolio. The investments in this portfolio are managed by external investment professionals under the guidelines set out in the investment policy statement adopted by the System's Board.

This policy includes the target allocations for the System's investment program. The System's investment program's target asset allocation, excluding cash and cash equivalents maintained for operating purposes, provides for a commitment to equity securities (30%), fixed income investments (20%) and select alternative investment classes (50%). Limitations are placed on investment managers as to the overall amount that can be invested in one issuer (except for U.S. government obligations and its agencies) or economic sector. See disclosure of the composition of the System's investment assets within Note 6. FAIR VALUE.

Investment income (including both realized and unrealized gains on investments) significantly impacts the System's financial results. Market fluctuations have affected and will likely continue to materially affect the value of those investments and those fluctuations may be and historically have been material. Reduction in investment income, or realized and unrealized losses, and the market value of its investments may have a negative impact on the System's financial condition, including its ability to provide its own liquidity for variable rate debt or to fund capital expenditures from cash and investments.

For the three months ended March 31, 2022 and March 31, 2021, the investment return, including investment returns reported as part of operating income and restricted funds was \$(254,615) and \$311,581, respectively. The decrease in investment earnings is consistent with overall market returns.

The System's financing strategy is to ensure liquidity and access to capital markets, to maintain a balanced spectrum of debt maturities and to manage our net exposure to floating interest rate volatility. Within these parameters, we seek to minimize our borrowing costs. The ability to access the long-term debt and commercial paper markets helps provide the System with sources of liquidity. Management is authorized to issue commercial paper and/or have lines of credit in place up to a combined maximum of \$2,500,000 (with a sublimit of \$1,000,000 on commercial paper) at any given time.

## **Days Cash on Hand**

Days cash on hand was 297 as of March 31, 2022 compared to 348 as of December 31, 2021. Excluding the Medicare accelerated and advance payments and the deferred employer portion of the Social Security tax portion of FICA taxes, days cash on hand was 284 as of March 31, 2022 and 330 as of December 31, 2021. The decline from December 31, 2021 is reflective of an increase in day's operating expenses, investment return losses and working capital uses.

## **Indebtedness**

Master Indenture Obligations: Substantially all of the System's outstanding Related Bonds and certain other obligations to lenders, banks and swap counterparties are all secured by Obligations issued under the

Second Amended and Restated Master Trust Indenture dated as of August 1, 2018, with the Members of the Obligated Group and U.S. Bank National Association, as master trustee (the "System Master Indenture").

On April 8, 2021, the System issued \$170,210 of Additional Taxable Bonds to refinance certain tax-exempt bonds in the aggregate principal amount of \$159,725 and to pay certain expenses incurred in connection with their issuance.

Under the terms of the bond indentures and other arrangements, various amounts are to be on deposit with trustees and certain specified payments are required for bond redemption and interest payments. The System Master Indenture and other debt agreements, including bank credit agreements, also place restrictions on the System to maintain certain financial ratios. Each of the bank agreements requires various reporting, operating and financial covenants to be maintained. These covenants may be waived, modified or amended by the related bank in its sole discretion and without notice to or consent by any bond trustee, the Master Trustee or the holders of any outstanding Related Bonds. Violation of any such covenants may result in an Event of Default under the System Master Indenture, which could result in acceleration of all Obligations issued under the System Master Indenture.

The System's total long-term debt and commercial paper was as follows:

	<b>March 31, 2022</b>	<b>December 31, 2021</b>
Tax-exempt bonds	\$ 1,215,541	\$ 1,218,375
Taxable bonds	1,941,372	1,941,573
Financing arrangements	265,284	270,876
Taxable term loan	80,226	80,219
Commercial paper	50,000	50,000
Total long-term debt	<u>\$ 3,552,423</u>	<u>\$ 3,561,043</u>

Standby Bond Purchase Agreements ("SBPA"): The System is a party to three SBPAs with two banks to provide liquidity support for the three subseries of the Series 2008C Bonds in the event of a failed remarketing of any such Series 2008C Bonds. The termination dates of the SBPAs are as follows:

<b>Subseries</b>	<b>Par</b>	<b>Expiration</b>
2008C-1	\$ 129,500	1/15/2024
2008C-2B	58,200	9/30/2025
2008C-3A	87,700	9/27/2024
Total	<u>\$ 275,400</u>	

In the event any bonds are not remarketed within one year from the date they are purchased by a bank pursuant to an SBPA ("Bank Bonds"), the System has agreed to cause such Bank Bonds to be redeemed pursuant to the related bond indenture such that the unpaid principal balance of all outstanding Bank Bonds shall amortize in approximately equal quarterly installments, with the first installment commencing on the date that is one year and one day after the date on which such Series 2008C Bond became a Bank Bond, the final installment payable on the date that is five years from the date on which such Series 2008C Bond became a Bank Bond (or, with respect to any Series 2008C-1 Bond or Series 2008C-2B that is a Bank Bond, if earlier, the date that is one year and one day following the then current Stated Expiration Date). At March 31, 2022, there were no Bank Bonds outstanding.

