

Advocate Aurora Health, Inc.

Condensed Consolidated Financial Statements and Other Information

As of and for the Year Ended December 31, 2020



ADVOCATE AURORA HEALTH, INC.
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ADVOCATE AURORA HEALTH, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

	Note 1	
	December 31, 2020	December 31, 2019
Assets		
Current assets		
Cash and cash equivalents	\$ 959,878	\$ 449,712
Assets limited as to use	125,053	106,529
Patient accounts receivable	1,570,738	1,605,607
Other current assets	686,686	619,542
Third-party payors receivables	16,933	15,331
Collateral proceeds under securities lending program	19,789	18,284
Total current assets	<u>3,379,077</u>	<u>2,815,005</u>
Assets limited as to use	11,107,210	9,140,565
Property and equipment, net	5,851,977	5,901,923
Other assets		
Goodwill and intangible assets, net	82,752	76,830
Investments in unconsolidated entities	210,303	212,415
Reinsurance receivable	50,514	52,312
Operating lease right-of-use assets	309,678	352,295
Other noncurrent assets	458,132	382,024
Total other assets	<u>1,111,379</u>	<u>1,075,876</u>
Total assets	<u>\$ 21,449,643</u>	<u>\$ 18,933,369</u>

(Continued)

ADVOCATE AURORA HEALTH, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

	Note 1	
	December 31, 2020	December 31, 2019
Current liabilities		
Long-term debt and commercial paper, current portion	\$ 101,996	\$ 184,098
Long-term debt subject to short-term financing arrangements	119,660	147,535
Operating lease liabilities, current portion	79,934	77,957
Accrued salaries and employee benefits	1,207,672	950,391
Accounts payable and other accrued liabilities	1,341,619	912,644
Third-party payors payables	318,801	303,300
Accrued insurance and claim costs, current portion	130,391	114,741
Collateral under securities lending program	19,789	18,284
Total current liabilities	3,319,862	2,708,950
Noncurrent liabilities		
Long-term debt, less current portion	3,310,401	2,729,366
Operating lease liabilities, less current portion	268,575	314,106
Accrued insurance and claims cost, less current portion	593,739	544,839
Accrued losses subject to insurance recovery	50,514	52,312
Obligations under swap agreements	118,620	91,340
Other noncurrent liabilities	1,387,888	793,792
Total noncurrent liabilities	5,729,737	4,525,755
Total liabilities	9,049,599	7,234,705
Net assets		
Without donor restrictions		
Controlling interest	12,012,719	11,309,819
Noncontrolling interest in subsidiaries	154,645	146,740
Total net assets without donor restrictions	12,167,364	11,456,559
With donor restrictions	232,680	242,105
Total net assets	12,400,044	11,698,664
Total liabilities and net assets	\$ 21,449,643	\$ 18,933,369

Note 1: December 31, 2020 financial statement information was derived from and should be read in conjunction with the Advocate Aurora Health, Inc. consolidated audited financial statements as of and for the year ended December 31, 2020, available on the Electronic Municipal Market Access website (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 December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Revenue				
Patient service revenue	\$ 2,895,963	\$ 2,801,599	\$ 10,216,386	\$ 10,660,969
Capitation revenue	275,207	311,271	1,121,428	1,264,162
Other revenue	492,971	250,758	1,794,375	880,292
Total revenue	<u>3,664,141</u>	<u>3,363,628</u>	<u>13,132,189</u>	<u>12,805,423</u>
Expenses				
Salaries, wages and benefits	1,929,912	1,832,815	7,427,903	6,988,562
Supplies, purchased services and other	1,180,534	1,048,312	4,200,203	3,999,005
Contracted medical services	105,628	127,040	502,420	543,716
Depreciation and amortization	140,260	154,027	560,215	569,956
Interest	28,248	24,506	112,126	106,314
Total expenses	<u>3,384,582</u>	<u>3,186,700</u>	<u>12,802,867</u>	<u>12,207,553</u>
Operating income before nonrecurring expenses	279,559	176,928	329,322	597,870
Nonrecurring expenses	<u>39,666</u>	<u>22,210</u>	<u>116,355</u>	<u>116,800</u>
Operating income	239,893	154,718	212,967	481,070
Nonoperating income (loss)				
Investment income, net	784,365	341,130	593,283	1,053,898
Loss on debt refinancing	—	(21,665)	(12,244)	(21,665)
Change in fair value of interest rate swaps	5,768	13,219	(27,280)	(21,079)
Pension settlement loss	—	—	(119,658)	—
Other nonoperating (loss) income, net	(16,279)	(32,051)	(38,943)	54,473
Total nonoperating income, net	<u>773,854</u>	<u>300,633</u>	<u>395,158</u>	<u>1,065,627</u>
Revenue in excess of expenses	1,013,747	455,351	608,125	1,546,697
Less noncontrolling interest	<u>(20,815)</u>	<u>(19,465)</u>	<u>(50,093)</u>	<u>(60,749)</u>
Revenue in excess of expenses - attributable to controlling interest	\$ 992,932	\$ 435,886	\$ 558,032	\$ 1,485,948

(Continued)

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

	Unaudited		Note 1	
	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Net assets without donor restrictions, controlling interest				
Revenue in excess of expenses - attributable to controlling interest	\$ 992,932	\$ 435,886	\$ 558,032	\$ 1,485,948
Pension-related changes other than net periodic pension costs	31,093	(222,059)	138,208	(106,221)
Net assets released from restrictions for purchase of property and equipment	1,677	1,154	6,206	4,839
Other, net	47	73	454	1,108
Increase in net assets without donor restrictions, controlling interest	1,025,749	215,054	702,900	1,385,674
Net assets without donor restrictions, noncontrolling interest				
Revenues in excess of expenses	20,815	19,465	50,093	60,749
Distributions to noncontrolling interest	(13,974)	(9,096)	(41,948)	(32,488)
Other, net	(240)	—	(240)	11
Increase in net assets without donor restrictions, noncontrolling interest	6,601	10,369	7,905	28,272
Net assets with donor restrictions				
Contributions	5,977	8,628	22,971	27,627
Investment income, net	11,405	4,518	9,948	14,400
Net assets released from restrictions for operations	(6,756)	(5,379)	(17,074)	(18,596)
Net assets released from restrictions for purchase of property and equipment	(1,677)	(1,154)	(6,206)	(4,839)
Central IL net assets with donor restrictions sold	—	—	(18,949)	—
Other, net	87	(1,118)	(115)	(278)
Increase (decrease) in net assets with donor restrictions	9,036	5,495	(9,425)	18,314
Increase in net assets	1,041,386	230,918	701,380	1,432,260
Net assets at beginning of period	11,358,658	11,467,746	11,698,664	10,242,977
Adoption of ASU 2016-02 (Leases)	—	—	—	23,427
Net assets at end of period	\$ 12,400,044	\$ 11,698,664	\$ 12,400,044	\$ 11,698,664

Note 1: December 31, 2020 financial statement information was derived from and should be read in conjunction with the Advocate Aurora Health, Inc. consolidated audited financial statements as of and for the year ended December 31, 2020, available on the Electronic Municipal Market Access website (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 December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Cash flows from operating activities				
Increase in net assets	\$ 1,041,386	\$ 230,918	\$ 701,380	\$ 1,432,260
Adjustments to reconcile change in net assets to net cash provided by operating activities:				
Depreciation, amortization and accretion	138,312	155,848	555,515	564,270
Amortization of operating lease right-of-use assets	14,425	13,372	63,840	64,801
Loss on debt refinancing	—	21,665	12,244	21,665
Loss on sale of property and equipment	327	(269)	12,571	2,618
Change in fair value of swap agreements	(5,768)	(13,219)	27,280	21,079
Pension-related changes other than net periodic pension cost	(31,093)	222,059	(138,208)	106,221
Net assets released from restrictions for operations	(6,756)	(5,379)	(17,074)	(18,596)
Distribution to noncontrolling interest	13,973	845	50,205	29,446
Distributions from unconsolidated entities	2,883	13,936	14,951	23,707
Gain on Bay Area Medical Center acquisition	—	—	—	(81,736)
Loss on sale of Central IL disposal group	—	—	21,346	—
Central IL net assets with donor restrictions sold	—	—	18,949	—
Changes in operating assets and liabilities				
Trading securities, net	(1,359,739)	(530,859)	(2,025,066)	(1,433,305)
Accounts receivable, net	(82,857)	(7,089)	31,871	(103,625)
Accounts payable and accrued liabilities	708,931	28,657	1,006,265	203,877
Third-party payors receivable and payable, net	(756,302)	(18,852)	16,896	1,640
Other assets and liabilities, net	245,080	(9,092)	240,620	(280,549)
Net cash (used in) provided by operating activities	(77,198)	102,541	593,585	553,773
Cash flows from investing activities				
Capital expenditures	(187,619)	(181,960)	(703,611)	(653,207)
Proceeds from sale of property and equipment	95	2,341	1,998	4,102
Purchases of investments designated as non-trading, net	7	2,278	241	69
Investments in unconsolidated entities, net	(5,000)	(2,646)	(8,016)	(31,005)
Cash received from sale of Central IL disposal group	—	—	190,000	—
Investments acquired in Bay Area Medical Center acquisition	—	—	—	34,018
Other	(12,106)	(6,659)	(15,879)	(7,534)
Net cash used in investing activities	(204,623)	(186,646)	(535,267)	(653,557)
Cash flows from financing activities				
Proceeds from issuance of debt	—	439,970	695,915	496,074
Repayments of long-term debt	(10,015)	(450,789)	(226,781)	(544,046)
Distribution to noncontrolling interest	(13,973)	(845)	(50,205)	(29,446)
Proceeds from restricted contributions and income on investments	17,382	13,146	32,919	42,027
Net cash (used in) provided by financing activities	(6,606)	1,482	451,848	(35,391)
Net (decrease) increase in cash and cash equivalents	(288,427)	(82,623)	510,166	(135,175)
Cash and cash equivalents at beginning of period	1,248,305	532,335	449,712	584,887
Cash and cash equivalents at end of period	\$ 959,878	\$ 449,712	\$ 959,878	\$ 449,712

Supplemental disclosures of noncash information

Operating lease right-of-use assets in exchange for new operating lease liabilities	\$	5,553	\$	6,269	\$	24,272	\$	425,142
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Note 1: December 31, 2020 financial statement information was derived from and should be read in conjunction with the Advocate Aurora Health, Inc. consolidated audited financial statements as of and for the year ended December 31, 2020, available on the Electronic Municipal Market Access website (www.emma.msrb.org).

