Obligated Group Financial Statements

2nd Quarter
March 31, 2023

Scripps

Scripps Health
Obligated Group

Table of Contents
For the Quarter and Six Months Ended March 31, 2023

Scripps

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENTS OF FINANCIAL POSITION
March 31, 2023
($000s)

	March 2023	March 2022	September 2022
ASSETS			
Current Assets:			
Cash and Cash Equivalents	$ 122,813	$ 483,621	$ 400,216
Accounts Receivable, Net	426,034	469,394	439,744
Assets Limited As To Use	-	10	10
Other Current Assets	335,925	304,304	297,589
Total Current Assets	**884,772**	**1,257,328**	**1,137,559**
Investments:			
Assets Limited As To Use	298,458	332,198	303,966
Unrestricted	3,158,895	3,280,959	2,819,488
Property, Plant and Equipment	4,565,508	4,482,412	4,668,026
Less Accumulated Depreciation	(2,110,749)	(2,256,595)	(2,331,001)
Property, Plant and Equipment, Net	**2,454,760**	**2,225,817**	**2,337,025**
Right of Use Assets	244,255	240,732	255,612
Other Assets	220,024	219,499	251,496
Total Assets	**$ 7,261,165**	**$ 7,556,533**	**$ 7,105,146**
LIABILITIES AND EQUITY			
Current Liabilities:			
Current Portion of Long-term Debt	$ 39,432	$ 240,492	$ 48,963
Line of Credit	-	83,992	83,992
Accounts Payable	287,538	215,560	308,396
Accrued Liabilities	256,881	431,935	323,129
Current Portion of Lease Liability	29,700	28,551	29,797
Total Current Liabilities	**613,550**	**1,000,530**	**794,277**
Long Term Debt	1,338,257	1,087,410	1,276,274
Other Liabilities	82,205	93,293	90,347
Long Term Lease Liability	219,007	224,445	226,504
Total Liabilities	**2,253,019**	**2,405,678**	**2,387,402**
Net Assets:			
Without Donor Restrictions			
Controlling Interest	4,742,447	4,849,978	4,446,394
With Donor Restrictions	265,698	300,877	271,350
Total Net Assets	**5,008,146**	**5,150,855**	**4,717,744**
Total Liabilities and Net Assets	**$ 7,261,165**	**$ 7,556,533**	**$ 7,105,146**

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENT OF OPERATIONS
($000s)

	FOR THE QUARTER ENDED MARCH 31, 2023	FOR THE QUARTER ENDED MARCH 31, 2022
Revenues, gains, and other support without donor restrictions:		
Patient service revenue	$ 914,015	$ 801,651
Provider tax revenue	-	-
Total patient service revenue	914,015	801,651
Capitation premium	28,382	34,015
CARES act / FEMA	25,269	20,346
Other	30,037	25,604
Net assets released from restrictions used for operations	9,132	14,386
Total operating revenues	**1,006,834**	**896,003**
Operating expenses:		
Wages and benefits	480,485	422,329
Supplies	193,222	170,529
Physician services	182,767	162,664
Other services	117,872	96,037
Provider fee	-	-
Capitation services	1,373	1,157
Depreciation and amortization	44,522	50,921
Interest	8,780	5,975
Total operating expenses	**1,029,021**	**909,612**
Operating loss before corporate overhead allocation & income tax	**(22,187)**	**(13,609)**
Corporate overhead allocation	1,044	423
Provision for income tax expense	(310)	(226)
Operating loss after corporate overhead allocation & income tax	**(21,453)**	**(13,412)**
Nonoperating gains:		
Interest and dividends	14,110	9,877
Realized gains	3,295	18,288
Unrealized gains / (loss) on trading portfolio	126,581	(226,157)
Contributions	431	398
Market adjustment on Interest rate swaps	(225)	6,395
Excess of revenues over expenses	**$ 122,739**	**$ (204,611)**

Scripps

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENTS OF CHANGES IN NET ASSETS
($000s)

