

Children's Hospital and Health System, Inc., and Affiliates

Consolidated Financial Statements as of and for the
Years Ended December 31, 2018 and 2017,
Supplementary Consolidating Information as of
and for the Year Ended December 31, 2018, and
Independent Auditors' Reports

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Children's Hospital and Health System, Inc. and Affiliates:

We have audited the accompanying consolidated financial statements of Children's Hospital and Health System, Inc. and Affiliates (the "Organization"), which comprise the consolidated statements of financial position as of December 31, 2018 and 2017, and the related consolidated statements of operations and changes in net assets, and of cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Children's Hospital and Health System, Inc. and Affiliates as of December 31, 2018 and 2017, and the results of their operations and changes in net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2 to the consolidated financial statements, in 2018, Children's Hospital and Health Systems, Inc. adopted new accounting guidance related to the presentation of financial statements for not-for-profit entities. Our opinion is not modified with respect to this matter.

Deloitte & Touche LLP

April 24, 2019

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION AS OF DECEMBER 31, 2018 AND 2017 (Dollars in thousands)

	2018	2017
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 216,475	\$ 186,057
Patient accounts receivable	89,492	89,086
Other receivables	36,213	38,517
Inventory of supplies	10,599	10,312
Prepaid expenses	<u>18,258</u>	<u>12,582</u>
Total current assets	<u>371,037</u>	<u>336,554</u>
INVESTMENTS	<u>934,581</u>	<u>860,244</u>
ASSETS LIMITED AS TO USE:		
Limited under bond indentures for capital additions	93,085	100,042
Restricted by donors for specific purpose	53,638	57,039
Restricted by donors in perpetuity	<u>174,533</u>	<u>183,692</u>
Total assets limited as to use	<u>321,256</u>	<u>340,773</u>
PROPERTY AND EQUIPMENT—Net	<u>456,129</u>	<u>456,037</u>
OTHER ASSETS	<u>18,425</u>	<u>19,825</u>
TOTAL	<u>\$2,101,428</u>	<u>\$2,013,433</u>

(Continued)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION AS OF DECEMBER 31, 2018 AND 2017 (Dollars in thousands)

	2018	2017
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable	\$ 49,041	\$ 41,032
Accrued expenses:		
Salaries and benefits	50,857	43,643
Personal leave benefits	25,251	24,113
Interest	4,958	622
Estimated third-party payor settlements	1,145	1,534
Current installments of long-term debt	6,690	6,295
Claims payable and other current liabilities	<u>78,486</u>	<u>44,583</u>
Total current liabilities	216,428	161,822
OTHER LONG-TERM LIABILITIES	57,723	46,028
ACCRUED PENSION	37,287	33,414
LONG-TERM DEBT—Less current installments	<u>351,906</u>	<u>359,371</u>
Total liabilities	<u>663,344</u>	<u>600,635</u>
COMMITMENTS AND CONTINGENCIES (Note 9 and Note 14)		
NET ASSETS:		
Without donor restrictions	1,209,913	1,172,067
With donor restrictions:		
Restricted by purpose	53,638	57,039
Restricted in perpetuity	<u>174,533</u>	<u>183,692</u>
Total net assets	<u>228,171</u>	<u>240,731</u>
Total net assets	<u>1,438,084</u>	<u>1,412,798</u>
TOTAL	<u>\$ 2,101,428</u>	<u>\$ 2,013,433</u>

See notes to consolidated financial statements.

(Concluded)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

(Dollars in thousands)

	2018	2017
OPERATING REVENUE:		
Net patient service revenue	\$ 728,374	\$ 685,867
Premium revenue and other capitated arrangements	461,408	278,347
Other	<u>102,274</u>	<u>103,154</u>
Total operating revenue	<u>1,292,056</u>	<u>1,067,368</u>
OPERATING EXPENSES:		
Salaries	348,683	331,110
Employee benefits	99,160	86,995
Medical supplies	89,243	81,325
Non-medical supplies and other	31,793	27,941
Net medical claims expenses	335,916	214,467
Purchased services and professional fees	133,641	113,757
Operation and maintenance of facilities	39,433	37,332
Medical College of Wisconsin and resident fees	55,518	46,664
Provider tax	10,751	10,867
Depreciation	63,178	60,552
Interest	<u>12,807</u>	<u>13,374</u>
Total operating expenses	<u>1,220,123</u>	<u>1,024,384</u>
OPERATING INCOME	<u>71,933</u>	<u>42,984</u>
NONOPERATING INCOME (EXPENSES):		
Investment income	52,229	35,866
Change in net unrealized gains and losses on investments	(81,021)	54,827
Loss on early extinguishment of debt	-	(16,061)
Other	<u>(2,768)</u>	<u>319</u>
Net nonoperating (expenses) income	<u>(31,560)</u>	<u>74,951</u>
EXCESS OF REVENUE OVER EXPENSES	<u>\$ 40,373</u>	<u>\$ 117,935</u>

(Continued)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017 (Dollars in thousands)

	2018	2017
NET ASSETS WITHOUT DONOR RESTRICTIONS:		
Excess of revenue over expenses	\$ 40,373	\$ 117,935
Net assets released from restrictions—capital acquisitions	1,706	4,689
Pension-related changes other than net periodic pension cost	(4,233)	(217)
Assets restricted for donor match	<u>-</u>	<u>(5,000)</u>
Increase in net assets without donor restrictions	<u>37,846</u>	<u>117,407</u>
NET ASSETS WITH DONOR RESTRICTIONS:		
Contributions	14,851	22,613
Investment return	(8,723)	22,922
Net assets released from restrictions—capital acquisitions	(1,706)	(4,689)
Net assets released from restrictions—operations	(16,982)	(17,407)
Assets restricted for donor match	<u>-</u>	<u>5,000</u>
(Decrease) increase in net assets with donor restrictions	<u>(12,560)</u>	<u>28,439</u>
INCREASE IN NET ASSETS	25,286	145,846
NET ASSETS—Beginning of year	<u>1,412,798</u>	<u>1,266,952</u>
NET ASSETS—End of year	<u>\$1,438,084</u>	<u>\$1,412,798</u>

See notes to consolidated financial statements.