Covenant Agreements ("CAs"): The System is party to CAs with a bank, related to the Series 2011C Bonds and Series 2011D Bonds issued in September 2011 and purchased by the bank. The Series 2011C Bonds and Series 2011D Bonds currently bear interest at an indexed rate until September 3, 2024. At the end of their initial periods, the Series 2011C Bonds and the Series 2011D Bonds will be subject to mandatory tender, unless waived by the holders thereof, and the System presently anticipates that the Series 2011C Bonds and



Series 2011D Bonds will be remarketed to new holders in one of the interest rate modes available under the related bond indenture. In the event the Series 2011C Bonds or the Series 2011D Bonds are not remarketed on their respective mandatory tender dates, then, as long as no default or event of default (as defined in the CAs) has occurred and is continuing, the Series 2011C Bonds or Series 2011D Bonds, as applicable, may either be repaid over a three-year period or remarketed during that time.

Windows Variable Rate Bonds: The System's Series 2011B Bonds bear interest at Windows Interest Rates (the "Windows Variable Rate Bonds") and are subject to optional and mandatory tender for purchase. The Windows Variable Rate Bonds are not supported by any external dedicated liquidity facility. Holders of Windows Variable Rate Bonds have a right to optionally tender their Bonds for purchase. If the tendered Windows Variable Rate Bonds are not successfully remarketed within the 30-day period that follows the date that notice of such optional tender is received by the Remarketing Agent (the "Remarketing Window"), then all Windows Variable Rate Bonds are required to be purchased on the day that is 210 days after notice of such optional tender is received by the Remarketing Agent (the "Windows Mandatory Tender Date"). The period from the end of the Remarketing Window until the Windows Mandatory Tender Date (initially, 180 days) is referred to as the Funding Window. During the Funding Window, the System expects that it would analyze the then current market conditions, availability and relative cost of any refinancing or restructuring alternatives for those Windows Variable Rate Bonds that are required to be purchased on the Windows Mandatory Tender Date (including, without limitation, conversion of those bonds to another interest mode or the refinancing or repayment of those bonds). The Windows Variable Rate Bonds are classified as current liabilities at March 31, 2022 and December 31, 2021 in the accompanying condensed consolidated balance sheets because these bonds may be subject to tender on a date that was within one year of the balance sheet date.

Long-term Rate Bonds: The Series 2018B-1, 2018B-2, Series 2018B-3, Series 2018B-4 Bonds and Series 2018C-1 Bonds ("the Long-Term Rate Bonds") bear interest at long-term rates for a particular interest rate period and are subject to mandatory tender at the end of each particular interest rate period.

The following table summarizes the next scheduled mandatory tender dates for the Long-Term Rate Bonds as of March 31, 2022. In the event these Long-Term Rate Bonds are not remarketed upon mandatory tender at the end of their current interest rate period, management anticipates utilizing marketable unrestricted investments, commercial paper issuance and/or available lines of credit to meet the purchase obligations.

<b>Subseries</b>	<b>Par</b>	<b>Expiration</b>
Series 2018B-1	40,130	7/1/2027
Series 2018B-2	46,310	1/25/2023
Series 2018B-3	48,560	1/31/2024
Series 2018B-4	49,420	1/29/2025
Series 2018C-1	40,885	7/29/2026
Total	<u>\$ 225,305</u>	

On April 8, 2021, \$40,885 of the Series 2018C-1 Bonds were remarketed for a new long-term rate period and will next be subject to mandatory tender on July 29, 2026. In connection with the remarketing, \$9,115 of the Series 2018C-1 Bonds were redeemed.

On January 26, 2022, \$46,690 of the Series 2018B-1 Bonds were remarketed for a new long-term rate period and will next be subject to mandatory tender on July 1, 2027. In connection with the remarketing, \$6,560 of the Series 2018B-1 Bonds were redeemed.

Indexed Floating Rate Bonds: The Series 2018C-2 Bonds, Series 2018C-3 Bonds and Series 2018C-4 Bonds (collectively the "Indexed Rate Bonds") bear interest at an indexed rate. At the end of their respective initial

index rate periods, the Indexed Rate Bonds will be subject to mandatory tender. The following table summarizes the next scheduled mandatory tender dates for the Indexed Rate Bonds as of March 31, 2022.