	FOR THE QUARTER ENDED MARCH 31,	
	2023	**2022**
Other change in net assets without donor restrictions:		
Excess of revenues over expenses attributable to controlling interests	$ 122,739	$ (204,611)
Net assets released from restrictions used for purchase of property & equipment	3,342	6,359
Other	-	(101)
Increase / (decrease) in net assets without donor restrictions	**126,081**	**(198,354)**
Change in net assets with donor restrictions:		
Contributions	3,152	8,711
Interest and dividends	613	378
Realized gains	212	825
Unrealized gains / (losses) on trading portfolio	5,283	(6,233)
Net assets released from restrictions used for operations	(9,132)	(14,386)
Net assets released from restrictions used for purchases of property & equipment	(3,342)	(6,359)
Change in value of deferred gifts	113	153
Other	-	1
Decrease in net assets with donor restrictions	**(3,100)**	**(16,910)**
Total increase / (decrease) in net assets	**$ 122,980**	**$ (215,264)**

Scripps

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENT OF OPERATIONS
($000s)

	FOR THE SIX MONTHS ENDED MARCH 31, 2023	2022
Revenues, gains, and other support without donor restrictions:		
Patient service revenue	$ 1,806,124	$ 1,633,979
Provider tax revenue	30,295	38,494
Total patient service revenue	1,836,418	1,672,472
Capitation premium	59,985	68,616
CARES act / FEMA	25,269	21,350
Other	59,238	52,020
Net assets released from restrictions used for operations	19,765	21,617
Total operating revenues	**2,000,675**	**1,836,075**
Operating expenses:		
Wages and benefits	931,920	838,322
Supplies	374,805	346,494
Physician services	355,030	315,227
Other services	219,518	184,510
Provider fee	25,209	27,161
Capitation services	2,655	2,279
Depreciation and amortization	87,055	100,556
Interest	18,552	12,484
Total operating expenses	**2,014,744**	**1,827,033**
Operating (loss) / gains before corporate overhead allocation & income tax	**(14,069)**	**9,042**
Corporate overhead allocation	1,413	776
Provision for income tax expense	(563)	(843)
Operating (loss) / gains after corporate overhead allocation & income tax	**(13,219)**	**8,976**
Nonoperating gains:		
Interest and dividends	42,895	56,529
Realized (loss) / gains	(21,420)	63,823
Unrealized gains / (loss) on trading portfolio	275,359	(228,374)
Contributions	2,376	2,210
Market adjustment on Interest rate swaps	402	7,282
Excess of revenues over expenses	**$ 286,393**	**$ (89,554)**

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENTS OF CHANGES IN NET ASSETS
($000s)

	FOR THE SIX MONTHS ENDED MARCH 31, 2023	2022
Other change in net assets without donor restrictions:		
Excess of revenues over expenses attributable to controlling interests	$ 286,393	$ (89,554)
Net assets released from restrictions used for purchase of property & equipment	9,574	9,065
Other	-	(253)
Increase / (decrease) in net assets without donor restrictions	**295,966**	**(80,742)**
Change in net assets with donor restrictions:		
Contributions	13,345	19,766
Interest and dividends	1,758	1,538
Realized (losses) / gains	(878)	2,001
Unrealized gains / (losses) on trading portfolio	12,039	(4,945)
Net assets released from restrictions used for operations	(19,765)	(21,617)
Net assets released from restrictions used for purchases of property & equipment	(9,574)	(9,065)
Change in value of deferred gifts	(2,623)	1,276
Other	10	158
Decrease in net assets with donor restrictions	**(5,688)**	**(10,888)**
Total increase / (decrease) in net assets	**$ 290,279**	**$ (91,631)**

Scripps

SCRIPPS HEALTH
OBLIGATED GROUP
STATEMENT OF CASH FLOWS
($000)

	For the Six Months Ended	
	March 31, 2023	March 31, 2022
Operating activities and nonoperating gains		
Total increase / (decrease) in net assets	$290,279	($91,631)
Reconciliation of total change in net assets to cash flows provided by		
operating activities and nonoperating gains and losses:		
Depreciation and amortization	87,055	100,556
Amortization of debt issuance costs	120	127
Amortization of original issue premium / discount	(271)	(275)
Realized and unrealized (gains) / loss on investments	(265,100)	167,495
Purchases of investments designated as trading	(417,536)	(493,379)
Proceeds from sale of investments designated as trading	343,229	364,240
Interest rate swaps	2,957	(7,242)
(Loss) / gain on disposal of property	1,476	(897)
Restricted contributions and investment income	(14,225)	(23,305)
Change in assets and liabilities:		
Accounts receivables - net	13,710	79,585
Right of use operating lease liabilities	(14,895)	(13,882)
Other current assets	(19,678)	28,777
Other assets	27,657	29,443
Accounts payable and accrued liabilities	(92,085)	(83,328)
Other liabilities	(12,319)	(51,174)
Net cash (used in) / provided by operating activities:	(69,628)	5,111
Investing activities:		
Purchases of property, plant and equipment	(199,986)	(164,264)
Purchases of investments designated as assets limited as to use	(4,007)	-
Sales of investments designated as assets limited as to use	9,525	11,753
Net cash used in investing activities:	(194,468)	(152,511)
Financing activities:		
Proceeds from restricted contributions and investment income	16,559	27,182
Proceeds from line of credit	100,000	-
Payments from line of credit	(83,992)	-
Payment of bond issuance costs	-	(305)
Right of use financing lease payment	(1,391)	(2,528)
Proceeds from long-term debt	-	250,000
Payments on long-term debt	(44,665)	(33,975)
Proceeds from sale of donated financial assets	182	202
Net cash (used in) / provided by financing activities:	(13,307)	240,576
(Decrease) / Increase in cash and cash equivalents	(277,403)	93,176
Cash and cash equivalents at beginning of period	400,216	390,445
Cash and cash equivalents at end of period	$122,813	$483,621
Supplemental non-cash disclosure:		
Operating Lease	$7,301	$1,953
Financing Lease	-	240