(Concluded)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017 (Dollars in thousands)

	2018	2017
OPERATING ACTIVITIES:		
Increase in net assets	\$ 25,286	\$ 145,846
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Restricted contributions and pledges for capital projects, investment income, and contributions restricted in perpetuity	(14,442)	(18,080)
Pension-related changes other than net periodic pension cost	4,233	217
Change in net unrealized gains and losses on investments	101,396	(70,513)
Realized gain on sale of investments	(39,506)	(22,782)
Depreciation of property and equipment	63,178	60,552
Amortization and other	(95)	4,795
Changes in operating assets and liabilities:		
Patient accounts receivable	(406)	(9,608)
Other receivables	2,304	(13,600)
Inventory, prepaid and deferred expenses, and other assets	(4,836)	(7,194)
Accounts payable	6,304	4,317
Estimated third-party payor settlements	(389)	(1,102)
Other accrued expenses and liabilities	58,286	10,157
Accrued pension	(360)	(1,963)
Net cash provided by operating activities	<u>200,953</u>	<u>81,042</u>
INVESTING ACTIVITIES:		
Capital expenditures	(61,739)	(51,094)
Purchases of investments	(687,469)	(620,322)
Proceeds from sales of investments	<u>568,005</u>	<u>443,016</u>
Net cash used in investing activities	<u>(181,203)</u>	<u>(228,400)</u>
FINANCING ACTIVITIES:		
Proceeds from long-term borrowings	-	368,210
Payment of debt issuance costs	-	(2,580)
Payments on long-term borrowings	(6,295)	(256,012)
Proceeds from contributions for capital projects and endowments	<u>16,963</u>	<u>15,942</u>
Net cash provided by financing activities	<u>10,668</u>	<u>125,560</u>

(Continued)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017 (Dollars in thousands)

	2018	2017
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	\$ 30,418	\$ (21,798)
CASH AND CASH EQUIVALENTS:		
Beginning of year	<u>186,057</u>	<u>207,855</u>
End of year	<u>\$ 216,475</u>	<u>\$ 186,057</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION—Cash paid during the year for interest	<u>\$ 9,535</u>	<u>\$ 17,407</u>
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITY—Capital acquisitions funded through accounts payable	<u>\$ 4,037</u>	<u>\$ 2,332</u>
See notes to consolidated financial statements.		(Concluded)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017 (Dollars in thousands)

1. ORGANIZATION

Children's Hospital and Health System, Inc., and Affiliates (CHHS) is committed to ensuring a healthier future for children by providing an integrated health services network for infants, children, and adolescents, advocating on their behalf, and discovering new ways to keep kids healthy. CHHS' consolidated financial statements include the following:

Children's Hospital and Health System, Inc.—A not-for-profit organization that delivers outpatient health care services, administers a foster care medical home, and provides operational support services, research, and health education services. Children's Hospital and Health System, Inc., is the sole corporate member, or sole shareholder of the for-profit corporation where applicable, of the following entities:

Children's Hospital of Wisconsin, Inc. (the Hospital), which consists of the following:

- Children's Hospital of Wisconsin—Milwaukee, a 298-bed, independent pediatric hospital
- Children's Hospital of Wisconsin—Fox Valley, a 42-bed, independent pediatric hospital, which includes a 22-bed neonatal intensive care unit, located on the campus of Theda Clark Medical Center

Organizationally, these independently licensed, not-for-profit hospitals operate under the Hospital's corporate entity and federal tax identification number.

Children's Hospital of Wisconsin Foundation, Inc. (the Foundation)—A not-for-profit foundation that solicits funds for the maintenance and benefit of the Hospital and CHHS, their programs and activities, and other affiliated not-for-profit organizations within the state of Wisconsin.

Children's Medical Group, Inc.—A not-for-profit organization established for the purpose of providing pediatric primary care services.

Children's Service Society of Wisconsin (CSSW)—A statewide not-for-profit organization that provides child well-being services. CSSW provides services to children and their families in the areas of child welfare, foster care case management, counseling, prevention services, and out-of-home care.

Children's Community Health Plan, Inc. (CCHP)—A nonstock, not-for-profit health insurance organization licensed in the state of Wisconsin under Chapter 613 of the Wisconsin Statutes, *Service Insurance Corporations*. CCHP offers both a Medicaid HMO and commercial exchange product to its members.

Surgicenter of Greater Milwaukee, LLC (the Surgicenter)—A Wisconsin limited liability company wholly owned by Children’s Hospital and Health System, Inc., that consists of an ambulatory surgery center and a medical office building.

Obligated Group—The Hospital and Foundation are the only members of the obligated group (the Obligated Group) for purposes of the issuance of bonds through the Wisconsin Health and Educational Facilities Authority (WHEFA) (see Note 7).

Children’s Specialty Group, Inc. (CSG)—A joint venture between CHHS and the Medical College of Wisconsin (MCW) that provides pediatric specialty health care services. CHHS accounts for its interest in CSG under the equity method of accounting, however, pursuant to an operating agreement, as amended, between CHHS and MCW, all earnings and any material distributions flow to MCW or are retained in CSG for future program development. Therefore, there was no investment recorded in CSG as of December 31, 2018 and 2017.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation—The consolidated financial statements of CHHS have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). All intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates—The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Significant estimated amounts in the consolidated financial statements include contractual allowances, pension obligations, and claims payable.

Cash and Cash Equivalents—Cash and cash equivalents include highly liquid investments purchased with original maturities of three months or less.

Inventory of Supplies—Inventory of supplies is stated at the lower of cost or market, determined using the first-in, first-out method.