<b>Subseries</b>	<b>Principal Amount</b>	<b>Next Mandatory Tender date</b>
Series 2018C-2	50,000	7/1/2026
Series 2018C-3	49,065	7/26/2023
Series 2018C-4	50,350	7/31/2024
Total	<u>\$ 149,415</u>	

**Taxable Term Note:** The System is party to a taxable term loan agreement with a bank, relating to a \$80,226 term loan, the proceeds of which were used to defease a portion of the Series 2010 Bonds. Absent an agreement between the System and the bank to extend the final maturity, the taxable term loan matures on September 27, 2024.

**Commercial Paper:** In order to enhance the System's liquidity, Management has the authority to issue up to \$1,000,000 from time to time under the System's commercial paper program. As of March 31, 2022, \$50,000 of commercial paper notes were outstanding and the System has the authority to issue \$950,000 of additional commercial paper.

**Lines of Credit:** At March 31, 2022, the System had lines of credit agreements with banks totaling \$1,250,000. These agreements expire as follows: \$100,000 in December 2022, \$350,000 in December 2023, \$150,000 in August 2024, \$325,000 in December 2024 and \$325,000 in December 2025. At March 31, 2022, the System had a \$150,000 line of credit, under which letters of credit can also be issued. At March 31, 2022, letters issued under the line of credit totaling \$69,802 were outstanding. At March 31, 2022, there were no outstanding draws on the line of credit or letters of credit. Each line of credit is secured by a separate Obligation issued under the System Master Indenture.

Under regulatory rules of the State of Illinois, Advocate is required to post a letter of credit or surety bond with a State Agency, Advocate held a surety bond in the amount of \$17,475. No amounts were drawn on this surety bond at March 31, 2022.

**Other Indebtedness:** At March 31, 2022, the System had various finance lease arrangements totaling \$265,284 classified as long-term debt. These arrangements, which relate to various administrative and medical support buildings, had initial lease terms of 10 to 25 years.

**Interest Rate Swaps:** The System has multiple floating-to-fixed interest rate swap arrangements with respect to the Series 2008C Bonds (collectively, the Series 2008C Swaps) pursuant to ISDA Master Agreements. Pursuant to the Series 2008C Swaps, Wells Fargo Bank, National Association ("Wells Fargo") and PNC Bank, National Association ("PNC") pay the System the sum of a percentage of the one-month London Interbank Offered Rate ("LIBOR") plus a spread, and the System pays Wells Fargo and PNC amounts based on a fixed rate (approximately 3.605%). All Wells Fargo, PNC and the System payments are made on a same day net payment basis with reference to a notional amount that declines over the term of the Series 2008C Swaps. Unless terminated earlier in accordance with their terms, the Series 2008C Swaps' scheduled termination date is November 1, 2038. Under certain circumstances, however, the Series 2008C Swaps are subject to termination prior to the scheduled termination date.

In connection with an acquisition, the System acquired a floating-to-fixed interest rate swap agreement ("Portfolio Swap"). Piper Jaffray Financial Products Inc. ("Piper Jaffray") pays the System a percentage of the one-month LIBOR and the System pays Piper Jaffray amounts based on a fixed rate (approximately 3.314%) based on the notional amount which declines over the term of the Portfolio Swap. Unless terminated earlier

in accordance with their terms, the Portfolio Swap's scheduled termination date is February 1, 2038. Under certain circumstances, the Portfolio Swap is subject to termination prior to the scheduled termination date.

See Note 6. FAIR VALUE and Note 11. INTEREST RATE SWAP PROGRAM for discussion of the fair value and a description of the accounting treatment of the System's interest rate swap arrangements.

Risks Associated with Discontinuance of LIBOR: Certain of the System's outstanding interest rate swaps, credit facilities and other indebtedness are currently payable based on LIBOR, which is an interbank offered rate. Recent statements from U.S. bank regulators have stressed that supervised institutions should stop originating new LIBOR-linked instruments by the end of 2021 and existing contracts referencing LIBOR are expected to transition on or before the anticipated cessation of LIBOR immediately after June 30, 2023.

If future uncertainty surrounding the replacement reference rate results in increases in LIBOR rates, the amounts payable by the System on its LIBOR-based instruments may be affected. Further, the phase out of LIBOR and the uncertainty as to the replacement reference rate may increase the costs and availability of financing. The replacement of LIBOR with a successor rate could cause amounts payable by the System on its LIBOR-based obligations to be different or higher than expected.

Securities Lending: As part of the management of the investment portfolio, the System has entered into an arrangement whereby securities owned by the System are loaned, primarily to brokers and investment banks. The loans are arranged through a bank. Borrowers are required to post collateral in the form of cash or highly rated securities for securities borrowed equal to no less than 102% of the value of the security loaned on a daily basis. The bank is responsible for reviewing the credit-worthiness of the borrowers. The System has also entered into an arrangement whereby the bank is responsible for the risk of borrower bankruptcy and default. At March 31, 2022 and December 31, 2021, the System loaned approximately \$12,984 and \$17,760, respectively in securities and accepted collateral for these loans in the amount of \$13,622 and \$18,550, respectively which represented cash and government securities. The collateral received under the securities lending program has been reflected as a current asset and a current obligation payable in the accompanying condensed consolidated balance sheets presented. The balance of securities on loan and accepted collateral fluctuates daily.