SCRIPPS HEALTH
OBLIGATED GROUP
NOTES TO THE OBLIGATED GROUP FINANCIAL STATEMENTS
(UNAUDITED)

NOTE (1) SUMMARY OF SIGNIFICANT ACCOUNTING PRINCIPLES

Basis of Presentation

In the opinion of management, all adjustments, consisting of normal recurring adjustments necessary for the fair presentation of the statements of financial position and results of operations as of and for the quarter ended March 31, 2023 and 2022 as well as for the year-to-date September 30, 2022 have been made.

NOTE (2) FAIR VALUE MEASUREMENTS

The Organization accounts for certain assets and liabilities at fair value. A fair value hierarchy for valuation inputs prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels and is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are as follows:

Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the measurement date. Financial assets and liabilities in Level 1 include U.S. and foreign equity securities.

Level 2: Pricing inputs are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Financial assets and liabilities in this category generally include U.S. and foreign government securities, asset-backed securities, U.S. and foreign corporate bonds and loans, municipal bonds, commingled funds, interest rate swaps, real estate, real estate held for sale, and annuity/unitrust liabilities.

Level 3: Pricing inputs are generally unobservable for the assets or liabilities and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities. The fair values are therefore determined using factors that involve considerable judgment and interpretations, including, but not limited to, private and public comparables, third-party appraisals, discounted cash flow models, and fund manager estimates.

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

Assets and liabilities measured at fair value are based on one or more of the three valuation techniques. Where more than one technique is noted, individual assets or liabilities were valued using one or more of the noted techniques. The valuation techniques are as follows:

a) Market approach. Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

b) Income approach. Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques, option-pricing, and excess earnings models).

c) Cost approach. Measurement alternative for equity securities without readily determinable fair values and are not eligible to use Net Asset Value (NAV) of accounting. Cost minus impairment, if any, changes resulting from observable changes in orderly transactions from an identical or similar investment of the same issuer.

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

The following represents financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2023 (in thousands). Alternative investments are accounted for using NAV, which is not a fair value measurement.

	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Active Markets for Identical Assets (Level 3)	NAV	Total	Valuation Technique (a, b, c)
Investments						
Liquid investments:						
Cash equivalents	$ 1,047	$ –	$ –	$ –	$ 1,047	a
Equity securities:						
U.S. equity	757,556	–	–	–	757,556	a
Foreign equity	724,222	–	–	–	724,222	a
Foreign equity (commingled)	–	200,629	–	–	200,629	a
	1,481,778	200,629	–	–	1,682,407	
Fixed income securities:						
U.S. government	–	70,157	–	–	70,157	a
U.S. government agencies	–	20,805	–	–	20,805	a
U.S. federal agency mortgage-backed	–	94,189	–	–	94,189	a
U.S. corporate	–	473,149	–	–	473,149	a
U.S. corporate (commingled)	–	348,207	–	–	348,207	a
Foreign corporate	–	19,354	–	–	19,354	a
	–	1,025,861	–	–	1,025,861	
Other investments:						
Multi-strategy hedge funds	–	–	–	354,018	354,018	
Private capital funds	–	–	–	299,603	299,603	
Defensive equity funds (commingled)	–	19,323	–	–	19,323	a
Real estate	–	27,094	–	–	27,094	a
Limited partnership	–	–	48,000	–	48,000	c
	–	46,417	48,000	653,621	748,038	
Total investments	1,482,825	1,272,907	48,000	653,621	3,457,353	
Other assets:						
Real estate held for sale	–	710	–	–	710	a
Total assets	$1,482,825	$1,273,617	$48,000	$653,621	$3,458,063	
Other liabilities:						
Interest rate swap	$ –	$ 5,980	$ –	$ –	$ 5,980	b
Annuity/unitrust liabilities	–	8,760	–	–	8,760	b
Total liabilities	$ –	$ 14,470	$ –	$ –	$ 14,470	