Investments—Investments are reported at fair value based primarily upon quoted market prices in active markets, other observable inputs, or unobservable inputs. Both realized and unrealized gains and losses are included in the consolidated statements of operations and changes in net assets, and the change in net unrealized gains or losses on investments without donor restrictions is included within the excess of revenue over expenses. Investment income on funds is allocated between net assets without donor restrictions and net assets with donor restrictions based on amounts invested and donor restrictions. CHHS continues to elect the fair value option for all fixed-income, equity, and mutual fund purchases. A portion of investments without donor restrictions is not intended to be used for current operations, and therefore, is classified as noncurrent assets.

Assets Limited as to Use—Assets limited as to use include assets with donor restrictions and assets held by trustees under indenture agreements.

Pledges—Pledges are recorded based on written instructions from donors. Pledges, less allowances for estimated uncollectible amounts, are recorded as receivables in the year received. Pledges without donor restrictions are recorded as contributions within other operating revenue, and pledges with donor restrictions are recorded as increases in net assets with donor restrictions.

Property and Equipment—Property and equipment are recorded at cost. Depreciation is provided on the straight-line method over the estimated useful lives of the assets, which range from three to 40 years, using American Hospital Association guidelines. Interest costs incurred on borrowed funds during the period of construction are capitalized as a component of the costs of acquiring these assets. Costs of computer software developed or obtained for internal use (including external direct costs of materials and services, payroll, and payroll-related costs for employees directly associated with internal use software development projects incurred during the development period) are expensed or capitalized depending on whether the costs are incurred in the preliminary project stage, development stage, or operational stage. These assets are included in major movable equipment.

CHHS periodically evaluates the carrying value of land, property, equipment, and other intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. There were no impairment charges recorded for the years ended December 31, 2018 and 2017.

Net Assets with Donor Restrictions—Donor restrictions by purpose are for various health-related services, capital projects, child welfare services, research, and for time-restricted remainderman trusts and estates. Donor restrictions in perpetuity restrict the use of funds released for expenditure to various health-related services, child welfare services, and research.

When a donor restriction expires, such as when a stipulated time restriction ends or a purpose restriction is accomplished, net assets with donor restrictions are reclassified as net assets without donor restrictions and reported in the consolidated statements of operations and changes in net assets as other operating revenue (if used for operating purposes) or as net assets released from restrictions—capital acquisitions. Contributions received without donor restrictions are reported as other operating revenue.

Excess of Revenue over Expenses—The consolidated statements of operations and changes in net assets include excess of revenue over expenses. Changes in net assets without donor restrictions, which are excluded from excess of revenue over expenses, include contributions of long-lived assets (including assets acquired using contributions that, by donor restriction, were to be used for the purposes of acquiring such assets), pension-related changes other than net periodic pension cost, and other items in accordance with industry practice.

Net Patient Service Revenue—Net patient service revenue is reported at the amount that reflects the consideration to which CHHS expects to be entitled to in exchange for providing patient care. These amounts are due from patients, third party payors (including managed care payors and government programs) and others and includes 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 shortly 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. 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.

Performance obligations are determined based on the nature of the services provided by CHHS. Revenues for performance obligations satisfied over time are recognized based on actual charges incurred in relation to total expected (or actual) charges. CHHS believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in our hospital receiving inpatient acute care services. CHHS measures the performance obligation from admission into the hospital, or commencement of outpatient services, to the point when it is no longer required to provide services to that patient, which is generally at 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 results as recognizing the obligation at a point in time. Revenue for performance obligations satisfied at a point in time is generally recognized when goods or services are provided and CHHS does not believe it is required to provide additional services to the patient.

CHHS determines the transaction price based on standard charges for services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured or underinsured patients in accordance with CHHS' policies and/or implicit price concessions provided to uninsured or underinsured patients. CHHS determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. CHHS determines its estimates of implicit price concessions based on its historical collection experience with a respective class of patient.

CHHS 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 portfolio consists of major payor classes for inpatient revenue and outpatient revenue. Based on the historical collection trends and other analyses, CHHS believes that revenue recognized by utilizing the portfolio approach approximates the revenue that would have been recognized if an individual contract approach were used.

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

Premium Revenue and Other Capitated Arrangements—Premium revenue is recognized during the period in which CCHP or CHHS is obligated to provide services.

Other Operating Revenue—Other operating revenue comprises grants, contributions without donor restrictions, net assets released from restrictions for operations, rental income, cafeteria revenue, and other revenue. This includes awards from the Department of Health and Human Services for medical education, net of estimated retroactive adjustments.

Donated Goods and Services—CHHS has recorded the estimated fair market value of donated goods and services as revenue and expenses in the consolidated statements of operations and changes in net assets. The amount recorded was \$461 and \$275 for the years ended December 31, 2018 and 2017, respectively. Included in the value of donated goods and services are materials, such as raffle items, auction items, food and beverages, printing, and videotaping services.

CHHS also receives various donated goods and services for which no comparable fair market value is readily determinable. Accordingly, these items are not recorded in the consolidated financial statements.

Professional Liability Insurance—CHHS, along with substantially all Wisconsin health care providers, has professional liability insurance through the Injured Patients and Families Compensation Fund (the "Fund"). CHHS maintains an occurrence basis policy that covers professional liability claims occurring during the policy term, with insurance coverage limits of \$1,000 for each occurrence and \$3,000 for all occurrences in any policy year. The Fund is responsible for paying claims in excess of these limits. CHHS is required to pay an annual assessment to the Fund for the purpose of providing the Fund with monies for payment of claims.

Laws and Regulations—CHHS is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medicaid programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Management believes that CHHS is in substantial compliance with current laws and regulations.

Litigation—CHHS is involved in litigation arising in the normal course of business. After consultation with legal counsel, it is management's opinion that these matters will be resolved without material adverse effect on the consolidated financial position or consolidated results of operations.