See accompanying notes to condensed consolidated financial statements.

ADVOCATE AURORA HEALTH, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2020
(in thousands)

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 24 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 and central Illinois and eastern Wisconsin.

On April 1, 2019, the System became the sole corporate member of Bay Area Medical Center ("BAMC") through the acquisition of the remaining 51% interest in BAMC and its results have been fully consolidated into the condensed consolidated financial statements of the System as of this date. The acquisition will improve the availability, scope and access to health care in the communities served by BAMC.

Basis of Presentation

The accompanying condensed consolidated financial statements as of and for the year ended December 31, 2020, 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 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, 2020. 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>.

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.

At various times in 2020 and at various locations the System postponed or canceled elective procedures to comply with public health protocols. This, along with the growth in the volume of COVID-19 patients, had a negative impact on operations and revenues and has also caused the System to estimate the timing, source and rate of reimbursement for COVID-19 related patient care.

The 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 is monitoring liquidity and cash flow and has taken, and will continue to take, steps to protect its fiscal health, including a focus on maintaining liquidity to meet its obligations. In addition, the System has 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.

For the three months and year ended December 31, 2020, the System received \$190,655 and \$786,655, respectively, 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 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 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. For the three months and year ended December 31, 2020, the System recognized approximately \$37,000 of revenue for the employee retention tax credit, which is included in other operating revenue within the condensed consolidated statement of operations and changes in net assets and a corresponding receivable that is included in other current assets in the 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 approximately \$773,000 from the Centers for Medicare and Medicaid Services ("CMS") as an advance payment for Medicare services during 2020. The funds are provided through the expansion of the Medicare Accelerated and Advance Payment Program to ensure providers and suppliers have the resources needed to combat the COVID-19 pandemic. The advances will be 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. Recoupments are scheduled to begin in April 2021. Subsequent to the twenty-nine month recoupment period any unpaid remaining balance is subject to an interest charge of 4 percent

per annum. Medicare accelerated and advance payments of approximately \$285,000 and \$488,000 are included in accounts payable and other accrued liabilities and other noncurrent liabilities, respectively, within the condensed consolidated balance sheets at December 31, 2020. 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. Through December 31, 2020, the System deferred approximately \$215,000 of these taxes. At December 31, 2020, approximately \$107,500 is included in accrued salaries and employee benefits and other noncurrent liabilities, respectively, within the condensed consolidated balance sheets.

On July 1, 2020, the System sold a majority of the assets and certain liabilities (the "disposal group") related to operations of the System in Central Illinois. The disposal group had assets sold in excess of liabilities transferred of \$205,273, consisting primarily of property and equipment and certain investment interests in unconsolidated entities. The purchase price for the disposal group was \$190,000. The System recorded a loss, inclusive of selling costs, of \$21,346 that is included in nonrecurring expenses in the condensed consolidated financial statements.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of the 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 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 (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 (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 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 (first-in, first-out) or market. Retail pharmaceutical inventories are stated at replacement cost.

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 \$63,740 and \$62,172 is included in goodwill and intangible assets, net in the accompanying condensed consolidated balance sheets at December 31, 2020 and 2019, respectively. In 2019, the System 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 of \$1,857, \$7,255 and \$6,982 is included in depreciation and amortization in the accompanying condensed consolidated statements of operations and changes in net assets for the three months ended December 31, 2020 and the years ended December 31, 2020 and 2019, respectively. 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 years ended December 31, 2020 and 2019.

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 assets 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 cost or equity method. 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. All other unconsolidated entities are accounted for using the cost method. The income (loss) on health care-related unconsolidated entities is included in other revenue in the accompanying condensed consolidated statements of operations and changes in net assets. The income or loss on non-health-related unconsolidated entities is included within other nonoperating (loss) income, net.

Derivative Financial Instruments

The System has entered into transactions to manage its interest rate, credit and market risks. Derivative 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 formation of the System, the implementation of an electronic medical records and billing system, the implementation of an enterprise resource planning system and, as part of the initiative to reduce operating expenses, an early retirement incentive program and position restructuring. Also recorded in nonrecurring expenses is the loss incurred on the divestiture of Central Illinois disposal group (see Note 2. SIGNIFICANT EVENTS). Due to the nature of these expenses, the costs were recorded 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 a gain on the acquisition of BAMC, 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 in Excess of Expenses and Changes in Net Assets

The accompanying condensed consolidated statements of operations and changes in net assets includes the revenue in excess of expenses as the performance indicator. Changes in net assets without donor restrictions, which are excluded from revenue 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 February 2016, the Financial Accounting Standards Board ("FASB") issued ASU 2016-02, Leases (Topic 842). This guidance introduced a lessee model that brings most leases on to the balance sheet. The standard also aligns certain of the underlying principles of the new lessor model with those in ASU 2014-09, the revenue recognition standard. This standard was adopted by the System effective January 1, 2019, using the modified retrospective approach. The System elected the package of practical expedients permitted under the transition guidance within the new standard, which among other things, allowed the System to carry forward the historical lease classification.

The System recorded a right-of-use asset of \$388,097, which is net of tenant improvements previously recorded prior to adoption, and right-of-use liabilities of \$426,794 due to the adoption of this standard on January 1, 2019. Additionally, the System recognized a cumulative-effect adjustment of \$23,427 to net assets without donor restrictions on January 1, 2019, related to the deferred gains on various sale-leaseback transactions.

In August 2018, the FASB issued ASU 2018-15, *Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. This guidance requires an entity in a hosting arrangement that is a service contract to follow the guidance in Subtopic 350-40 to determine which implementation costs to capitalize as an asset and which costs to expense as incurred. Also, this guidance requires the entity to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. Further, the guidance requires the entity to present the expense related to the capitalized implementation costs in the same line item in the consolidated statement of operations and changes in net assets as the fees associated with the hosting element (service) of the arrangement and classify payments for capitalized implementation costs in the consolidated statement of cash flows in the same manner as payments made for fees associated with the hosting element. The entity is also required to present the capitalized implementation costs in the condensed consolidated balance sheets in the same line item that a prepayment for the fees of the associated hosting arrangement would be presented. This guidance is effective for fiscal years beginning after December 15, 2020, and interim periods within annual periods beginning after December 15, 2021. Early adoption is permitted. The System early adopted this guidance effective January 1, 2019, on a prospective basis. This guidance did not have a material impact on the System's accompanying consolidated financial statements.

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 December 31, 2020 and 2019, and the years ended December 31, 2020 and 2019 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 December 31, 2020 and 2019 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 December 31, 2020. 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:

	Classification	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Reimbursement	Patient service revenue	\$ 71,942	\$ 67,815	\$ 286,105	\$ 271,260
Assessment	Supplies, purchased services and other expense	44,350	41,306	171,312	165,222

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:

	Classification	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Reimbursement	Patient service revenue	\$ 34,270	\$ 30,974	\$ 137,317	\$ 117,150
Assessment	Supplies, purchased services and other expense	25,219	25,470	101,477	100,777

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:

Three Months Ended December 31	2020		2019	
Managed care	\$ 1,551,405	54 %	\$ 1,510,567	54 %
Medicare	810,066	27	945,841	34
Medicaid - Illinois	253,463	9	122,023	4
Medicaid - Wisconsin	134,237	5	128,078	5
Self-pay and other	146,792	5	95,090	3
	<u>\$ 2,895,963</u>	<u>100 %</u>	<u>\$ 2,801,599</u>	<u>100 %</u>

Year Ended December 31	2020		2019	
Managed care	\$ 5,521,363	53 %	\$ 5,829,566	55 %
Medicare	3,124,812	31	3,380,458	31
Medicaid - Illinois	773,851	8	694,406	7
Medicaid - Wisconsin	481,215	5	457,583	4
Self-pay and other	315,145	3	298,956	3
	<u>\$ 10,216,386</u>	<u>100 %</u>	<u>\$ 10,660,969</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 their 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:

	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Illinois	\$ 1,525,880	\$ 1,541,343	\$ 5,713,977	\$ 6,086,737
Wisconsin	1,645,290	1,571,527	5,623,837	5,838,394
Total patient service revenue and capitation	3,171,170	3,112,870	11,337,814	11,925,131
Other revenue	492,971	250,758	1,794,375	880,292
Total revenue	<u>\$ 3,664,141</u>	<u>\$ 3,363,628</u>	<u>\$ 13,132,189</u>	<u>\$ 12,805,423</u>
Hospital	\$ 2,103,100	\$ 2,047,290	\$ 7,611,197	\$ 7,859,715
Clinic	668,806	683,056	2,231,783	2,450,681
Home Care	64,965	58,681	240,043	241,151
Other	59,092	12,572	133,363	109,422
Total patient service revenue	2,895,963	2,801,599	10,216,386	10,660,969
Capitation revenue	275,207	311,271	1,121,428	1,264,162
Other revenue	492,971	250,758	1,794,375	880,292
Total revenue	<u>\$ 3,664,141</u>	<u>\$ 3,363,628</u>	<u>\$ 13,132,189</u>	<u>\$ 12,805,423</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:

	December 31, 2020		December 31, 2019	
Managed care	\$ 681,078	43 %	\$ 698,731	44 %
Medicare	350,948	22	327,723	20
Medicaid - Wisconsin	41,694	3	44,357	3
Medicaid - Illinois	188,280	12	216,618	13
Self-pay and other	308,738	19	318,178	20
	<u>\$ 1,570,738</u>	<u>100 %</u>	<u>\$ 1,605,607</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 \$4,504,346 and \$4,123,306 at December 31, 2020 and 2019, 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 December 31, 2020, the System had additional commitments to fund alternative investments, including callable distributions of \$1,406,684 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. These instruments require the System to deposit cash or securities collateral with the broker or custodian. Collateral provided was \$13,031 and \$6,770 at December 31, 2020 and 2019, respectively. The notional value of the derivatives in long positions was \$241,232 and \$104,072 at December 31, 2020 and 2019, respectively. The notional value of the derivatives in a short position was \$(91,862) and \$(58,527) at December 31, 2020 and 2019, 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 with 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 \$49,512 and \$38,355 at December 31, 2020 and 2019, respectively. Unsettled purchases resulted in payables due to brokers of \$88,890 and \$41,977 at December 31, 2020 and 2019, respectively.

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

	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Interest income and dividends	\$ 27,984	\$ 20,107	\$ 83,232	\$ 84,684
Income from alternative investments	258,058	75,904	51,675	333,212
Net realized gains	51,715	41,485	41,293	150,422
Net unrealized gains	469,726	222,385	476,794	553,287
Total	<u>\$ 807,483</u>	<u>\$ 359,881</u>	<u>\$ 652,994</u>	<u>\$ 1,121,605</u>

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

	<u>Three Months Ended December 31, 2020</u>	<u>Three Months Ended December 31, 2019</u>	<u>Year Ended December 31, 2020</u>	<u>Year Ended December 31, 2019</u>
Other revenue	\$ 11,713	\$ 14,233	\$ 49,763	\$ 53,307
Investment income, net	784,365	341,130	593,283	1,053,898
Net assets with donor restrictions	11,405	4,518	9,948	14,400
Total	<u>\$ 807,483</u>	<u>\$ 359,881</u>	<u>\$ 652,994</u>	<u>\$ 1,121,605</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:

	<u>December 31, 2020</u>	<u>December 31, 2019</u>
Internally designated for capital and other	\$ 10,291,819	\$ 8,345,172
Held for self-insurance	658,466	645,697
Donor restricted	137,980	132,024
Investments under securities lending program	18,945	17,672
Total noncurrent assets limited as to use	<u>11,107,210</u>	<u>9,140,565</u>
Cash and cash equivalents	959,878	449,712
Current assets limited as to use	125,053	106,529
Total cash and cash equivalents and assets limited as to use	<u>\$ 12,192,141</u>	<u>\$ 9,696,806</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 entity 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:

December 31, 2020	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets				
Investments				
Cash and short-term investments	\$ 1,861,490	\$ 1,296,986	\$ 564,504	\$ —
Corporate bonds and other debt securities	705,552	—	705,552	—
United States government bonds	615,723	—	615,723	—
Bond and other debt security funds	1,325,705	73,668	1,252,037	—
Non-government fixed-income obligations	18,944	—	18,944	—
Equity securities	826,194	826,194	—	—
Equity funds	2,307,912	143,521	2,164,391	—
	7,661,520	\$ 2,340,369	\$ 5,321,151	\$ —
Investments at net asset value				
Alternative investments	4,530,621			
Total investments	\$ 12,192,141			
Collateral proceeds received under securities lending program	\$ 19,789		\$ 19,789	
Liabilities				
Obligations under swap agreements	\$ (118,620)		\$ (118,620)	
Obligations to return capital under securities lending program	\$ (19,789)		\$ (19,789)	

	December 31, 2019	Quoted Prices in Active Markets for Identical Assets (Level 1)	Other Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investments				
Cash and short-term investments	\$ 909,297	\$ 872,262	\$ 37,035	\$ —
Corporate bonds and other debt securities	582,327	—	582,327	—
United States government bonds	583,429	—	583,429	—
Bond and other debt security funds	688,728	102,555	586,173	—
Non-government fixed-income obligations	26,176	—	26,176	—
Equity securities	782,581	782,581	—	—
Equity funds	1,976,779	134,951	1,841,828	—
	<u>5,549,317</u>	<u>\$ 1,892,349</u>	<u>\$ 3,656,968</u>	<u>—</u>
Investments at net asset value				
Alternative investments	4,147,489			
Total investments	<u>\$ 9,696,806</u>			
Collateral proceeds received under securities lending program	<u>\$ 18,284</u>		<u>\$ 18,284</u>	
Liabilities				
Obligations under swap agreements	<u>\$ (91,340)</u>		<u>\$ (91,340)</u>	
Obligations to return capital under securities lending program	<u>\$ (18,284)</u>		<u>\$ (18,284)</u>	

7. PROPERTY AND EQUIPMENT, NET

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

	December 31, 2020	December 31, 2019
Land and improvements	\$ 461,831	\$ 497,363
Buildings and fixed equipment	7,536,013	7,519,607
Movable equipment and computer software	2,520,502	2,496,988
Construction-in-progress	478,335	355,733
	<u>10,996,681</u>	<u>10,869,691</u>
Accumulated depreciation and amortization	(5,144,704)	(4,967,768)
Property and equipment, net	<u>\$ 5,851,977</u>	<u>\$ 5,901,923</u>

During 2020, the System wrote off fully depreciated property and equipment totaling \$233,800.

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 December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Depreciation expense	<u>\$ 141,069</u>	<u>\$ 145,654</u>	<u>\$ 553,634</u>	<u>\$ 560,221</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 consolidated balance sheets. For lease agreements entered into after the adoption of ASU 2016-02 on January 1, 2019, 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	December 31, 2020	December 31, 2019
Assets			
Operating	Operating lease right-of-use assets	\$ 309,678	\$ 352,295
Finance	Property and equipment, net	149,961	161,970
Total lease assets		<u>\$ 459,639</u>	<u>\$ 514,265</u>
Liabilities			
Current			
Operating	Operating lease liabilities, current portion	\$ 79,934	\$ 77,957
Finance	Long-term debt and commercial paper, current portion	9,182	8,445
Noncurrent			
Operating	Operating lease liabilities, less current portion	268,575	314,106
Finance	Long-term debt, less current portion	165,507	176,811
Total lease liabilities		<u>\$ 523,198</u>	<u>\$ 577,319</u>

Finance lease assets are recorded net of accumulated amortization of \$57,873 and \$49,743 as of December 31, 2020 and 2019, 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 December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Operating lease cost	Supplies, purchased services and other	\$ 21,130	\$ 21,603	\$ 85,253	\$ 85,037
Short term lease cost	Supplies, purchased services and other	2,958	2,384	13,407	10,686
Variable lease cost	Supplies, purchased services and other	9,663	8,191	36,740	29,099
Finance lease cost					
Amortization of lease assets	Depreciation and amortization	3,261	2,984	11,629	10,719
Interest on lease liabilities	Interest	2,942	3,098	12,093	10,053
Sublease income	Other revenue	(607)	(611)	(2,434)	(2,593)
Net lease cost		<u>\$ 39,347</u>	<u>\$ 37,649</u>	<u>\$ 156,688</u>	<u>\$ 143,001</u>

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

	<u>As of December 31, 2020</u>	<u>As of December 31, 2019</u>
Weighted average remaining lease term (in years)		
Operating	5.5	6.0
Finance	11.6	12.9
Weighted average discount rate		
Operating	2.24 %	2.34 %
Finance	7.54 %	7.44 %

	<u>Three Months Ended December 31, 2020</u>	<u>Three Months Ended December 31, 2019</u>	<u>Year Ended December 31, 2020</u>	<u>Year Ended December 31, 2019</u>
Cash paid for amounts included in the measurement of lease liabilities				
Operating cash flows from operating leases	\$ 22,041	\$ 21,139	\$ 88,387	\$ 86,504
Operating cash flows from finance leases	2,349	3,269	11,500	10,563
Financing cash flows from finance leases	1,407	1,910	8,184	7,605