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

The following represents financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2022 (in thousands). Alternative investments are accounted for using NAV, which is not a fair value measurement.

	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Active Markets for Identical Assets (Level 3)	NAV	Total	Valuation Technique (a, b, c)
Investments						
Liquid investments:						
Cash equivalents	$ 1,341	$ –	$ –	$ –	$ 1,341	a
Equity securities:						
U.S. equity	627,030	–	–	–	627,030	a
Foreign equity	513,369	–	–	–	513,369	a
Foreign equity (commingled)	–	266,915	–	–	266,915	a
	1,140,399	266,915	–	–	1,407,314	
Fixed income securities:						
U.S. government	–	54,573	–	–	54,573	a
U.S. government agencies	–	17,932	–	–	17,932	a
U.S. federal agency mortgage-backed	–	91,030	–	–	91,030	a
U.S. corporate	–	461,597	–	–	461,597	a
U.S. corporate (commingled)	–	322,350	–	–	322,350	a
Foreign corporate	–	17,362	–	–	17,362	a
	–	964,844	–	–	964,844	
Other investments:						
Multi-strategy hedge funds	–	–	–	372,822	372,822	
Private capital funds	–	–	–	284,324	284,324	
Defensive equity funds (commingled)	–	17,726	–	–	17,726	a
Real estate	–	27,094	–	–	27,094	a
Limited partnership	–	–	48,000	–	48,000	c
	–	44,820	48,000	657,146	749,966	
Total investments	1,141,740	1,276,579	48,000	657,146	3,123,465	
Other assets:						
Real estate held for sale	–	710	–	–	710	a
Total assets	$1,141,740	$1,277,289	$ 48,000	$ 657,146	$3,124,175	
Other liabilities:						
Interest rate swap	$ –	$ 3,023	$ –	$ –	$ 3,023	b
Annuity/unitrust liabilities	–	8,614	–	–	8,614	b
Total liabilities	$ –	$ 11,637	$ –	$ –	$ 11,637	

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

As of March 31, 2023 and September 30, 2022, the Level 2 instruments listed in the fair value hierarchy table above use the following valuation techniques and inputs:

U.S. Government Securities

The fair value of investments in U.S. government securities, classified as Level 2, was primarily determined using techniques consistent with the market approach. Significant observable inputs to the market approach include data points for benchmark constant maturity curves and spreads.

U.S. and Foreign Corporate Bonds

The fair value of the investments in U.S. and foreign corporate bonds, including mutual and commingled funds that invest primarily in such bonds, classified as Level 2, was primarily determined using techniques that are consistent with the market approach. Significant observable inputs include benchmark yields, reported trades, observable broker/dealer quotes, issuer spreads, and security specific characteristics (such as early redemption options).

Real Estate – Investments and Held for Sale

The fair values of the real estate investments and real estate held for sale were classified as Level 2 and were primarily determined using techniques that are consistent with the market approach. Significant observable inputs include sales of comparable properties, market rents, and market rent growth trends.

Annuity/Unitrust Liabilities

The fair value of the annuity/unitrust liabilities as Level 2 was primarily determined using techniques that are consistent with the income approach. Significant observable inputs to the income approach include data points for benchmark constant maturity curves and spreads.

Commingled Funds

The fair value of commingled fund investments classified as Level 2 was determined using fair value. The values for underlying investments are fair value estimates determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth, and other business and market sector fundamentals. Due to the significant unobservable inputs present in these valuations, Scripps Health classifies all such investments as Level 2.