Income Taxes—The CHHS not-for-profit organizations (see Note 1) are tax-exempt organizations under Sections 501(c)(3) of the Internal Revenue Code (the "Code") and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. Surgicenter is treated as a partnership for income tax purposes, and since it is owned by a tax-exempt entity, it is treated as a disregarded entity of Children's Hospital and Health System, Inc. CCHP is exempt from federal income taxes, but is subject to state income taxes as the State of Wisconsin does not recognize CCHP's federal tax-exempt status. CHHS evaluates its uncertain tax positions on an annual basis, and there have been no uncertain tax positions recorded for the years ended December 31, 2018 and 2017.

Recently Adopted Accounting Standard Updates—In 2018, CHHS adopted the Financial Accounting Standards Board ("FASB") Accounting Standards Update ("ASU") 2014-09, *Revenue from Contracts with Customers (Topic 606)*, using the modified retrospective approach. ASU 2014-09 supersedes the revenue recognition requirements in Topic 605, Revenue Recognition, and most industry specific guidance. The core principle under ASU 2014-09 is that revenues are recognized to depict the transfer of promised goods or services to customers (patients) in an amount that reflects the consideration at which the entity expects to be entitled in exchange for those goods or services. Additionally, ASU 2014-09 requires enhanced disclosures of revenue arrangements.

As CHHS's performance obligations relate to contracts with a duration of less than one year, CHHS has elected to apply the optional exemption provided in the guidance and is not, therefore, 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.

CHHS has elected the practical expedient allowed under the FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third party payors for the effects of a significant financing component due to CHHS' expectation that the period between the time the services are 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. CHHS does in certain instances enter into payment arrangements with patients that allow payments in excess of one year; however, in these cases the financing component is not deemed to be significant to the contract.

In 2018, CHHS adopted FASB ASU 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. The purpose of Update 2016-01 is to improve financial reporting for financial instruments by reducing the number of items recorded to other comprehensive income. In addition, this update eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities. The adoption of the standard did not have a material impact on our financial position or results of operations.

In 2018, CHHS adopted FASB ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. This update addresses the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return between not-for-profit entities. The changes required by the update have been applied retrospectively to all periods presented. A key change required by ASU 2016-14 are the net asset classes used in these financial statements. Amounts previously reported as unrestricted net assets are now reported as net assets without donor restrictions and amounts previously reported as temporarily restricted net assets and permanently restricted net assets are now reported as net assets with donor restrictions.

Accounting Standard Updates Pending Adoption—In February 2016, the FASB issued ASU 2016-02, *Leases*, which is intended to improve financial reporting related to leasing transactions. This ASU requires a lessee to recognize on the balance sheet assets and liabilities for rights and obligations created by leased assets with lease terms of more than 12 months. The new guidance will also require disclosures to help users of the financial statements better understand the amount, timing, and uncertainty of cash flows arising from leases. These disclosures include qualitative and quantitative requirements, providing additional information about the amounts recorded in the financial statements. The new standard is effective for CHHS as of January 1, 2019. CHHS is evaluating the effect that the guidance will have on its consolidated financial statement and related disclosures. We expect the standard will significantly increase short-term and long-term assets and liabilities upon adoption. The effect on the results of operations is not expected to be significant.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows—Classification of Certain Cash Receipts and Cash Payments*, which addresses the following eight specific cash flow issues in order to limit diversity in practice: debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. This ASU will be effective for CHHS as of January 1, 2019. CHHS is evaluating the effect that the guidance will have on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows—Restricted Cash*, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This ASU will be effective for CHHS as of January 1, 2019. CHHS is evaluating the effect that the guidance will have on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-07, *Compensation—Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. ASU 2017-07 addresses how employers that sponsor defined benefit pension and/or other postretirement benefit plans present the net periodic benefit cost in the income statement. Employers will be required to present the service cost component of net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. Employers will present the other components of the net periodic benefit cost separately from the line item that includes the service cost and outside of any subtotal of operating income, if one is presented. This ASU will be effective for CHHS as of January 1, 2019. Adoption of ASU 2017-07 will require CHHS to include the service cost component of net periodic benefit cost related to its defined benefit pension plans within employee benefits on the consolidated statements of operations and changes in net assets and to present all other components as a separate line item outside of operating income. Total net periodic benefit cost is recorded currently as a component of salaries and benefits on the consolidated statements of operations and changes in net assets.

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. This guidance clarifies and improves the scope and the accounting guidance for contributions received and made with the objective of reducing the existing diversity in practice. This ASU will be effective for CHHS as of January 1, 2019. CHHS is evaluating the effect that the guidance will have on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*. This guidance amends the disclosure requirements for recurring and

nonrecurring fair value measurements by removing, modifying, and adding certain disclosures. This ASU will be effective for CHHS as of January 1, 2020. CHHS is evaluating the impact that the guidance will have on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-14, *Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*. This guidance amends the disclosure requirements applicable to all employers that sponsor defined benefit pension or other postretirement plans by removing and adding certain disclosures. This ASU will be effective for CHHS as of January 1, 2021. CHHS is evaluating the impact that the guidance will have on its consolidated financial statements.

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 consolidated balance sheet in the same line item that a prepayment for the fees of the associated hosting arrangement would be presented. This ASU will be effective for CHHS as of January 1, 2021. CHHS is evaluating the impact that the guidance will have on its consolidated financial statements.

Subsequent Events—CHHS has evaluated subsequent events through April 24, 2019, the date the consolidated financial statements were issued. In February 2019, the CHHS/CHW Board of Directors approved a resolution to terminate the frozen CHHS and CSSW pension plans. CHHS management began the process which will include offering an option of a lump sum payment or annuity to any affected plan participant. The process is expected to be completed in 2020.