Future maturities of lease liabilities at December 31, 2020 are as follows:

	<u>Operating Leases</u>	<u>Finance Leases</u>	<u>Total</u>
2021	\$ 86,817	\$ 19,498	\$ 106,315
2022	75,933	21,094	97,027
2023	65,018	21,031	86,049
2024	48,089	21,532	69,621
2025	33,948	21,025	54,973
Thereafter	61,813	169,777	231,590
Future minimum lease payments	371,618	273,957	645,575
Less remaining imputed interest	23,109	99,268	122,377
Total	<u>\$ 348,509</u>	<u>\$ 174,689</u>	<u>\$ 523,198</u>

9. INVESTMENTS IN UNCONSOLIDATED ENTITIES

The System contributed \$25,000 to an independent foundation in conjunction with the BAMC transaction. See the additional discussion of this transaction in Note 17. ACQUISITION OF BAY AREA MEDICAL CENTER. Under the terms of the definitive agreement between the System and BAMC, the \$25,000 contribution is designated to support the operations and capital needs of BAMC and/or Aurora Bay Area Medical Group ("ABAMG"). The interest in that foundation is reflected in investments in unconsolidated entities in the accompanying condensed consolidated balance sheets, which amounted to \$18,668 and \$21,186 at December 31, 2020 and 2019, respectively. Cash distributions of \$475 and \$2,518 were received by BAMC from this Foundation under terms of the definitive agreement during the three months and year ended December 31, 2020, respectively.

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 \$109,017 and \$95,307 at December 31, 2020 and 2019, 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 \$8,288 and \$3,884 for the three months ended December 31, 2020 and 2019, respectively and \$17,287 and \$17,433 for the years ended December 31, 2020 and 2019, respectively. Cash distributions of \$0 were received by the System from MFHF under terms of the Agreement during the three months ended December 31, 2020 and 2019 and \$3,978 and \$3,347 during years the ended December 31, 2020 and 2019, respectively. In addition, MFHF made \$537 and 333 in contributions to the System for program support during the years ended December 31, 2020 and 2019, respectively.

At December 31, 2020, the System had a 49.5% ownership interest in RML Health Providers, L.P. ("RML") that is accounted for on an equity basis. RML is an Illinois not-for-profit limited partnership that operates a 115-bed licensed long-term acute care hospital in Hinsdale, Illinois, and an 86-bed licensed long-term acute care hospital in Chicago, Illinois. The System's investment in RML was \$35,235 and \$33,462 at December 31, 2020 and 2019, respectively, and is presented within investments in unconsolidated entities in the accompanying condensed consolidated balance sheets.

RML leases the Chicago, Illinois, facility from the System. The lease has a fixed term through June 30, 2025. The System recorded rental income of \$302 and \$293 for the three months ended December 31, 2020 and 2019, respectively and \$1,192 and \$1,157 for the years ended December 31, 2020 and 2019, respectively.

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

	<u>RML</u>	<u>MFHF</u>
As of December 31, 2020		
Total assets	\$ 131,256	\$ 112,993
Total liabilities	58,482	3,661
Partners' equity/net assets	72,774	109,332
Three Months Ended December 31, 2020		
Total revenue	31,983	9,729
Revenue less than expenses	6,585	8,294
Three Months Ended December 31, 2019		
Total revenue	27,146	5,606
Revenue in excess of expenses	1,799	2,976
Year Ended December 31, 2020		
Total revenue	123,067	18,613
Revenue less than expenses	16,677	13,697
Year Ended December 31, 2019		
Total revenue	111,745	19,160
Revenue less than expenses	12,170	13,542
As of December 31, 2019		
Total assets	123,345	99,827
Total liabilities	55,118	4,192
Partners' equity/net assets	68,227	95,635

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 2018C-1 of \$50,000, 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 December 31, 2020, 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 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 December 31, 2020, there were no bank-purchased bonds outstanding. To the extent that the standby bond purchase agreement expiration date is within 12 months after December 31, 2020, 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 March 2019, the System issued commercial paper in the amount of \$50,000. The proceeds of the commercial paper were used to redeem the Series 2008C-2A bonds of \$49,230 plus accrued interest and certain costs related to the issuance of the commercial paper. The remaining proceeds were used for general corporate purposes. The standby bond purchase agreement related to the Series 2008C-2A bonds was canceled effective March 5, 2019.

In connection with the BAMC acquisition, the System assumed \$81,465 of outstanding tax-exempt bonds originally issued for the benefit of BAMC, which were redeemed in November 2019 with a portion of the proceeds of \$82,000 of the System's commercial paper. Also in connection with the BAMC acquisition, the System acquired an interest rate swap. As the debt related to the swap is no longer outstanding, it is being held as a swap portfolio. This swap is secured under the System Master Indenture.

In November 2019, the System issued its Series 2019 Taxable Bonds in the amount of \$357,970. The proceeds of the Series 2019 Taxable Bonds were used to refinance all or a portion of the Series 2011A-2, Series 2012, Series 2013A and Series 2014 Bonds and to pay certain financing costs. In connection with this issuance, the System recognized a loss on refinancing in the amount of \$21,103.

In May 2020, the System issued its Series 2020A Taxable Bonds in the aggregate principal amount of \$700,000. The proceeds of the Series 2020A Taxable Bonds were used for general corporate purposes, to refinance a portion of the Series 2011B, Series 2011C, Series 2011D, Series 2012, Series 2013A, Series 2015 and Series 2015B Bonds, to repay \$82,000 of commercial paper and to pay certain financing costs. In connection with this transaction, the System recognized a loss on refinancing in the amount of \$12,231.

As of December 31, 2020, the System authorized the issuance of up to \$1,000,000 in commercial paper aggregate principal outstanding. As of December 31, 2020, \$50,000 of commercial paper notes were outstanding, with maturities ranging from 119 to 122 days. As of December 31, 2019, \$132,000 of commercial paper was outstanding, with maturities ranging from 27 to 62 days.

At December 31, 2020, the System had lines of credit with banks aggregating to \$1,425,000 in available commitments. These lines of credit provide for various interest rates and payment terms and as of December 31, 2020 expire as follows: \$1,225,000 in April 2021, \$100,000 in August 2021 and \$100,000 in December 2022. 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 December 31, 2020, letters of credit totaling \$58,326 have been issued under one of these lines. At December 31, 2020, no amounts were outstanding on these lines or 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, financing arrangements and interest rate swaps. The System's interest paid, net of capitalized interest and capitalized interest are as follows:

	<u>Three Months Ended December 31, 2020</u>	<u>Three Months Ended December 31, 2019</u>	<u>Year Ended December 31, 2020</u>	<u>Year Ended December 31, 2019</u>
Interest paid, net of capitalized interest	\$ 36,822	\$ 22,007	\$ 116,953	\$ 119,870
Capitalized interest	6,851	1,532	8,198	4,087

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 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 December 31, 2020, 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. As the Series 2008C-2A bonds were redeemed on March 5, 2019, the portion of the swap related to these bonds is now held as a swap portfolio.

In connection with the BAMC acquisition, the System acquired an interest rate swap. As the debt related to the swap is no longer outstanding, it is being held as a swap portfolio.

The following is a summary of the outstanding positions under these interest rate swap agreements at December 31, 2020:

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	26,170	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 interest rate 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 \$118,620 and \$91,340 as of December 31, 2020 and 2019, respectively. No collateral was posted under these swap agreements as of December 31, 2020 and 2019.

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

	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Year Ended December 31, 2020	Year Ended December 31, 2019
Net cash payments on interest rate swap agreements (interest expense)	\$ 2,862	\$ 1,935	\$ 10,241	\$ 6,711
Change in fair value of interest rate swaps	\$ 5,768	\$ 13,219	\$ (27,280)	\$ (21,079)

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 Condell Health Network Retirement Plan ("Condell Plan") was frozen effective January 1, 2008, to new participants and participants ceased to accrue additional pension benefits. During the years ended December 31, 2020 and 2019, \$3,000 and no contributions were made to the Condell Plan.

The Aurora Health Care, Inc. Pension Plan ("Aurora Plan") was frozen on December 31, 2012. During the years ended December 31, 2020 and 2019, no contributions were made to the Aurora Plan.

In June 2019, the System approved a plan to freeze the Advocate Health Care Network Pension Plan ("Advocate Plan") that covered substantially all of Advocate's employees. Effective December 31, 2019, the Advocate Plan was closed to new participants and participants ceased accruing additional pension benefits. The Advocate Plan was remeasured as of June 30, 2019 and a curtailment gain of \$72 was recorded in nonoperating (loss) income, net in the accompanying condensed consolidated statements of operations and changes in net assets as of December 31, 2019. In addition, \$86,396 of previously unrecognized net actuarial loss was recognized in net assets without donor restrictions as a component of pension-related changes other than net periodic pension cost at December 31, 2019. The accompanying condensed consolidated balance sheets contain an other noncurrent liability related to the Advocate Plan totaling \$134,325 and \$173,939 at December 31, 2020 and 2019, respectively. During the three months ended and year ended December 31, 2020, \$0 and \$40,000, respectively, in cash contributions were made to the Advocate Plan.