## **Capital Expenditures**

For the three months ended March 31, 2022, capital expenditures of the System were \$129,581; on March 31, 2022 the System had \$471,057 of construction-in-progress. The amounts of construction-in-progress on March 31, 2022 relate to various projects to improve existing facilities and expand access to health care in the markets served.

The System has four significant capital projects that are ongoing or approved. The System is currently expanding the Center for Advanced Care at Advocate Illinois Masonic Medical Center in Chicago, Illinois. This expansion is expected to cost approximately \$121,300 and is estimated to be completed in January 2025. The System is building a medical campus, replacing an existing campus, in Sheboygan, Wisconsin. Management currently anticipates a cost of approximately \$325,000 for that campus, with an expected completion date of July 2022. The System approved a project in December 2021 for Advocate Illinois Masonic Medical Center Patient Pavilion. The project is the final phase of a decade-long master plan to privatize all patient rooms. The total project will cost approximately \$348,000 with an expected completion date of August 2026 for the bed pavilion and finalization of the total project by September 2029. Currently, management expects to fund capital commitments and expenditures with cash generated from operations and investment income, as well as from existing cash and investment balances.

Management continues to evaluate planned capital projects and routine capital expenditures with a focus on liquidity needs, operating margin considerations and alignment with the strategic plan.

## **LEGAL AND REGULATORY COMPLIANCE**

The System operates in a highly litigious industry. As a result, various lawsuits, claims and proceedings have been instituted or asserted against it from time to time. The System has knowledge of certain pending suits against certain of its entities that have arisen in the ordinary course of business. In the opinion of management, the System maintains adequate insurance and/or other financial reserves to cover the estimated potential liability for damages in these cases, or, to the extent such liability is uninsured, adverse decisions will not have a material adverse effect on the financial position or operations of the System.

As a health care provider, the System entities are subject to extensive and frequently changing federal, state and local laws and regulations governing various aspects of our business. In particular, the System entities provide a broad range of services, many of which are regulated by different government agencies, subject to differing regulatory schemes and subject to contractual reviews and program audits in the normal course of business. Many operations that the System entities undertake are subject to significant governmental certification and licensing regulations, as well as federal and state laws.

The System, like all major health care systems, periodically may be subject to investigations or audits by federal, state and local agencies involving compliance with a variety of laws and regulations. These investigations seek to determine compliance with, among other things, laws and regulations relating to Medicare and Medicaid reimbursement, including billing practices for certain services. Violation of such laws could result in substantial monetary fines, civil and/or criminal penalties and exclusion from participation in Medicare, Medicaid or similar programs.

### **Compliance and Internal Audit Programs**

The System's Compliance and Integrity Program ("Program") is overseen by the System Chief Compliance Officer. The System Chief Compliance Officer reports to the Chief Executive Officer, with reporting accountability to the Audit and Compliance Committee of the System Board of Directors. The Program is modeled after the seven essential elements of an effective compliance program, as set forth in the U.S. Health and Human Services, Office of Inspector General Compliance Program Guidance and further interpreted by the Federal Sentencing Guidelines and the U.S. Department of Justice Guidelines for the Federal Prosecution of Corporations. The Program includes mandatory annual education of all employees regarding specific legal and regulatory requirements applicable to health care organizations, including requirements related to patient confidentiality, information privacy, information systems security, conflicts of interest, licensure and certification, federal fraud and abuse laws, billing, coding and documentation, civil rights and non-retaliation. The Program is based on a Code of Conduct and includes an anonymous hotline available to report violations or seek guidance on compliance issues.

The System also has an internal audit department responsible for providing independent and objective assurance and consulting services designed to add value and help the System accomplish its objectives by bringing a systematic, disciplined approach to evaluate the effectiveness of risk management, control and governance processes. The System Audit Officer reports functionally to the Audit and Compliance Committee of the Board of Directors and administratively to the Chief Financial Officer. The internal audit department carries out an annual audit program that assesses the System's design and operation of internal controls to achieve efficient and effective operations, accurate and reliable financial reporting, compliance with policies, laws and regulations and the proper safeguarding of assets.

## **BOND RATINGS**

In August 2021, Fitch affirmed a rating of AA (stable outlook) and Moody's affirmed a rating of Aa3 (positive outlook) on the Related Bonds. In September 2021, S&P affirmed a rating of AA (stable outlook).

The ratings above reflect only the view of the rating organization providing the same, and an explanation of the significance of such ratings may be obtained only from the rating agency furnishing the same. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by such rating agency if, in its judgment, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of System's outstanding bonds. A securities rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time.