3. CASH, CASH EQUIVALENTS, INVESTMENTS, AND ASSETS LIMITED AS TO USE

Cash, cash equivalents, investments, and assets limited as to use as of December 31, 2018 and 2017, consisted of the following:

	2018	2017
Cash	\$ 206,201	\$ 151,232
Investments at fair value:		
Money market funds (cash equivalent)	28,369	60,124
Accrued investment income	3,759	3,517
U.S. government securities	243,782	239,180
U.S. government agency mortgage-backed securities	148,499	127,759
Corporate fixed-income securities	143,587	154,122
International fixed-income securities	75,863	49,264
Municipal fixed-income securities	3,016	3,165
Pooled fixed-income mutual funds	70,702	54,403
Blended mutual funds	40,268	-
Alternative investments-equities	11,894	2,511
Domestic equity securities and mutual funds	373,834	404,120
International equity securities and mutual funds	<u>97,739</u>	<u>110,630</u>
Total	<u>\$ 1,447,513</u>	<u>\$ 1,360,027</u>

These assets are classified on the consolidated statements of financial position as of December 31, 2018 and 2017, as follows:

	2018	2017
Cash and cash equivalents	\$ 216,475	\$ 186,057
Investments	934,581	860,244
Assets limited as to use:		
Limited under bond indentures for capital additions	93,085	100,042
Restricted by donors for specific purpose	42,377	44,755
Restricted by donors in perpetuity	<u>160,995</u>	<u>168,929</u>
Total	<u>\$ 1,447,513</u>	<u>\$ 1,360,027</u>

4. NET ASSETS

CHHS has assets that are restricted by donors either for a specific purpose or to be held in perpetuity. Net assets with donor restrictions for a specific purpose represent amounts that are to be used for capital acquisitions or operating purposes. Net assets with donor restrictions to be held in perpetuity are maintained in accordance with the donor's wishes, and accordingly, may be maintained in perpetuity or may allow for the annual release of funds for expenditure. Board designated assets represent unrestricted funds to be used for future strategic initiatives and require board approval for

appropriations from the fund. As of December 31, 2018 and 2017, net assets without donor restrictions are held for the following purposes:

	2018	2017
Net assets without donor restrictions:		
Undesignated	\$ 801,497	\$ 770,678
Board designated	<u>408,416</u>	<u>401,389</u>
Total net assets without donor restrictions	<u>\$ 1,209,913</u>	<u>\$ 1,172,067</u>

As of December 31, 2018 and 2017, net assets with donor restrictions are held for the following purposes:

	Subject to Expenditure for Specified Purpose		Subject to Spending Policy and Appropriation		Total	
	2018	2017	2018	2017	2018	2017
Net assets with donor restrictions:						
Health care services	\$ 48,021	\$ 50,092	\$ 172,675	\$ 182,520	\$ 220,696	\$ 232,612
Capital projects	1,890	3,143	787	-	2,677	3,143
Health education	2,183	2,551	277	300	2,460	2,851
Social services	<u>1,544</u>	<u>1,253</u>	<u>794</u>	<u>872</u>	<u>2,338</u>	<u>2,125</u>
Total net assets with donor restrictions	<u>\$ 53,638</u>	<u>\$ 57,039</u>	<u>\$ 174,533</u>	<u>\$ 183,692</u>	<u>\$ 228,171</u>	<u>\$ 240,731</u>

As of December 31, 2018 and 2017, the assets of CHHS designated for restricted purposes include the following:

	Subject to Expenditure for Specified Purpose		Subject to Spending Policy and Appropriation		Total	
	2018	2017	2018	2017	2018	2017
Investments—Endowment	\$ 6,957	\$ 9,269	\$ 160,995	\$ 168,929	\$ 167,952	\$ 178,198
Investments—other	35,420	35,486	-	-	35,420	35,486
Pledges receivable—net	10,521	11,550	10,505	11,406	21,026	22,956
Charitable trusts and bequests	<u>740</u>	<u>734</u>	<u>3,033</u>	<u>3,357</u>	<u>3,773</u>	<u>4,091</u>
Total	<u>\$ 53,638</u>	<u>\$ 57,039</u>	<u>\$ 174,533</u>	<u>\$ 183,692</u>	<u>\$ 228,171</u>	<u>\$ 240,731</u>

5. ENDOWMENT INVESTMENTS

The Foundation manages one investment portfolio and allocates a portion of the investments to assets limited as to use based on the amount of net assets with restrictions, less outstanding pledges and trusts. The Foundation follows the direction set forth by the donor to determine the preservation of the historic value of endowment funds. Restricted investments are adjusted for fair value changes or investment returns when specifically required by the donor's wishes.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or the law requires the Foundation to retain as a fund of perpetual duration. There were no deficiencies of this nature for the years ended December 31, 2018 and 2017.

The Foundation does not limit its spending of purpose-restricted donations based on its investment portfolio and return objectives. Purpose-restricted funds become available

for expenditure once cash is received from the donor and the circumstances requested by the donor occur. Certain donors have elected to follow the Foundation's endowment policy whereby the endowment funds retain their related investment returns and release an annual allocation for spending based on each fund's historical value. All other endowment funds are maintained in perpetuity, while the related investment income is released for spending based on the donor's wishes. In order to preserve Foundation assets and plan annual grants in support of pediatric activities in accordance with the Foundation's articles of incorporation, expenditures of Foundation assets without donor restrictions are limited to 5% of the trailing three-year fair market value of cash and investments without donor restrictions. This policy can be adjusted with the approval of the board of directors.

The Foundation's primary objective for endowment funds is to optimize the total return of Foundation funds and preserve capital within stated parameters, and secondarily to generate current income. The Investment Subcommittee of the CHHS Board of Directors (the "Investment Subcommittee") evaluates an investment manager's performance against their respective benchmark.