In September 2020, the System transferred benefit obligations for certain participants of the Advocate Plan, Condell Plan and Aurora Plan through the purchase of annuity contracts. As a result of this transaction, all three Plans were remeasured as September 30, 2020 and a combined settlement loss of \$119,658 was recorded in the nonoperating income (loss) section in the accompanying condensed consolidated statements of operations and changes in net assets as of December 31, 2020.

On December 31, 2020, the Condell Plan liabilities and assets were merged into the Aurora Plan. There was an other noncurrent liability related to the Aurora Plan of \$66,494 and \$83,321 at December 31, 2020 and 2019, respectively. There was an other noncurrent liability related to the Condell Plan of \$1,824 at December 31, 2019.

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

Three Months Ended December 31, 2020

	<u>Advocate</u>	<u>Condell</u>	<u>Aurora</u>	<u>Total</u>
Interest cost	\$ 6,976	\$ 387	\$ 10,391	\$ 17,754
Expected return on plan assets	(10,460)	(378)	(11,422)	(22,260)
Amortization of:				
Actuarial loss	1,035	57	2,483	3,575
Prior service cost	—	—	1	1
Settlement	5,455	104	451	6,010
Net pension expense	<u>\$ 3,006</u>	<u>\$ 170</u>	<u>\$ 1,904</u>	<u>\$ 5,080</u>

Three Months Ended December 31, 2019

	<u>Advocate</u>	<u>Condell</u>	<u>Aurora</u>	<u>Total</u>
Service cost	\$ 14,519	\$ —	\$ —	\$ 14,519
Interest cost	8,500	581	15,663	24,744
Expected return on plan assets	(11,596)	(601)	(19,046)	(31,243)
Amortization of:				
Actuarial loss	—	27	1,908	1,935
Prior service cost	—	—	1	1
Net pension expense (income)	<u>\$ 11,423</u>	<u>\$ 7</u>	<u>\$ (1,474)</u>	<u>\$ 9,956</u>

Year Ended December 31, 2020

	<u>Advocate</u>	<u>Condell</u>	<u>Aurora</u>	<u>Total</u>
Interest cost	\$ 34,835	\$ 1,995	\$ 51,860	\$ 88,690
Expected return on plan assets	(43,456)	(1,473)	(61,085)	(106,014)
Amortization of:				
Actuarial loss	4,897	323	11,475	16,695
Prior service cost	—	—	3	3
Settlement	33,561	1,932	90,175	125,668
Net pension expense	<u>\$ 29,837</u>	<u>\$ 2,777</u>	<u>\$ 92,428</u>	<u>\$ 125,042</u>

Year Ended December 31, 2019

	<u>Advocate</u>	<u>Condell</u>	<u>Aurora</u>	<u>Total</u>
Service cost	\$ 57,645	\$ —	\$ —	\$ 57,645
Interest cost	38,384	2,327	62,649	103,360
Expected return on plan assets	(55,543)	(2,413)	(76,183)	(134,139)
Amortization of:				
Actuarial loss	3,634	108	7,631	11,373
Prior service cost	(72)	—	3	(69)
Settlement/curtailment	(72)	642	—	570
Net pension expense (income)	<u>\$ 43,976</u>	<u>\$ 664</u>	<u>\$ (5,900)</u>	<u>\$ 38,740</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:

	<u>Advocate</u>	<u>Aurora</u>	<u>Total</u>
2021	\$ 60,586	\$ 46,832	\$ 107,418
2022	61,578	52,219	113,797
2023	62,241	55,154	117,395
2024	61,506	58,191	119,697
2025	61,336	61,722	123,058
2026-2030	294,108	345,472	639,580
Total	<u>\$ 601,355</u>	<u>\$ 619,590</u>	<u>\$ 1,220,945</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:

Asset Category - Advocate Plan	<u>December 31, 2020</u>		<u>December 31, 2019</u>	
	<u>Target</u>	<u>Actual</u>	<u>Target</u>	<u>Actual</u>
De-risking portfolio	75 %	67 %	75 %	58 %
Domestic and international equity securities	21	22	21	20
Alternative investments	2	7	2	13
Cash and fixed-income securities	2	4	2	9
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

Asset Category - Condell Plan	<u>December 31, 2020</u>		<u>December 31, 2019</u>	
	<u>Target</u>	<u>Actual</u>	<u>Target</u>	<u>Actual</u>
De-risking portfolio	90 %	90 %	75 %	85 %
Domestic and international equity securities	4	4	11	6
Cash and fixed-income securities	6	6	14	9
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

Asset Category - Aurora Plan	<u>December 31, 2020</u>		<u>December 31, 2019</u>	
	<u>Target</u>	<u>Actual</u>	<u>Target</u>	<u>Actual</u>
De-risking portfolio	85 %	82 %	75 %	73 %
Domestic and international equity securities	12	15	21	22
Alternative investments	1	1	2	2
Cash and fixed-income securities	2	2	2	3
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

Assumptions used to determine benefit obligations are as follows:

	<u>December 31, 2020</u>
Discount rate - Advocate Plan	2.49 %
Discount rate - Aurora Plan	2.79 %
Assumed rate of return on assets - Advocate Plan	4.40 %
Assumed rate of return on assets - Aurora Plan	3.40 %

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. As the Advocate Plan was frozen on

December 31, 2019, the assumed rate of return and the target asset allocations were adjusted and actual allocations are being adjusted to more closely align with the new target allocations.

In addition to these plans, the System sponsors defined contribution plans for its employees. As of January 1, 2020, three plans were merged into one existing plan, the Advocate Health Care Network 401(k) plan. At this time the Advocate Health Care Network 401(k) plan was restated and became known as the Advocate Aurora Health 401(k) plan ("AAH 401(k)"). Effective January 1, 2020, the AAH 401(k) contribution plan was enhanced to add an annual contribution component to the employer match. Expense related to these plans, which are included in salaries, wages and benefits expense in the condensed consolidated statements of operations and changes in net assets are as follows:

	<u>Three Months Ended December 31, 2020</u>	<u>Three Months Ended December 31, 2019</u>	<u>Year Ended December 31, 2020</u>	<u>Year Ended December 31, 2019</u>
Defined contribution plan expense	\$ 71,035	\$ 45,141	\$ 300,971	\$ 207,194

13. FUNCTIONAL EXPENSES

For the three months and years ended December 31, 2020 and 2019, 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 consolidated balance sheets date for general expenditures are as follows:

	<u>December 31, 2020</u>	<u>December 31, 2019</u>
Current assets		
Cash and cash equivalents	\$ 959,878	\$ 449,712
Assets limited as to use	125,053	106,529
Patient accounts receivable	1,570,738	1,605,607
Third-party payors receivables	16,933	15,331
Collateral proceeds under securities lending program	19,789	18,284
Total current assets	<u>2,692,391</u>	<u>2,195,463</u>
Assets limited as to use		
Internally designated for capital and other	10,291,819	8,345,172
Held for self-insurance	658,466	645,697
Donor restricted	137,980	132,024
Investments under securities lending program	18,945	17,672
Total assets limited as to use	<u>11,107,210</u>	<u>9,140,565</u>
Total financial assets	13,799,601	11,336,028
Less		
Amounts unavailable for general expenditures		
Alternative investments	(2,110,330)	(1,791,717)
Total amounts unavailable for general expenditure	<u>(2,110,330)</u>	<u>(1,791,717)</u>
Amounts unavailable to management without approval		
Held for self-insurance	(783,519)	(752,226)
Donor restricted	(137,980)	(132,024)
Investments under securities lending program	(18,945)	(17,672)
Total amounts unavailable to management without approval	<u>(940,444)</u>	<u>(901,922)</u>
Total financial assets available to management for general expenditure within one year	<u>\$ 10,748,827</u>	<u>\$ 8,642,389</u>

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 December 31, 2020 and 2019.

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. ACQUISITION OF BAY AREA MEDICAL CENTER

The System had a 49% interest in BAMC that was accounted for under the equity method of accounting until the remaining equity interest was purchased on April 1, 2019. BAMC is a 99-bed general acute care hospital located in Marinette, Wisconsin.

At the time of the acquisition, BAMC and the System owned a 73% and 27% interest, respectively, in AABAMG. ABAMG provides inpatient, outpatient and other professional medical services in Marinette, Wisconsin and its surrounding communities. As part of the acquisition of BAMC, the System now owns 100% of ABAMG and its financial results are included in the consolidated financial statements of the System.

The acquisition will improve the availability, scope and access to health care in the communities served by BAMC. As of April 1, 2019, BAMC and ABAMG are fully consolidated within the accompanying condensed consolidated financial statements of the System.

In conjunction with the BAMC transaction, the System contributed \$25,000 to a newly formed independent foundation. This interest in that foundation is reflected in investments in unconsolidated entities in the accompanying condensed consolidated balance sheets. Under the terms of the definitive agreement between the System and BAMC, the use of the \$25,000 contribution is designated to support the operations and capital needs of BAMC and/or ABAMG.