Additional information on the System's bond ratings can be obtained from the Investor Relations section on <https://www.advocateaurorahealth.org/investor-relations>.

## **MANAGEMENT**

Key members of the management of the System are described within the "GOVERNANCE AND MANAGEMENT" section in Appendix A to the Offering Memorandum dated April 28, 2020, relating to the Series 2020A Bonds. The Offering Memorandum can be accessed at <http://munios.com>. Since April 28, 2020, the following changes occurred:

In December 2021, Dr. Vincent Bufalino, Chief Advocate Medical Group Officer, retired. As a result of Dr. Bufalino's retirement, Dr. Jeffery Bahr, Chief Aurora Medical Group Officer, was named the System's Chief Medical Group Officer. In this role, Dr. Bahr is responsible for Advocate Aurora's medical group operations, clinical service lines, physician recruitment, clinical quality and programming, as well as access. He is also accountable for Advocate Aurora Health's academic programs.

In March 2021, Shoeb Sitafalwalla, MD was announced as the System's new Chief Strategy Officer, effective April 1, 2021. Scott Powder, the System's previous Chief Strategy Officer, transitioned to focus exclusively on the whole person health portion of the System's strategic plan and thus, was appointed President of Advocate Aurora Enterprises.

In March 2021, Meghan Woltman was appointed as the System's Chief Government Relations Officer, replacing Joyce Rogers, who resigned from the System in January 2021.

In December 2020, Mike Lappin, the System's Chief Integration Officer, left the System. There are currently no plans to fill this position.

## **SYSTEM STRATEGY**

The System maintains a strategic plan and is well positioned to carry out its purpose: to help people live well. The plan calls for transformation of the System's core business of health care delivery while simultaneously building the System's future as a consumer health company. The plan has three major focus areas: transform the core, consumer-first and whole person health. Transform the core includes strategies to develop new care models, deliver purpose driven care with continuous engagement in the context of platform operations. Consumer-first includes strategies to provide a seamless and connected consumer experience. Whole person health includes strategies to develop, acquire or partner with entities that allow us to augment care delivery capacity outside of standard clinical tools that help augment a consumer's health and wellness journey.

In furtherance of the System's whole person health strategy, on April 1, 2022, the System acquired MobileHelp Group Holdings, LLC for \$290,670.

## **Potential Affiliation**

On May 11, 2022, the System and Atrium Health, Inc. signed an agreement to come together to create a leading health and wellness delivery system to best meet patients' needs by redefining how, when and where care is delivered (the "Proposed Combination"). The completion of the Proposed Combination is contingent upon the satisfaction of certain conditions precedent, including the completion of a federal antitrust filing under the Hart-Scott-Rodino Act. Through the System can provide no assurances the Proposed Combination will occur, the System anticipates closing the transaction during 2022. Additional information on this Proposed Combination is available on the Electronic Municipal Market Access website ([www.emma.msrb.org](http://www.emma.msrb.org)) or on the investor relations section of the System's website at <https://www.advocateaurorahealth.org/investor-relations>.

The System will continue to evaluate potential affiliations, divestitures, joint ventures and other strategic relationships that it believes will be advantageous.

## **ENVIRONMENTAL, SOCIAL AND GOVERNANCE PRACTICES ("ESG")**

The System's focus on environmental sustainability, team member development, wellness, diversity, equity and inclusion and safety are rooted in the System's purpose to help people live well. This commitment extends beyond the boundaries of our System and into the communities the System is privileged to serve.




### ***Environmental Sustainability***

The System is steadfast in efforts to eliminate harm to human and environmental health, and to improve environmental quality by enhancing policies, programs and practices for all its business activities. Towards this end, the System adopted environmentally preferable purchasing guidelines and strategies that inform sourcing and contracting decisions. The System seeks to purchase environmentally preferable products from environmentally responsible suppliers whenever financially feasible. Additionally, the scale of the System is utilized to drive the market toward transparency and accelerated development of healthier, safer products and building materials which protect human and environmental health across their entire life cycle.

The System's sustainability efforts also focus on reducing waste (e.g., recycling, single use device reprocessing, paper utilization and food waste) and energy conservation. The System aims for Leadership in Energy and Environmental Design ("LEED") for Healthcare certification on select new major buildings. A roadmap also guides all current and future renovations and construction projects across the System on a path of sustainability. The roadmap meets or exceeds the U.S. Green Building Council requirements for LEED Certification. In addition, the System has announced a commitment to power its health care operations with 100% renewable electricity by 2030. Over the next decade, all major construction and renovation projects will be evaluated for the addition of on-site renewables and implemented when financially feasible.