The Foundation targets a long-term asset allocation mix of approximately 65% risk assets (defined as the sum of equities and alternatives) with the balance in fixed-income securities. The Investment Subcommittee monitors and controls the distribution of investments among its selected investment managers to maintain a maximum-minimum range of 70% to 50% for equities, 10%–0% for alternative investments, and 50%–20% for fixed-income securities. The diversification of securities held in each investment manager's portfolio, among sectors and issuers, is the responsibility of each investment manager, consistent with the market objectives identified at the time of the initial investment. Each investment manager is expected to diversify the portfolio sufficiently to minimize the risk of a large loss from a single security or from the securities of a single issuer.

Information regarding the composition of the Foundation endowment fund activity as of and for the years ended December 31, 2018 and 2017, is as follows:

	Total	Board Designated Endowment Funds	Donor-Restricted Endowment Funds
Balances—December 31, 2016	\$ 404,227	\$ 250,353	\$ 153,874
Total investment return	68,969	46,141	22,828
Contributions	2,917	451	2,466
Transfers to board designated	109,444	109,444	-
Transfers from board designated	-	(5,000)	5,000
Net assets released from restrictions	<u>(5,970)</u>	<u>-</u>	<u>(5,970)</u>
Balances—December 31, 2017	579,587	401,389	178,198
Total investment return	(28,289)	(19,604)	(8,685)
Contributions	5,585	631	4,954
Transfers to board designated	26,000	26,000	-
Net assets released from restrictions	<u>(6,515)</u>	<u>-</u>	<u>(6,515)</u>
Balances—December 31, 2018	<u>\$ 576,368</u>	<u>\$ 408,416</u>	<u>\$ 167,952</u>

The information above reflects the activity of the Foundation's endowment investable funds. The above information excludes pledge receivables and charitable trusts and bequests of \$13,538, \$14,763, and \$5,768, from funds with donor restrictions as of December 31, 2018, 2017, and 2016, respectively.

Pledges—As of December 31, 2018 and 2017, pledges receivable of \$21,092 and \$23,088, respectively, were recorded. Pledges receivable in excess of one year are discounted at the risk-free rate in the year the pledge is received. Discount rates ranged from 0.7% to 2.5% and 0.7% to 2.2% as of December 31, 2018 and 2017, respectively. Such discounts amounted to \$917 and \$1,073 as of December 31, 2018 and 2017, respectively. Allowances for uncollectible pledges totaled \$800 and \$851 as of December 31, 2018 and 2017, respectively. The maturities of the pledges receivable as of December 31, 2018 and 2017, are as follows:

	2018	2017
Pledges—less than one year	\$ 9,043	\$ 8,786
Pledges—one to five years	11,050	12,650
Pledges—over five years	999	1,652

Charitable Trusts and Bequests—As of December 31, 2018 and 2017, \$3,773 and \$4,091, respectively, of charitable trusts and bequests have been recorded where the Foundation is an irrevocable beneficiary. Such assets are recorded as restricted by purpose or restricted in perpetuity until the stipulations of the donors have been satisfied. These charitable trusts and bequests are recorded at estimated fair value. Assumptions used to determine the fair values as of December 31, 2018 and 2017, include an investment rate of return of 5.25% and 5.50%, respectively, and a discount rate using the federally published rate in effect at the time the gift was received.

The Foundation has a policy whereby charitable trusts are recorded when the trust is irrevocable, and the current value of the trust assets is available. The Foundation is aware of certain trusts for which it may be the beneficiary, which do not meet these criteria. Estimates of the value of such trusts are not recorded in the consolidated financial statements.

6. PROPERTY AND EQUIPMENT

As of December 31, 2018 and 2017, property and equipment consisted of the following:

	2018	2017
Cost of property and equipment:		
Land	\$ 1,723	\$ 1,723
Buildings and improvements	646,179	637,261
Major movable equipment	249,387	260,994
Projects in progress	<u>33,934</u>	<u>15,602</u>
Total cost of property and equipment	931,223	915,580
Less accumulated depreciation and amortization	<u>(475,094)</u>	<u>(459,543)</u>
Property and equipment—net	<u>\$ 456,129</u>	<u>\$ 456,037</u>

Projects in progress as of December 31, 2018 relate primarily to renovation and expansion projects at the Hospital.

7. EMPLOYEE BENEFIT PLANS

Defined Contribution Plans—CHHS sponsors the Shared Retirement Savings Plans, defined contribution plans that include a discretionary employer match of one-half of employee contributions up to 8% of eligible employee compensation and a service-based contribution for eligible employees. During the years ended December 31, 2018 and 2017, the combined CHHS matching and service-based contribution was approximately \$18,103 and \$16,546, respectively, which is included in employee benefits expense on the consolidated statements of operations and changes in net assets.

Pension Plans—CHHS maintains a multiple-employer noncontributory, defined-benefit pension plan (the "CHHS pension plan"). The CHHS pension plan includes only certain employees of CHHS, and substantially all plan participants were employees of the Hospital. The Hospital makes all employer contributions, records the accrued pension liability and pension-related changes other than net periodic pension cost, and allocates the annual net periodic pension cost to the participating CHHS affiliates. The CHHS board of directors approved the curtailment of the CHHS pension plan effective December 31, 2009.

CSSW sponsors a defined-benefit pension plan (the "CSSW pension plan") that covered substantially all CSSW employees employed prior to its curtailment. The CSSW pension plan calls for benefits to be paid to eligible employees at retirement, based primarily upon each eligible employee's years of service with CSSW and compensation rate near retirement. The CSSW board of directors approved the curtailment of the CSSW pension plan effective December 31, 2004.