As the System previously had an interest in BAMC, this transaction was accounted for as an acquisition achieved in stages. The System remeasured its previously held equity interest in BAMC to fair market value resulting in a gain of \$44,000, which was recorded within other nonoperating (loss) income, net in the condensed consolidated statements of operations and changes in net assets as of December 31, 2019. The System then recorded its 100% interest in BAMC at fair market value, resulting in an

inherent contribution of \$37,736, which was recorded within other nonoperating (loss) income, net in the condensed consolidated statements of operations and changes in net assets as of December 31, 2019.

The fair value of assets and liabilities of BAMC acquisition at April 1, 2019 consisted of the following:

Current assets	\$	37,239
Assets limited as to use		18,795
Property and equipment		157,206
Other noncurrent assets		7,879
Other intangible assets		460
Total assets	<u>\$</u>	<u>221,579</u>
Current liabilities		19,812
Long-term debt, less current portion		78,959
Other noncurrent liabilities		12,080
Total liabilities		<u>110,851</u>
Net assets with donor restrictions		792
Net assets without donor restrictions		109,936
Total liabilities and net assets	<u>\$</u>	<u>221,579</u>

Total 2019 revenue and operating loss from the date of acquisition for BAMC of \$109,309 and \$(9,599), respectively were included in the condensed consolidated statements of operations and changes in net assets. The 2019 BAMC related changes in net assets without donor restrictions of \$(13,074) from the date of acquisition is included in the condensed consolidated balance sheets.

The proforma financial information presented below were prepared on a consolidated basis utilizing the accounting records of the System and BAMC as if the acquisition had occurred for the entirety of the period presented. The proforma information presented have been adjusted to eliminate activity between the System and BAMC. Management believes the assumptions underlying the proforma financial information presented, including the assumptions regarding the elimination of intercompany activity are reasonable. Nevertheless, the proforma information may not reflect the results of operations had BAMC been a combined company during the periods presented and is not intended to project the System's results of operations for any future periods.

	<u>Year Ended</u> <u>December 31, 2019</u>
Total revenue	\$ 12,833,303
Operating income	480,701
Revenues in excess of expenses	1,546,032

18. SUBSEQUENT EVENTS

The System evaluated events and transactions subsequent to December 31, 2020 through March 22, 2021, the date of consolidated financial statement issuance.

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, 2020, 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 years ended December 31, 2020 and 2019, and such information should not be relied upon as indicative of future financial performance. The COVID-19 pandemic described herein may adversely affect the System's future financial performance to an extent that could be material.

ADVOCATE AURORA HEALTH, INC.
KEY FINANCIAL RATIOS

	Three Months Ended,	
	December 31, 2020	December 31, 2019
Profitability		
Operating margin ⁽¹⁾	7.6%	5.3%
Operating cash flow margin ⁽²⁾	12.2%	10.6%
Excess margin ⁽³⁾	22.8%	12.4%
EBIDA margin ⁽⁴⁾	32.3%	18.8%
	Year Ended,	
	December 31, 2020	December 31, 2019
Profitability		
Operating margin ⁽¹⁾	2.5%	4.7%
Operating cash flow margin ⁽²⁾	7.6%	10.0%
Excess margin ⁽³⁾	4.5%	11.2%
EBIDA margin ⁽⁴⁾	9.8%	17.4%
	As of December 31, 2020	As of December 31, 2019
Leverage and Liquidity		
Debt to capitalization ⁽⁵⁾	22.5%	21.1%
Cash to debt ⁽⁶⁾	319%	288%
Days cash on hand ⁽⁷⁾	334	274
Historical debt service coverage ratio	5.6x	8.4x

Profitability

⁽¹⁾ Operating income before nonrecurring expenses/Total revenue

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

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

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

Liquidity

⁽⁵⁾ (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)

⁽⁶⁾ 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)

⁽⁷⁾ 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 years ended December 31, 2020 and 2019.

ADVOCATE AURORA HEALTH, INC.
KEY FINANCIAL RATIOS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2020
(in thousands)

	Year Ended December 31, 2020
Debt Service Coverage	
Revenue in excess of expenses- attributable to controlling interest	\$ 558,032
Adjustments:	
Depreciation and amortization expense	560,215
Interest expense	112,126
Unrealized gain on investments	(524,365)
Unrealized loss on interest rate swap obligation	27,280
Pension settlement loss	119,658
Loss on early extinguishment of debt	12,244
Asset impairment charges	4,006
Nonrecurring expenses	116,355
Total income available for debt service	985,551
Debt service requirement	174,574
Historical debt service coverage ratio	5.6

	Year Ended December 31, 2020
Days Cash on Hand	
Cash and cash equivalents	\$ 959,878
Assets limited as to use, current	125,053
Assets limited as to use, noncurrent	11,107,210
Less: restricted funds	921,499
Unrestricted cash and investments	11,270,642
Operating expenses	12,802,867
Plus: nonrecurring expenses	116,355
Less: depreciation and amortization	560,215
Adjusted operating expenses	12,359,007
Number of days in period	366
Operating expense per day	33,768
Days cash on hand	334

(Continued)

ADVOCATE AURORA HEALTH, INC.
KEY FINANCIAL RATIOS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2020
(in thousands)

	<u>Year Ended December 31, 2020</u>
Debt to Capitalization	
Debt	
Long-term debt and commercial paper, current portion	\$ 101,996
Long-term debt subject to short-term financing arrangements	119,660
Long-term debt, less current portion	<u>3,310,401</u>
Total debt	3,532,057
Capitalization	
Total debt	3,532,057
Total net assets without donor restrictions	<u>12,167,364</u>
Total capitalization	15,699,421
Debt to capitalization	22.5 %

(Concluded)

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

	Three Months Ended December 31, 2020	Three Months Ended December 31, 2019	Change	% Change	Modified Change⁽²⁾	Modified % Change⁽²⁾
Discharges	63,865	68,680	(4,815)	(7.0)%	(2,548)	(3.8)%
Observation Cases	20,943	27,270	(6,327)	(23.2)%	(5,581)	(21.0)%
Hospital Outpatient Visits	942,595	1,170,543	(227,948)	(19.5)%	(184,050)	(16.3)%
Physician Visits	2,395,324	2,627,783	(232,459)	(8.8)%	(170,465)	(6.6)%
Home Care Visits	200,367	192,198	8,169	4.3 %		
Capitated Member Lives ⁽¹⁾	248,691	283,299	(34,608)	(12.2)%		

	Year Ended December 31, 2020	Year Ended December 31, 2019	Change	% Change	Modified Change⁽³⁾	Modified % Change⁽³⁾
Discharges	247,888	271,135	(23,247)	(8.6)%	(14,700)	(7.4)%
Observation Cases	84,646	106,684	(22,038)	(20.7)%	(14,590)	(18.7)%
Outpatient Visits	3,557,189	4,455,746	(898,557)	(20.2)%	(623,220)	(19.5)%
Physician Visits	8,761,821	9,853,681	(1,091,860)	(11.1)%	(999,082)	(10.4)%
Home Care Visits	745,968	778,908	(32,940)	(4.2)%		

⁽¹⁾ As of the date set forth in the column header

⁽²⁾ For comparison purposes the impact of Central Illinois for the three month period October through December 2019 is excluded as Central Illinois was disposed of in 2020 and therefore there are no comparable amounts for the three months ended December 31, 2020. See discussion of this transaction within Note 2. SIGNIFICANT EVENTS of the Condensed Consolidated Financial Statements.

⁽³⁾ For comparison purposes the impact of Central Illinois for the period of July through December 2019 is excluded as Central Illinois was disposed of July 1, 2020 and therefore there are no comparable amounts in the December 31, 2020 year to date results and the impact of the three month period ended March 31, 2020 for Bay Area Medical Center are excluded as Bay Area was acquired on April 1, 2019 and therefore there are no comparable amounts in 2019. See discussion of this transaction within NOTE 17. ACQUISITION OF BAY AREA MEDICAL CENTER of the Condensed Consolidated Financial Statements.

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

The management discussion and analysis section refers to the condensed consolidated statements of operations.

Results of Operations – Year Ended December 31, 2020 Compared to Year Ended December 31, 2019

Operating income before nonrecurring expenses was \$329,322 for the year ended December 31, 2020, resulting in an operating margin of 2.5%, compared to operating income before nonrecurring expenses of \$597,870 for the year ended December 31, 2019, for an operating margin of 4.7%. This represented a period-over-period decrease of \$268,548. If the impact of both the Central Illinois disposal and BAMC acquisition were excluded, the period-over-period decrease would increase by \$17,465 to \$286,013.

In response to the COVID-19 pandemic, at various times, the System postponed or canceled elective procedures to comply with public health protocols and open surge capacity. The public also curtailed visits to physicians, clinics and emergency rooms for fear of contracting COVID-19. These actions served to decrease revenues from non-COVID-19 patients while driving up costs to prepare for and care for COVID-19 patients. While operating results improved when the System restarted elective procedures and clinic visits, the System continues to be impacted by COVID-19. In 2020, the System received and recognized as other operating revenue in the condensed consolidated financial statements \$786,655 of grant funding from the U.S. Department of Health and Human Services (“HHS”). These grant funds were distributed from the Provider Relief Fund established under the Coronavirus Aid, Relief and Economic Security Act (Phase 3). These grant funds were provided as partial coverage for lost revenues and expenses incurred by the System attributed to COVID-19.