Environmental sustainability goals are governed by the System's sustainability team. The sustainability team sets the areas of focus and most implementation strategies for environmental stewardship work at the System. The sustainability team lead meets regularly with senior leadership to discuss proposed goals, progress, barriers and initiatives. Progress towards the System's established sustainable operations goals is conveyed through the Environmental Sustainability Dashboard.

Below are metrics from the System's 2021 Environmental Sustainability Dashboard:

Category			2021 System Target	2021 System Results*
 Sustainable Purchases	<b>Chemical Free Furniture Purchases</b>	Percent of freestanding furniture and medical furnishing purchases without the use formaldehyde, perfluorinated compounds, polyvinyl chloride (PVC), antimicrobials, and flame retardants (where code permits).	90%	96%
	<b>Certified Green Cleaners Purchases</b>	Percent of general-purpose, window/glass, bathroom, carpet/rug, and floor cleaner purchases that are certified by a third-party for having reduced environmental and public health impacts compared to similar products.	70%	66%
	<b>Antibiotic Free Meat Purchases</b>	Percent of meat purchased from animals raised without the routine use of antibiotics. Low doses of antibiotics are often given to farm animals to boost growth and prevent disease in otherwise healthy animals; this practice contributes to antibiotic resistance.	35%	31%
 Waste Reduction	<b>Waste Reduction</b>	Percent reduction of the volume of solid and medical waste produced per adjusted patient day (APD) from baseline. Waste reduction activities include waste prevention, reprocessing, donation, and recycling.	-1% from 2020 baseline	-3.7%
	<b>Paper Reduction</b>	Percent reduction in paper utilization from the previous year.	-2% from 2020 baseline	0.2%
 Energy and Climate	<b>Energy Use Intensity</b>	Percent reduction of the building's weather-normalized energy use intensity (12-month rolling). Energy Use Intensity (EUI) calculates the amount of energy used per square foot in the building (total energy usage/gross floor area).	<0% from 2020 baseline	-1.85%
	<b>Greenhouse Gas (GHG) Emission Intensity</b>	Percent reduction of the buildings GHG intensity. GHG intensity is calculated by dividing the total GHG emissions of the building in one year by the total gross floor area of the building.	-2% from 2020 baseline	-1.85%

\* Results from Green Cleaners, Waste Reduction, Energy and GHG Emissions include hospital data only.

To foster environmental sustainability in the community, the System provides national leadership and mentoring in sustainable health care through membership and participation in several sustainability leadership councils and groups. A summary of the significant initiatives the System has taken to spur movement toward healthier and more sustainable practices throughout the health care sector and wider marketplace include:

- Member of the [Healthcare Anchor Network](#) ("HAN") and a signatory of the HAN Impact Purchasing Commitment.
- Member of the Health Care Climate Council to lead the transformation to climate-smart health care.
- Member of the Healthcare Facility Advisory Board of Healthcare Plastics Recycling Coalition.
- Continued leadership in Health Care Without Harm and Practice Greenhealth.
- Signatory of the Chemical Footprint Project.

External recognition of the System's sustainability efforts include:

- Recipient of the 2021 System for Change Award from Practice Greenhealth. This is the thirteenth consecutive year the System has received this award, the longest run in the country.
- Recipient of the 2021 Environmental Excellence Award for all the System's acute care hospitals.
- Nine of the System's hospitals have received ENERGY STAR certification.

- Named a 2021 Climate Champion in the category of Climate Leadership through the Health Care Climate Challenge.

### ***Socially Responsible Investment***

The System has numerous social responsibility guidelines in place within its Investment program. The security selection process involves screening the sources of revenue of potential investments. The System does not invest directly in companies that derive 20% or greater of their revenue from certain prohibited activities. Additionally, the System believes that investment performance and diversity can co-exist. On December 31, 2021, 9.4% of the System's investment assets were managed by diverse-owned investment management firms. Per the Knight Foundation's "Diversity of Asset Manager's Study" in 2021, 1.4% of U.S. based assets under management are overseen by diverse-owned investment management firms. The System proactively seeks out diverse investment managers to manage its investment assets.

### ***Human Capital***

The System is committed to creating and maintaining a diverse, inclusive and engaged environment where team members can pursue their passion and feel supported, valued and recognized. The System believes attraction, development, engagement and retention of team members is critical to fulfilling its purpose and thus, dedicates resources to support these efforts including training and talent development programs.

The System is also committed to supporting personal well-being and preserving a healthy environment for its approximate 75,000 team members. The System's team member well-being program is designed to educate and encourage all team members. Those who take action to manage and improve their health are incentivized and recognized for their efforts and achievements. The System offers discounts at its fitness centers, indoor and outdoor guided walking paths at each hospital location and a variety of physical, mental and social programs, resources and interventions to support team members in their well-being journey. In 2021 in the midst of a pandemic, the System achieved top quartile team member engagement.