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

Limited Partnership

In 2021, Scripps Health recognized receipt of a donated nonmarketable equity interest in a limited partnership measured at fair value based on a third-party analysis using discounted cash flow and adjusted book value method. Significant unobservable inputs were a discount rate of 10.0% to the after-tax cash flows and a discount for lack of full control in the limited partnership of 2.0%. The limited partnership is measured on a recurring basis and classified as Level 3 within the fair value hierarchy. Management elected the measurement alternative to value the interest in the limited partnership without a readily determinable fair value which requires a qualitative assessment to indicate if the investment is impaired and the fair value of the investment is less than its carrying value. At March 31, 2023, and September 30, 2022, Scripps Health performed a qualitative assessment to consider impairment indicators to evaluate whether the investment is impaired. No impairment was recognized.

Interest Rate Swap

The fair value of the interest rate swap liability classified as Level 2 is based on independent valuations obtained and is determined by calculating the fair value of the discounted cash flows of the differences between the fixed interest rate of the interest rate swaps and the counterparty's forward LIBOR curve, which is the input used in the valuation, also taking into account any nonperformance risk.

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

Included within the assets above are investments in certain entities that report fair value. The following table (in thousands) and explanations identify attributes relating to the nature and risk of such investments:

	March 31, 2023	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Commingled:				
Equity securities[1]	$ 200,629	$ –	Daily	Same day
Fixed income securities[2]	348,207	–	Daily	15 days
	$ 548,836	$ –		
Alternative investments:				
Hedge funds[3]	$ 354,018	$ –	Monthly to biennially	45 to 90 days
Private capital[4]	299,603	248,988	N/A	N/A
Defensive equity (commingled)[5]	19,323	–	Monthly	5 days
	$ 672,944	$ 248,988		

	September 30, 2022	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Commingled:				
Equity securities[1]	$ 266,915	$ –	Monthly	10 days
Fixed income securities[2]	322,350	–	Daily	15 days
	$ 589,265	$ –		
Alternative investments:				
Hedge funds[3]	$ 372,822	$ –	Monthly to biennially	45 to 90 days
Private capital[4]	284,324	278,009	N/A	N/A
Defensive equity (commingled)[5]	17,726	–	Monthly	5 days
	$ 674,872	$ 278,009		

NOTE (2) FAIR VALUE MEASUREMENTS (CONTINUED)

(1) Commingled funds: Equity – This category includes investments in commingled funds with underlying investments that are fair value estimates determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth, and other business and market sector fundamentals. The investments are diversified by geography, sector, and organization. Liquidity is provided on a daily abasis.

(2) Commingled funds: Fixed income – This category includes investments in one commingled fund with underlying investments that are fair value estimates determined either internally or by an external fund manager based on recent filings, operating results, balance sheet stability, growth, and other business and market sector fundamentals. The investments are diversified by geography, sector, maturity, and issue. Liquidity is provided on a daily basis. As of March 31, 2023, the category consisted of 100% daily liquidity.

(3) Hedge funds – This category includes investments in fifteen multi-strategy funds with underlying investments that are fair value estimates determined by a third-party administrator based on recent filings, operating results, balance sheet stability, growth, and other business and market sector fundamentals. The investments are diversified by geography, sector, and organization. Liquidity is provided on a monthly, quarterly, and annual basis. As of March 31, 2023, the category consisted of 13.3% monthly liquidity, 66.7% quarterly liquidity, 6.7% annual liquidity and 13.3% illiquid.

(4) Private capital – This category includes investments in thirty-two private capital funds with underlying investments that are fair value estimates determined either internally or by a third-party administrator based on recent filings, operating results, balance sheet stability, growth, and other business and market sector fundamentals. The investments are diversified by geography, sector, maturity, and issue. All funds have liquidity in excess of one year.

(5) Defensive equity – This category includes an investment in a commingled defensive equity fund with underlying investments that are fair value estimates determined by a third-party administrator as of the end of each calendar month (or more frequently in the event that interests are purchased or withdrawn intra-month), determined by its assets less its liabilities. The underlying investments consist primarily of money market funds and/or cash; short-term investments, including U.S. Treasuries and other high-quality government or corporate bonds; and written options. Liquidity is provided on a monthly basis.

NOTE (3) ENDOWMENTS

The Organization's endowments consist of 92 and 90 individual funds as of March 31, 2023 and 2022, established for a variety of purposes. Net assets associated with the endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

California Senate Bill No. 1329 enacted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) for California. The Organization is subject to UPMIFA and, thus, classifies amounts in its donor-restricted endowment funds as net assets with donor restrictions because those net assets are time restricted until the Board of Trustees appropriates such amounts for expenditures. Most of those net assets also are subject to purpose restrictions that must be met before reclassifying those net assets to net assets without donor restrictions. The Board of Trustees of the Organization has interpreted as not requiring the maintenance of purchasing power of the original gift amount contributed to an endowment fund, unless a donor stipulates to the contrary. As a result of this interpretation, when reviewing its donor-restricted endowment funds, the Organization considers a fund to be underwater if the fair value of the fund is less than the sum of (a) the original value of initial and subsequent gift amounts donated to the fund and (b) any accumulations to the fund that are required to be maintained in perpetuity in accordance with the direction of the applicable donor gift instrument.