Total revenue for the year ended December 31, 2020 was \$13,132,189, which was \$326,766 (2.6%) higher than the comparative period of 2019. If the impact of the Central Illinois disposal and the BAMC acquisition were excluded, the increase in total revenue would be \$433,963 (3.4%).

Patient service revenue decreased \$444,583 (4.2%), in the year ended December 31, 2020 compared to the same period in the prior year. If the impact of Central Illinois disposal and the BAMC acquisition were excluded, the decrease in patient service revenue would be reduced by \$91,536 to \$353,047 (3.3%). The decrease was primarily due to a decrease in total patient volumes over the comparative period and an increase in bad debt as a result of the COVID-19 pandemic.

Capitation revenue decreased \$142,734 (11.3%) in the year ended December 31, 2020, compared to the same period in the prior year due to a decrease in capitated lives of 12.2%. The decrease in membership was driven by less demand for exchange plan products as a result of higher employment rates prior to the COVID-19 pandemic and the lack of the federal mandate requiring insurance coverage.

Other operating revenue of \$1,794,375 increased \$914,083 (103.8%). Included in this amount were amounts provided under the CARES act including \$786,655 related to the HHS Provider Relief grants and \$37,000 related to the employee retention tax credit. The remaining increase of \$90,428 was driven by increased pharmacy and shared savings revenue.

Total expenses (excluding nonrecurring expenses) for the year ended December 31, 2020 was \$12,802,867, which was \$595,314 (4.9%) higher than the comparative period of 2019. If the impact of the Central Illinois disposal and the BAMC acquisition were excluded, the increase in total expenses would be \$715,181 (5.9%).

Salaries, wages and benefits expenses increased \$439,341 (6.3%). If the impact of the Central Illinois disposal and the BAMC acquisition were excluded, the increase in salaries and wages would be \$501,678 (7.3%) due to an increase in full-time equivalent employees ("FTE's") of 1.5% and the significant increases in employee compensation to respond to the COVID-19 pandemic and pay and benefit continuation programs for furloughed employees.

Supplies, purchased services and other expenses increased \$201,198 (5.0%). If the impact of the Central Illinois disposal and the BAMC acquisition were excluded, the increase would be \$241,622 (6.1%). The increase is primarily due to the higher acuity of COVID-19 patients, costs of personal protective equipment and increased drug costs, including specialty drugs and medical and patient supply costs.

Nonrecurring expenses were \$116,355 and \$116,800 for the years ended December 31, 2020 and 2019, respectively. Included in the year ended December 31, 2020 is the \$21,346 loss on the divestiture of operations in Central Illinois as described in NOTE 2. SIGNIFICANT EVENTS of the condensed consolidated financial statements. Nonrecurring expenses, in addition to the loss on divestiture, consist of costs incurred in connection with the implementation of an electronic medical records and billing system, the implementation of an enterprise resource planning system and, as part of the initiative to reduce operating expenses, an early retirement incentive program and position restructuring.

The nonoperating income of \$395,158 for the year ended December 31, 2020 compares unfavorably to the nonoperating income of \$1,065,627 for the year ended December 31, 2019 primarily due to investment income, net which decreased \$460,615 over the comparative period. See disclosure of the composition of investment income, net within Note 5. INVESTMENTS of the condensed consolidated financial statements. The decrease is due to a deterioration in the financial markets over the comparative period resulting from the COVID-19 pandemic. The change in fair value of interest rate swaps is attributable to the change (a decline) in interest rates. The pension settlement loss of \$119,658 is related to the transfer of pension benefit obligations in September 2020, see disclosure within Note 12. RETIREMENT PLANS of the condensed consolidated financial statements. Other nonoperating (loss) income, of \$(38,943) compared unfavorably to the other nonoperating income (loss) of \$54,473 primarily due to the BAMC gain of \$81,736 recorded during the year ended December 31, 2019.

Overall, the System reported revenue in excess of expenses - attributable to controlling interest of \$558,032 for the year ended December 31, 2020 compared to \$1,485,948 for the year ended December 31, 2019 due primarily to decreased investment yields and additional operating expenses resulting from the COVID-19 pandemic.

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.

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 334 as of December 31, 2020 compared to 274 as of December 31, 2019. The increase in days cash on hand is primarily due to the Series 2020A issuance, receipt of Medicare accelerated and advance payments and deferred remittance of employer portion of the Social Security tax portion of FICA taxes. 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 305.

Indebtedness

Master Indenture Obligations: Substantially all of the System's outstanding 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").

In connection with the BAMC acquisition, the System assumed \$81,465 of tax-exempt bonds, which were redeemed with the proceeds from the issuance of commercial paper in the amount of \$82,000.

On November 14, 2019, the System issued \$357,970 of 30-year Taxable Bonds to refinance certain tax-exempt bonds in the aggregate principal amount of \$323,325 and to pay certain expenses incurred in connection with their issuance.

On May 5, 2020, the System issued \$700,000 of Taxable Bonds for general corporate purposes, to refinance certain tax-exempt bonds in the aggregate principal amount of \$78,750, to refinance commercial paper in the amount of \$82,000 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 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:

	<u>December 31, 2020</u>	<u>December 31, 2019</u>
Tax-exempt bonds	\$ 1,409,326	\$ 1,514,551
Taxable bonds	1,760,500	1,064,331
Financing arrangements	214,360	235,249
Taxable term loan	97,871	114,868
Commercial paper	50,000	132,000
Total long-term debt	<u>\$ 3,532,057</u>	<u>\$ 3,060,999</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:

<u>Subseries</u>	<u>Par</u>	<u>Expiration</u>
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 December 31, 2020, 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 December 31, 2020 and 2019 in the 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 and Series 2018B-4 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 December 31, 2020. 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.

Subseries	Par	Expiration
Series 2018B-1	46,690	1/26/2022
Series 2018B-2	46,310	1/25/2023
Series 2018B-3	48,560	1/31/2024
Series 2018B-4	49,420	1/29/2025
Total	<u>\$ 190,980</u>	

The Series 2008A-1 Bonds were subject to mandatory tender on January 15, 2020 (the "Jan 2020 Mandatory Tender Date"). The Series 2008A-1 Bonds were classified as current liabilities as of December 31, 2019 in the condensed consolidated balance sheets as these bonds were subject to mandatory tender on a date that was within one year of the balance sheet date. While \$42,045 of the Series 2008A-1 Bonds were outstanding on the Jan 2020 Mandatory Tender Date, only \$36,455 of the Series 2008A-1 Bonds were remarketed. The reduction in the principal amount reflects the application of the premium paid on the Series 2008A-1 Bonds upon their remarketing, together with other funds, to the retirement of \$5,590 of the Series 2008A-1 Bonds on the Jan 2020 Mandatory Tender Date. The Series 2008A-1 Bonds will next be subject to mandatory tender on November 1, 2030, which is also the maturity date for the Series 2008A-1 Bonds.

The Series 2008A-2 Bonds were subject to mandatory tender on February 12, 2020 (the "Feb 2020 Mandatory Tender Date"). The Series 2008A-2 Bonds were classified as current liabilities as of December 31, 2019 in the condensed consolidated balance sheets as these bonds were subject to mandatory tender on a date that was within one year of the balance sheet date. While \$35,490 of the Series 2008A-2 Bonds were outstanding on the Feb 2020 Mandatory Tender Date, only \$30,820 of the Series 2008A-2 Bonds were remarketed. The reduction in the principal amount reflects the application of the premium paid on the Series 2008A-2 Bonds upon their remarketing, together with other funds, to the retirement of \$4,670 of the Series 2008A-2 Bonds on the Feb 2020 Mandatory Tender Date. The Series 2008A-2 Bonds will next be subject to mandatory tender on November 1, 2030, which is also the maturity date for the Series 2008A-2 Bonds.

The Series 2008A-3 Bonds were subject to mandatory tender on May 1, 2019 (the "2019 Mandatory Tender Date"). While \$42,795 of the Series 2008A-3 Bonds were outstanding on the 2019 Mandatory Tender Date, only \$36,535 of the Series 2008A-3 Bonds were remarketed. The reduction in the principal amount reflects the application of the premium paid on the Series 2008A-3 Bonds upon their remarketing, together with other funds, to the retirement of \$6,260 of the Series 2008A-3 Bonds on the 2019 Mandatory Tender Date.

The Series 2008A-3 Bonds will next be subject to mandatory tender on November 1, 2030, which is also the maturity date for the Series 2008A-3 Bonds.

Indexed Floating Rate Bonds: The Series 2018C-1 Bonds, Series 2018C-2 Bonds, Series 2018C-3 Bonds and Series 2018C-4 Bonds (collectively the "2018C Bonds") bear interest at an indexed rate. At the end of their respective initial index rate periods, the Series 2018C Bonds will be subject to mandatory tender. The Series 2018C-1 Bonds were classified as current liabilities as of December 31, 2020 in the condensed consolidated balance sheets as these bonds were subject to mandatory tender on a date that was within one year of the balance sheet date. The System presently anticipates that the Series 2018C Bonds will be remarketed to new holders in one of the interest rate modes available under the related bond indentures. The following table summarizes the next scheduled mandatory tender dates for these bonds.