The System believes that a diverse workforce, in a thriving inclusive environment, delivers a higher level of equitable care, serving patients across all communities. By recruiting and retaining a diverse workforce and empowering diverse perspectives, the System aims to inspire creativity that leads to innovative solutions. To assist in reaching these goals and reflective of the Systems commitment to and prioritization of diversity, equity and inclusion, the Board of Directors (which consists of 11 members: 4 are African American, 1 is LGBTQ and 4 are women) established a Diversity, Equity & Inclusion ("DE&I") Committee. The Committee, comprised of directors and external thought leaders in the work of DE&I in health care, is responsible to ensure that the DE&I strategy is embedded throughout the System and to maintain organizational accountability around that strategy. The Advocate Aurora Health Inclusion Council was also created along with core teams tasked with locally implementing DE&I efforts to strengthen the broader culture of inclusion.

Reflecting the commitment of inclusive excellence, the System has embedded its DE&I principles into the Code of Conduct comprising of clear standards for responding to difficult situations, behavior on social media, and interactions with the media. In addition, the System has updated the dress code policy to reflect its inclusive values. The System has also facilitated Inclusive Hiring sessions designed to help its leaders create a more inclusive hiring experience for candidates.

External recognition of the System's DE&I efforts include:

- Listed for the third time on Diversity MBA Magazine's as one of the best places to work for women and diverse managers.



- Named on of the top organizations for diversity by Modern Healthcare.
- Received the Healthcare Workforce Impact Award from the National Latino Education Institute.
- The System's Chief External Affairs Officer named one of 50 business leaders of color for 2021 by Chicago United and received a 2021 Health Care Champions award from the Milwaukee Business Journal.
- The System's Chief DEI office named on of Crain's 2021 notable executives in diversity, equity and inclusion.
- The System's Board of Director Chair received Modern Healthcare's 2022 Excellence in Governance awards for tackling the industry's challenges with a modern mindset, a dedication to expanding access and a focus on diversity, equity and inclusion.
- LGBTQ healthcare equality leader designation for all 24 of the System's hospitals, with a perfect Healthcare Equality Index score of 100.

Additional information regarding the System's diversity, equity and inclusion efforts is available in the [2021 DE&I Impact Report](#).

### ***Safety and High Reliability***

In furtherance of the System's efforts to do no harm, the System has developed a high reliability plan which incorporates proactive strategies to anticipate risks and to establish system wide safety process to address these risks. This plan applies across the care continuum and in both clinical and non-clinical areas. The System's high reliability plan includes several programs, such as:

- *Establishment and maintenance of safety as the cultural foundation of care.* This is inclusive of both patient safety and team member safety.
- *Teach leaders to lead to safety.* Educating and hard wiring the use of explicit high reliability leadership skills. Leaders are taught to define and demonstrate *Safety First* as part of the overall patient experience, to find problems and fix causes in systems and processes and reinforce and build accountability for high reliability behaviors.
- *Empower and support the frontline to address safety issues.* Through deliberate influence, frontline team members are encouraged to change culture by using high reliability tools and tactics, exercising autonomy in fixing latent safety threats and being the voice of patient safety at the local level.
- *Engagement of patients and families in patient safety.* A commitment to transparency with patients and their families enables strong partnerships and collaboration to learn from and prevent safety events.

### ***Addressing Health Inequities***

The System is committed to addressing health inequity while focusing on quality of care, safety and reducing the cost of care. The System provides charitable care and services to its communities including: charity and other uncompensated care that is provided free, subsidized or without full reimbursement from Medicare, Medicaid or other government-sponsored programs; subsidized health services that respond to unique community needs; education to train health care professionals; volunteer services provided by team members who donate time to supporting their communities; language assistance and interpreter services; and contributions of equipment, supplies and other assistance to community groups.

A summary of the significant initiatives taken to address health inequities and promote DE&I in the System's communities include:

- Launched the System's Diversity Partnership Pilot Program...Building Tomorrow's Healthcare in 2021. Partnering with general contractors and industry leaders, the System will use this program to

provide opportunities for diverse contractors to gain knowledge about the complexities of health care construction and project experience along with certification and mentorship.