The Organization has interpreted UPMIFA to permit spending from underwater funds in accordance with the prudent measures required under law. In accordance with UPMIFA, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) duration and preservation of the fund, (2) purposes of the Organization and the donor-restricted endowment fund, (3) general economic conditions, (4) possible effect of inflation or deflation, (5) expected total return from income and the appreciation of investments, (6) other resources of the Organization, and (7) investment policies of the Organization.

The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results while assuming a moderate level of investment risk. The Organization expects its endowment funds, over time, to provide an average rate of return of approximately 5% over the rate of inflation annually. Actual returns in any given year may vary from this amount.

NOTE (3) ENDOWMENTS (CONTINUED)

To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that places an emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

The Organization has a policy of appropriating for distribution 4% (with an additional 1% administrative fee) of its endowment fund's average fair value over the prior three-year rolling average market values. In establishing this policy, the Organization considered the long-term expected return on its endowment. Accordingly, over the long term, the Organization expects the current spending policy to allow its endowment to grow at an average of 3% to 4% annually above inflation. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return. The Organization has a policy that prohibits spending from underwater endowment funds.

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or UPMIFA requires Scripps Health to retain as a fund of perpetual duration. Deficiencies of this nature exist in two donor-restricted endowment funds, which in aggregate have an original gift value of approximately $510,000, a current fair value of $489,000and a deficiency of $21,000 as of March 31, 2023.

Changes in donor restricted endowment funds for the six months ended March 31, 2023, and 2022 are as follows (in thousands):

	2023	2022
Donor restricted endowment funds as of beginning of year	$ 116,801	$ 139,574
Investment return, net	11,656	(1,070)
Contributions	110	62
Appropriation of endowment assets for expenditure	(3,218)	(2,566)
Other changes	(1,376)	(1,321)
Donor restricted endowment funds as of end of period	$ 123,973	$ 134,679

NOTE (4) GOODWILL

Impairment assessments of the carrying amount of goodwill are completed annually, or whenever impairment indicators are present for SMF, which includes Scripps Clinic and Scripps Coastal Medical Centers. At March 31, 2023 and September 30, 2022 the amount of goodwill totaled approximately $58,310,000. No impairment or additions to goodwill were recorded for the six months ended March 31, 2023.

NOTE (5) LEASES

The Organization leases certain medical equipment and medical office properties under various operating and finance leases. These leases have remaining lease terms ranging from one to twenty. Many of the Organization's leases have rental escalation clauses which have been factored into the determination of lease payments. Generally, the Organization does not include renewal options in the lease terms for calculating the lease liability, as the Organization maintains operational flexibility and is not reasonably certain that renewal options will be exercised. The leases do not provide a readily determinable implicit rate in the contract; therefore, the risk-free rate is estimated to discount the lease payments based on information available at lease commencement. The Organization did not elect to implement the hindsight practical expedient.

The Organization elected the package of practical expedients permitted under the transition guidance within the new standard which, among other things, allowed the historical lease classification not to be reassessed. The Organization made an accounting policy election to not apply the recognition requirements of the guidance to short-term leases with a term of 12 months or less. The Organization also made an accounting policy election to not separate non-lease components from lease components for equipment and real estate.

The components of the right-of-use assets and lease liabilities consist of the following at March 31, 2023 and March 31, 2022 (in thousands):

		2023	2022
Property, Plant and Equipment, net			
Finance leases, net	$	4,205	7,946
Right-of-use assets			
Operating leases	$	244,255	240,733
Finance Leases Liabilities			
Current portion of long-term debt	$	2,465	3,928
Long-term debt		2,205	4,670
	$	4,670	8,598
Operating Lease Liabilities			
Current portion of lease liability	$	29,700	28,551
Long-term lease liability		219,007	224,445
	$	248,707	252,996

NOTE (5) LEASES (CONTINUED)

The components of lease expense reported within Other Services of Obligated Statement of Operations are for the six months ended March 31, 2023, and March 31, 2022 as follows (in thousands):