Subseries	Principal Amount	Next Mandatory Tender date
Series 2018C-1	\$ 50,000	7/28/2021
Series 2018C-2	50,000	7/27/2022
Series 2018C-3	49,065	7/26/2023
Series 2018C-4	50,350	7/31/2024
Total	\$ 199,415	

Taxable Term Note: The System is party to a taxable term loan agreement with a bank, relating to a \$97,871 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. On March 5, 2019, the System issued commercial paper in the amount of \$50,000. The proceeds of the commercial paper were used to redeem the Series 2008C-2A bonds of \$49,230 plus accrued interest and certain costs related to the issuance of the commercial paper. The remaining proceeds were used for general corporate purposes.

On November 19, 2019, the System issued commercial paper in the amount of \$82,000. The proceeds of the commercial paper were used to redeem certain bonds previously issued for BAMC in the aggregate principal amount of \$81,465 plus accrued interest. The remaining proceeds were used for general corporate purposes. In May 2020, a portion of the proceeds of the Series 2020A Bonds were used by the System to retire \$82,000 of commercial paper.

As of the date of this report, the System has the authority to issue \$950,000 of additional commercial paper.

Lines of Credit: At December 31, 2020, the System had lines of credit agreements with banks totaling \$1,425,000. These agreements expire as follows: \$1,225,000 in April 2021, \$100,000 in August 2021 and \$100,000 in December 2022. At December 31, 2020, the System had a \$100,000 line of credit, under which letters of credit can also be issued. At December 31, 2020, letters issued under the line of credit totaling \$58,365 were outstanding. At December 31, 2020, 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 \$16,425. No amounts were drawn on this surety bond at December 31, 2020.

Other Indebtedness: At December 31, 2020, the System had various finance lease arrangements totaling \$214,360 classified as long-term debt. These arrangements, which relate to various administrative and medical support buildings, had initial lease terms of 15 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, Well 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 the BAMC acquisition, the System acquired an interest rate swap. BAMC had entered into a floating-to-fixed interest rate swap agreement ("Bay Area Swap") pursuant to an ISDA Master Agreement. Piper Jaffray Financial Products Inc. ("Piper Jaffray") pays BAMC a percentage of the one-month LIBOR and BAMC pays Piper Jaffray amounts based on a fixed rate (approximately 3.314%) based on the notional amount which declines over the term of the Bay Area Swap. Unless terminated earlier in accordance with their terms, the Bay Area Swap's scheduled termination date is February 1, 2038. Under certain circumstances, the Bay Area 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.

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 December 31, 2020 and 2019, the System loaned approximately \$18,945 and \$17,672, respectively in securities and accepted collateral for these loans in the amount of \$19,789 and \$18,284, 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 condensed consolidated balance sheets presented. The balance of securities on loan and accepted collateral fluctuates daily.

Capital Expenditures

For the year ended December 31, 2020, capital expenditures of the System were \$703,611; at December 31, 2020 the System had \$478,335 of construction-in-progress. The amounts of construction-in-progress at December 31, 2020 relate to various projects to improve existing facilities and expand access to health care in the markets served.

The System had four significant capital projects that were either ongoing or completed in 2020. The System is currently expanding the Center for Advanced Care (ambulatory base) 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 June 2024. The System is also building a hospital and medical office building on a site along the I-94 corridor in Mount Pleasant, Wisconsin. Management expects that the hospital, medical office building and ancillary buildings will cost approximately \$230,000, with construction estimated to be

completed in 2021 and opened for patients in February 2022. 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 June 2022. Additionally, in October 2018, the System broke ground on an ambulatory surgery center and medical office building project in the Kenosha/Pleasant Prairie, Wisconsin area. The medical building was completed and opened for patients in June 2020 with the ambulatory surgery center opened for patients in November 2020. 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, but could elect to fund portions with the proceeds of additional indebtedness in light of the COVID-19 pandemic.

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.

Employees

As of December 31, 2020, the System employed approximately 74,800 individuals (approximately 64,100 FTE's). Approximately 0.7% of System employees are represented by collective bargaining groups.

As of December 31, 2020, the System employed approximately 3,600 physicians (3,300 FTE's) and approximately 1,600 FTE advanced practice clinicians. As of December 31, 2020, there were approximately 9,500 individuals on the active medical staffs of the System hospitals. Approximately 88% of the members of the active medical staff are board certified specialists.

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 CEO, 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 April 2020 in connection with the issuance of the Series 2020A Bonds, ratings were obtained for all of the System's debt. Fitch assigned a rating of AA (stable outlook), S&P assigned a rating of AA (stable outlook) and Moody's assigned a rating of Aa3 (positive 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 2020, Mike Lappin, the System's Chief Integration Officer, left the System. There are currently no plans to fill this position.

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 current Chief Strategy Officer, will transition to focus exclusively on the Whole Person Health portion of the System's strategic plan.

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

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 achieve breakthrough performance in safety, health outcomes, growth and affordability. Consumer-First includes strategies to provide a seamless and connected consumer experience. Whole Person Health includes strategies to develop new care models and new consumer-facing businesses targeted to individualized health and wellness needs.

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

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 for such information. 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 the "BONDHOLDERS' RISKS" section in the Offering Memorandum dated April 28, 2020, relating to the Series 2020A Bonds. The Offering Memorandum can be accessed at <http://munios.com>.

As described in the BONDHOLDERS' RISKS section in the Offering Memorandum, 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 spread of COVID-19 has altered the behavior of businesses and people in a manner that is having negative effects, including significant growth in unemployment and underemployment related to business curtailment and closures, on global and local economies. In response to COVID-19 concerns, which resulted in the deferral or cancellation of most elective procedures occurring within the System's facilities from mid-March to mid-May when reactivation began, the System's patient service revenue from March to December was approximately \$600,000 or 10% lower than the comparable period of 2019. The System has also incurred cost of approximately \$384,000 through December 31, 2020 associated with the COVID-19 pandemic primarily in the form of increased salaries and wages related to pay programs implemented to compensate team members assigned to COVID-19 hotspots and other continuity related pay and other preparation related costs. The System continues to evaluate its pay programs and other costs and will adjust as the System's needs continue to evolve. It is not possible to predict the costs associated with the potential treatment of an infectious disease outbreak by the System's health care operations or preparation for such treatment.

In addition to the direct impact to the health care industry, investment markets in the United States and globally saw a significant decline in value in March attributed to COVID-19 concerns. The investment markets started to recover in April, but continued spread of COVID-19 or any other similar outbreaks could result in another significant decline in value.

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.

In response to this crisis, the Coronavirus Aid, Relief and Economic Security Act ("CARES Act") stimulus package was passed by Congress and signed into law by President Trump. The CARES Act is designed to provide \$2,200,000 in emergency assistance to individuals, and various businesses, including hospitals and other health care providers. In April 2020, the Department of Health and Human Services ("HHS") began distributing the first grants to providers from a Provider Relief Fund ("PRF") established under the CARES Act. Through December 31, 2020, the System has received and recognized \$786,655 in grants distributed in various general or targeted tranches from the PRF. (See Management Discussion and Analysis of Results of Operations above and NOTE 2. SIGNIFICANT EVENTS of the condensed consolidated financial statements.) Payments from the PRF are intended to cover healthcare related expenses attributable to coronavirus that another source has not reimbursed and is not obligated to reimburse. PRF payment amounts not fully expended on healthcare related expenses attributable to coronavirus are then applied to patient care lost revenues. These payments are not required to be repaid, provided the recipient attests to and complies with the terms and conditions of the PRF grant funds. 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 50% of up to \$10 in qualified wages paid to each employee by an eligible employer whose business has been financially impacted by COVID-19. The System recognized approximately \$37,000 of revenue for the employee retention tax credit that is included in other operating revenue within the condensed consolidated statement of operations and changes in net assets and a corresponding receivable that is included in other current assets in the condensed consolidated balance sheets. Management 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.

The CARES Act also permits employers to defer the employer portion of Social Security taxes of the FICA payroll tax. Employers are required to remit one-half of the amount deferred by December 31, 2021 and the remaining half by December 31, 2022. Through December 31, 2020 the System deferred \$215,000, half of

this liability is included in accrued salaries and employee benefits and the other half is included in other noncurrent liabilities the condensed consolidated balance sheets.

In addition to the CARES Act grants, the System received approximately \$773,000 from the Centers for Medicare and Medicaid ("CMS") as an advance payment for Medicare services. The funds were provided through the expansion of the Accelerated and Advance Payment Program to ensure providers and suppliers have the resources needed to combat the COVID-19 pandemic. The advances will be recouped by withholding future Medicare fee-for-service payments for claims until such time as the full accelerated payment has been recouped. Recoupments are scheduled to begin in April 2021. Subsequent to twenty-nine month recoupment period any unpaid remaining balance is subject to an interest charge of 4 percent per annum.

The System has benefited through December 31, 2020 by \$56,500 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. Further, the System received through December 31, 2020 approximately \$9,000 in additional Illinois Medicaid Hospital Assessment Program and Wisconsin disproportionate share hospital payments.

The System does anticipate as a result of the significant increase in unemployment and underemployment caused by business curtailment and closures, collectability on the patient responsibility portions of its non-COVID-19 related accounts receivable will be negatively impacted. As a result, the System increased its estimate for uncollectible accounts by approximately \$40,000.

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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