- Joined Chicago Mayor Lori Lightfoot's Racial Equity Rapid Response Initiative with other health systems and community partners to incite real change to achieve racial justice and end health disparities.
- Co-led Chicago's South Side Healthcare Transformation and renewed its commitment to revitalize Milwaukee's near west side.
- Spearheaded the creation of the Racial and Health Equity Advisory Council within the Milwaukee Health Care Partnership to build an interorganizational anti-racism and health equity collaboration.
- Established a formal Business Diversity Program within the System with the focus to increase purchases that are made from diverse businesses. The System will seek to purchase goods and services from diverse suppliers whenever financially feasible with the belief that utilizing diverse suppliers can help provide economic strength to underserved communities in the regions the System serves.
- Founding member of the HAN, a national consortium of health systems dedicated to driving inclusive anchor strategies to positively impact the social and economic determinants of health. The System signed the HAN Racism is a Public Health Crisis statement.
- Contracted with NowPow to provide important social determinants of health to its patients. NowPow is used to screen patients for social determinants of health and provide referrals to community benefit organizations that provide services that address patient needs.
- Provided free, community based, flu vaccines for our most vulnerable populations.
- Introduced No Patient Left Behind, a program rooted in an ethical framework to optimize vaccine uptake by reaching out to secure appointments for patients in areas disproportionately affected by COVID-19.
- Created an LGBTQ-Inclusive provider directory designed to vet providers and ensure safe, equitable care for LGBTQ patients.
- Established a Health Equity Council to develop key innovation strategies to address inequities in our patient population.
- Established a community investment program that grants low interest loans to community organizations.

## **CYBERSECURITY**

Healthcare providers and insurers are highly dependent upon integrated electronic medical record and other information technology systems to deliver high quality, coordinated and cost-effective healthcare. These systems necessarily hold large quantities of highly sensitive protected health information that is highly valued on the black market. As a result, the electronic systems and networks of healthcare providers and insurers are considered likely targets for cyberattacks and other potential breaches of their systems. In addition to regulatory fines and penalties, the healthcare entities subject to the breaches may be liable for the costs of remediating the breaches, damages to individuals (or classes) whose information has been breached, reputational damage and business loss and damage to the information technology infrastructure. The System has taken, and continues to take, measures to protect its information technology system against such cyberattacks, but there can be no assurance that the System will not experience a significant breach. If such a breach occurs, the financial consequences of such a breach could have a materially adverse impact on the System.

As the System's investment in information technology continues to increase, cybersecurity continues to be a top priority. The System has developed a cyber security program and continues to implement tools, processes and policies to secure its technology infrastructure and protect its data assets. The cyber security program is dynamic in nature with all tenets under constant review and modification to protect against continually emerging threats and to ensure regulatory compliance.

## INDUSTRY RISKS

For a description of industry risks, see Exhibit I “BONDHOLDERS’ RISKS” section in the Official Statement Supplement dated January 26, 2022, relating to the remarketing of certain Series 2018B Bonds. The Official Statement Supplement can be accessed at <http://munios.com>.

As described in the BONDHOLDERS’ RISKS section in the Official Statement Supplement, the System is aware of certain additional risks regarding the spread of COVID-19, a strain of coronavirus. On March 11, 2020, the World Health Organization declared COVID-19 a pandemic, and on March 13, 2020, President Trump declared a national emergency. The federal government and a large number of state governments, including Illinois and Wisconsin, imposed strict measures to curtail certain aspects of public life in an effort to contain the spread of COVID-19.

An outbreak of an infectious disease, including any growth in the magnitude or severity of COVID-19 cases in the System’s service areas, could result in an abnormally high demand for health care services, potentially inundating hospitals with patients in need of intensive care services and the treatment of a highly contagious disease at one of the System’s facilities could also result in a temporary shutdown of facilities or diversion of patients or staffing shortages. Additionally, elective procedures may be deferred, resulting in reduced patient volumes and operating revenues at the System’s facilities. Further, the changing global economic conditions or potential global health concerns such as the COVID-19 virus may also affect the System’s partners, suppliers, distributors and payors, potentially disrupting or delaying the System’s supply chain and delaying reimbursement by governmental or private payors.

The continued spread of COVID-19 or any other similar outbreaks in the future may materially adversely impact the System’s financial condition and results of operations, as well as national and local economies. See Note 2. SIGNIFICANT EVENTS for further details on the financial effects on the System.

The System benefited approximately \$23,000 and \$102,000 for the three months March 31, 2022 and the year ended December 31, 2021, respectively, from the suspension of Medicare sequestration and the 20% add-on to the DRG payment of inpatients admitted with COVID-19 during the emergency period imposed under the CARES Act.

The System has reactivated all aspects of its health care operations. The success of such reactivation is subject to many factors external to the System including potential new government mandated prohibitions of non-essential healthcare procedures, the willingness of patients to resume preventive and elective care, availability of personal protection equipment and other supplies and drugs, changes in clinical care and patient and caregiver safety protocols and processes required by the Centers for Disease Control and Prevention, the Occupational Health and Safety Administration, states’ departments of public health and other government bodies.

Although the System has activated plans to address the COVID-19 pandemic and operates pursuant to infectious disease protocols, the potential impact of a pandemic, epidemic or outbreak of an infectious disease with respect to the System’s service areas or facilities is difficult to predict and could adversely impact the business, financial condition or results of operations, and, accordingly, may materially adversely impact the financial condition of the System.

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