	2023	2022
Lease/rental cost:		
Amortization of right-of-use assets	$ 1,300	$ 2,448
Interest on lease liabilities	61	94
Total finance lease cost	1,361	2,542
Operating lease cost	18,530	16,344
Short-term and variable lease cost	5,251	2,239
Total lease/rental cost	$ 25,142	$ 21,125
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from finance leases	$ 61	$ 94
Operating cash flows from operating leases	16,529	15,377
Financing cash flows from finance leases	1,391	2,528
Total	$ 17,981	$ 17,999
Right-of-use assets obtained in exchange for new operating lease liabilities	$ 7,301	$ 1,953
Right-of-use assets obtained in exchange for new financing lease liabilities	$ -	$ 240
Weighted average remaining lease term - finance leases	2.0 years	2.5 years
Weighted average remaining lease term - operating leases	11.3 years	12.4 years
Weighted average discount rate - finance leases	2.20%	2.16%
Weighted average discount rate – operating leases	1.18%	1.07%

NOTE (5) LEASES (CONTINUED)

Scheduled maturities of lease liabilities at March 31, 2023 were as follows:

		Undiscounted Finance Lease Payments	Imputed Interest	Finance Lease Liabilities
2023**	$	1,331	46	1,285
2024		2,403	51	2,352
2025		985	9	976
2026		57	-	57
Total	$	4,776	106	4,670

		Undiscounted Operating Lease Payments	Imputed Interest	Operating Lease Liabilities
2023**	$	16,279	1,553	14,726
2024		32,241	2,779	29,462
2025		30,570	2,345	28,225
2026		28,997	1,926	27,071
2027		23,005	1,545	21,460
2028		16,297	1,301	14,996
Thereafter		118,437	5,669	112,768
Total		265,826	17,118	248,708

** Excluding the six months ended March 31, 2023.

In September 2022, the Organization entered into a sale and leaseback transaction for the sale of property and three of the Organization's corporate administrative buildings thereon. The leaseback arrangements provide the Organization with free rent for approximately 18 months to accommodate new construction of build-to-suit administrative office space. The gain on the sale was $87,116,000, which includes $11,520,000 related to the leaseback arrangements. The gain on sale is recognized within the obligated financial statements as other operating revenues as of September 30, 2022.

NOTE (6) OTHER EVENTS

<u>Federal Public Assistance Grants Program</u>

In March 2023, Scripps accrued $25.3 million in other operating revenue based on notification letters received from California Office of Emergency Services ("CALOES") notifying us of satisfaction of all requirements for reimbursement requests totaling $25.3 million. Payments totaling this amount were received in April 2023.

NOTE (7) SUBSEQUENT EVENTS

The Organization has evaluated events and transactions occurring subsequent to March 31, 2023 through April 26, 2023, the date the financial statements were issued. During this period, there were no subsequent events requiring recognition in the financial statements.

Scripps

SCRIPPS HEALTH
OBLIGATED GROUP FINANCIAL STATEMENTS
MANAGEMENT DISCUSSION AND ANALYSIS
FOR THE QUARTER AND SIX MONTHS ENDED MARCH 31, 2023

	For the Quarter Ended ($000s)	
	March 31, 2023	March 31, 2022
	Actual	Actual
Operating Revenue	$1,006,834	$896,003
Operating Loss	($21,453)	($13,412)
Operating Margin	-2.1%	-1.5%
Operating EBITDA	$32,159	$43,710
Operating EBITDA Margin	3.2%	4.9%
Excess Margin	$122,739	($204,611)
Excess Margin %	10.7%	-29.0%

Scripps Health's ("**Scripps**") operating revenue for the quarter ended March 31, 2023 (the "**Quarter**") of $1,006.8 million was $110.8 million higher (+12.4%) than the quarter ended March 31, 2022 (the "**Prior Quarter**"). The increase was primarily attributable to higher patient volumes in the Quarter. Hospital activity, as measured by adjusted discharges, was up 14.4% as compared to the Prior Quarter, and physician foundation activity, as measured by wRVUs, was up 10.9%.

Operating expenses of $1,029.0 million in the Quarter were $119.4 million higher (+13.1%) as compared to the Prior Quarter, with the increase primarily attributable to a $58.2 million increase in labor expense due to high volume and annual merit / market increase, a $22.7 million increase in supplies ($9.3 million for pharmaceuticals, $4.0 million for prosthesis, and $3.1 million medical supplies), a $21.8 million increase in other services, and a $20.1 million increase in physician services expense. This is offset primarily by a $6.4 million positive adjustment to depreciation expense based on the implementation of revised useful life schedules.

Scripps generated non-operating gains of $144.2 million in the Quarter, driven primarily by the broad-based improvement in the investment markets.

Excess margin for the Quarter of $122.7 million was $327.4 million higher than the Prior Quarter, primarily due to the improvement in investment markets noted above.

	For the Six Months Ended ($000s)	
	March 31, 2023	March 31, 2022
	Actual	Actual
Operating Revenue	$2,000,675	$1,836,075
Operating (Loss) / Gain	($13,219)	$8,976
Operating Margin	-0.7%	0.5%
Operating EBITDA	$92,951	$122,859
Operating EBITDA Margin	4.6%	6.7%
Excess Margin	$286,393	($89,554)
Excess Margin %	12.5%	-5.2%

Scripps Health's ("**Scripps**") operating revenue for the year ended March 31, 2023 (the "**Year**") of $2,000.7 million was $164.6 million higher (+9.0%) than the year ended March 31, 2022 (the "**Prior Year**"). The increase was primarily attributable to higher patient volumes in the Year. Hospital activity, as measured by adjusted discharges, was up 11.3% as compared to the Prior Year, and physician foundation activity, as measured by wRVUs, was up 14.1%.

Operating expenses of $2,014.7 million in the Year were $187.7 million higher (+10.3%) as compared to the Prior Year, with the increase primarily attributable to a $93.6 million increase in labor expense due to higher volume and annual merit / market increases, a $39.8 million increase in physician services expense, a $35.0 million increase in other services, and $28.3 million increase in supplies ($14.3 million for pharmaceuticals). This is offset primarily by a $13.5 million positive adjustment to depreciation expense based on the implementation of revised useful life schedules.

Scripps generated non-operating gains of $299.6 million in the Year, driven primarily by the broad-based improvement in the investment markets.

Excess margin for the Year of $286.4 million was $375.9 million higher than the Prior Year, primarily due to the improvement in investment markets noted above.

	March 31, 2023	March 31, 2022	September 30, 2022
Unrestricted Cash & Investments ($000s)	$3,281,709	$3,764,580	$3,219,704
Days Unrestricted Cash on Hand	318.1	411.5	329.6
Days in AR, Net	43.3	53.4	46.8
Accounts Payable & Accrued Liabilities ($000s)	$544,419	$647,495	$308,397
Days in AP & Accrued Liabilities	52.8	70.8	64.7
Unrestricted Cash & Investments to Total Debt	238.2%	266.6%	228.5%
Long Term Debt ($000s)	$1,338,257	$1,087,410	$1,276,274
Current Portion of Long-Term Debt ($000s)	$39,432	$324,484	$132,955
Total Debt ($000s)	$1,377,689	$1,411,894	$1,409,229
Long-Term Debt to Capitalization	22.5%	22.5%	24.1%

SIGNIFICANT TRANSACTIONS

Provider Fee Program

In September 2022, CMS approved the January 1, 2022 through December 31, 2022 provider fee program. Scripps Health recognized program revenues and expenses on the accrual basis once the Federal waiver has been approved. The estimated total net benefit for Scripps Health for the entire program is $20 million. In FY2022, a net benefit of $15 million was recorded based on CHA model for the program period of January 2022 to September 2022. In FY2023, a net benefit of $5 million was recorded based on CHA model for the program period of October 2022 to December 2022.

Credit Ratings

During October 2022, S&P affirmed Scripps Health ratings at AA with stable outlook. Fitch's rating is expected to be published in early 2023. At Scripps' request, Moody's Investors Service withdrew its rating for Scripps Health.

Taxable and Tax-Exempt Bonds

In FY2023, Scripps Health made scheduled annual bond principal payments amounting to $34.9 million. In addition, Scripps Health defeased total $9.7 million of the 2007A, 2010BC, and 2019A bonds that financed the corporate office buildings' capital expenditures during first quarter of FY2023.

Line of Credit

In November 2022, Scripps repaid the $84 million drawn on its $300 million line of credit. In March 2023, Scripps Health drew down $100 million line of credit.

Federal Public Assistance Grants Program

In March 2023, Scripps accrued $25.3 million in other operating revenue based on notification letters received from California Office of Emergency Services ("**CALOES**") notifying us of satisfaction of all requirements for reimbursement requests totaling $25.3 million. Payments totaling this amount were received in April 2023.