CHHS' policy is to fund the amounts necessary to meet the requirements of Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974 (ERISA), as amended, for each of

the pension plans. Information regarding the benefit obligations and assets of the pension plans as of and for the years ended December 31, 2018 and 2017, is as follows:

	CHHS		CSSW	
	2018	2017	2018	2017
Change in benefit obligation:				
Benefit obligation—beginning of year	\$ 298,871	\$ 270,900	\$ 10,717	\$ 10,076
Service cost	-	-	37	37
Interest cost	11,528	12,151	412	461
Actuarial (gain) loss	(22,486)	23,327	(594)	715
Expenses	-	-	(32)	(32)
Benefit payments	<u>(8,239)</u>	<u>(7,507)</u>	<u>(583)</u>	<u>(540)</u>
Benefit obligation—end of year	<u>279,674</u>	<u>298,871</u>	<u>9,957</u>	<u>10,717</u>
Reconciliation of fair value of plan assets:				
Fair value of plan assets—beginning of year	267,816	237,832	8,358	7,984
Actual return on plan assets	(17,268)	34,591	(329)	946
Employer contributions	2,600	2,900	21	-
Benefit payments	(8,239)	(7,507)	(583)	(540)
Expenses	<u>-</u>	<u>-</u>	<u>(32)</u>	<u>(32)</u>
Fair value of plan assets—end of year	<u>244,909</u>	<u>267,816</u>	<u>7,435</u>	<u>8,358</u>
Unfunded status—end of year	<u>\$ 34,765</u>	<u>\$ 31,055</u>	<u>\$ 2,522</u>	<u>\$ 2,359</u>
Change in net amount recognized:				
Accrued pension—prior year	\$ 31,055	\$ 33,068	\$ 2,359	\$ 2,092
Net periodic pension cost	2,196	900	65	37
Employer contributions	(2,600)	(2,900)	(21)	-
Pension-related changes other than net periodic pension cost	<u>4,114</u>	<u>(13)</u>	<u>119</u>	<u>230</u>
Accrued pension—current year	<u>\$ 34,765</u>	<u>\$ 31,055</u>	<u>\$ 2,522</u>	<u>\$ 2,359</u>
Discount rate—January 1	3.92 %	4.56 %	3.92 %	4.56 %
Discount rate—December 31	4.48	3.92	4.48	3.92
Expected return on plan assets	5.50	6.00	6.75	7.50

As a result of the curtailment of both pension plans, the projected benefit obligation equals the accumulated benefit obligation.

Total expense for the CHHS and CSSW pension plans for the years ended December 31, 2018 and 2017 was \$2,261 and \$939, respectively. The expense is included in employee benefits in the accompanying consolidated statements of operations and changes in net assets.

To develop the expected long-term rate of return on asset assumptions, CHHS and CSSW considered the historical returns and future expectations for returns in each asset class, as well as targeted asset allocation percentages within the respective pension portfolios. Pension investments are managed in accordance with each pension

plan's statement of investment objectives and policy guidelines, as established and maintained by the Investment Subcommittee. The Investment Subcommittee selects investment managers based on the investment objectives and regularly evaluates each manager's performance based on industry benchmarks. The investment policy guidelines establish asset allocation, quality targets, and performance expectations, as well as regular reporting requirements. The target asset allocation for the CHHS pension plan is 25% equity and 75% fixed-income securities. The target allocation for the CSSW pension plan is 50% equity securities and 50% fixed-income securities. Within each plan, each class is diversified with multiple managers with differing styles of management. The fair value of pension plan assets measured using quoted prices in active markets for identical assets (Level 1 of the fair value hierarchy) and significant other observable inputs (Level 2 of the fair value hierarchy), using techniques consistent with those listed in Note 13, as of December 31, 2018 and 2017, are as follows:

	Total		Fair Value Measurements Using			
			(Level 1)		(Level 2)	
	2018	2017	2018	2017	2018	2017
CHHS pension plan assets:						
Money market accounts	\$ 5,528	\$ 9,376	\$ 5,528	\$ 9,376	\$ -	\$ -
Fixed-income securities:						
U.S. government	64,132	65,269	-	-	64,132	65,269
U.S. government agency mortgage-backed	3,254	1,971	-	-	3,254	1,971
Corporate	76,189	100,892	-	-	76,189	100,892
International	33,278	17,155	-	-	33,278	17,155
Municipal	1,369	1,120	-	-	1,369	1,120
Equity securities and funds:						
Large cap	30,576	37,767	30,576	37,767	-	-
Mid cap	8,499	9,041	8,499	9,041	-	-
Small cap	4,021	4,653	4,021	4,653	-	-
International	11,446	13,839	11,446	13,839	-	-
Emerging markets	3,435	4,162	3,435	4,162	-	-
Total	<u>\$ 241,727</u>	<u>\$ 265,245</u>	<u>\$ 63,505</u>	<u>\$ 78,838</u>	<u>\$ 178,222</u>	<u>\$ 186,407</u>
CSSW pension plan assets:						
Money market accounts	\$ 560	\$ 598	\$ 560	\$ 598	\$ -	\$ -
Equity securities and funds:						
Large cap	1,484	1,678	1,484	1,678	-	-
Mid cap	677	844	677	844	-	-
Small cap	337	419	337	419	-	-
International	687	880	687	880	-	-
Real Estate Investment Trust	383	406	383	406	-	-
Total	<u>4,128</u>	<u>4,825</u>	<u>\$ 4,128</u>	<u>\$ 4,825</u>	<u>\$ -</u>	<u>\$ -</u>
Investments measured at net asset value	<u>3,307</u>	<u>3,533</u>				
Total	<u>\$ 7,435</u>	<u>\$ 8,358</u>				

The components of net periodic pension cost that are included in employee benefits expense and pension-related changes other than net periodic pension cost, which are included as a change in unrestricted net assets in the consolidated statements of

operations and changes in net assets for the years ended December 31, 2018 and 2017, are as follows:

	CHHS		CSSW	
	2018	2017	2018	2017
Components of net periodic pension cost:				
Service cost	\$ -	\$ -	\$ 37	\$ 37
Interest cost	11,528	12,151	412	461
Expected return on plan assets	(13,899)	(14,352)	(545)	(601)
Amortization of net loss	<u>4,567</u>	<u>3,101</u>	<u>161</u>	<u>140</u>
Net periodic pension cost	<u>\$ 2,196</u>	<u>\$ 900</u>	<u>\$ 65</u>	<u>\$ 37</u>
Pension-related changes other than net periodic pension cost:				
Accumulated loss	\$ 8,681	\$ 3,088	\$ 280	\$ 370
Amortization of net loss	<u>(4,567)</u>	<u>(3,101)</u>	<u>(161)</u>	<u>(140)</u>
Total recognized as changes in net assets without donor restrictions	<u>\$ 4,114</u>	<u>\$ (13)</u>	<u>\$ 119</u>	<u>\$ 230</u>

A summary of the pension-related items recorded in unrestricted net assets and not yet recognized as a component of net periodic pension cost as of December 31, 2018 and 2017, is as follows:

	CHHS		CSSW	
	2018	2017	2018	2017
Amounts not yet reflected in net periodic pension cost—accumulated loss	<u>\$(63,993)</u>	<u>\$(59,879)</u>	<u>\$(3,153)</u>	<u>\$(3,034)</u>

A summary of the expected amortization amounts to be included in net periodic pension cost for 2019 is as follows:

	CHHS	CSSW
Net actuarial loss	<u>\$ 2,248</u>	<u>\$ 184</u>

The benefit payments are expected to be paid as follows:

Years Ending December 31	CHHS	CSSW
2019	\$10,336	\$ 640
2020	11,306	633
2021	12,251	631
2022	13,307	636
2023	14,180	648
2024 and thereafter	80,208	3,156

The expected CHHS contribution in 2019 is \$2,400.

8. LONG-TERM DEBT

As of December 31, 2018 and 2017, long-term debt is as follows:

	2018	2017
WHEFA Revenue Bonds ("Bonds"):		
Fixed-rate Series 2017—including unamortized premium and debt issuance costs of \$13,086 and \$13,861 2018 and 2017, respectively, principal payable in annual installments from 2023 through 2047 in amounts ranging from \$4,935 to \$19,615, interest payable semiannually at rates ranging from 3.25%–5.0%	\$ 328,486	\$ 315,400
Fixed-rate taxable bank loan, payable in monthly installments from 2019 through 2023 including principal amounts ranging from \$290 to \$630, and 2.38% interest	<u>30,110</u>	<u>36,405</u>
Total long-term debt	358,596	351,805
Less current installments	<u>(6,690)</u>	<u>(6,295)</u>
Long-term debt—net	<u>\$ 351,906</u>	<u>\$ 345,510</u>

The Hospital and Foundation are the only members of the Obligated Group for purposes of the Bonds. Payment of scheduled principal and interest is secured by a pledge of the Hospital's and Foundation's gross unrestricted receivables.

The Obligated Group must meet a debt service coverage ratio financial covenant required by the bond trustee. The Obligated Group was in compliance with its financial covenant at December 31, 2018.

Scheduled annual principal payments on the Bonds and taxable bank loan for the next five years and thereafter are as follows:

Years Ending December 31	
2019	\$ 6,690
2020	6,845
2021	7,015
2022	7,185
2023	7,310
Thereafter	<u>310,465</u>
Total	<u>\$345,510</u>

In 2017, the Hospital issued Series 2017 Bonds of \$315,400 and took out a taxable bank loan of \$36,405. The proceeds were used to repay \$248,315 of Series 2008A and 2008B Bonds, to fund \$100,000 of construction projects, and to fund the cost of issuance. The portion of the proceeds used to repay the Series 2008A and 2008B Bonds were deposited in a trust with an escrow agent to provide for all remaining future debt

payments on the Series 2008A and 2008B Bonds. These transactions resulted in a loss on extinguishment of debt of \$16,061, which is included as a nonoperating expense in the 2017 consolidated statement of operations and changes in net assets.

9. LEASES

CHHS and affiliates lease certain land, building space, and medical and other equipment under operating leases having terms of more than one year. Rent expense was approximately \$18,389 and \$16,818 for the years ended December 31, 2018 and 2017, respectively. These amounts are included in operation and maintenance of facilities or non-medical supplies and other in the consolidated statements of operations and changes in net assets.

The main campus of the Hospital, located in Wauwatosa, Wisconsin, is on approximately twelve acres of land leased from Milwaukee County. The lease has a term of 100 years, which commenced March 1, 1985, with nominal rent expense for the first 50 years. The Hospital leased an additional 43 acres of land on Milwaukee County grounds in 2001. This 100-year lease with Milwaukee County provides the Hospital with adequate space and parking to meet local and regional needs for pediatric health care, education, and research.

CHHS leases a portion of its facilities to other providers. Rental income was \$5,876 and \$5,403 for the years ended December 31, 2018 and 2017, respectively. These amounts are included in other operating revenue in the consolidated statements of operations and changes in net assets.

Aggregate commitments under operating leases that have initial or remaining lease terms in excess of one year, less rental income, are as follows:

Years Ending December 31	Operating Leases
2019	\$ 13,758
2020	13,724
2021	13,079
2022	11,687
2023	8,913
Thereafter	<u>82,076</u>
Total commitments under leases	143,237
Less rental income from noncancelable leases	<u>(14,680)</u>
Net commitments under operating leases	<u>\$128,557</u>

10. REVENUE AND RECEIVABLES

The amount, timing and uncertainty of revenue recognized is affected by payor and service line associated with this revenue. The composition of net patient service revenue by payor for the years ended December 31 is as follows:

	<u>2018</u>		<u>2017</u>	
Commercial and managed care	\$527,831	72 %	\$474,567	69 %
Medicaid and Medicaid HMO	189,191	26	199,514	29
Medicare and other government	7,059	1	7,798	1
Self pay and other	<u>4,293</u>	<u>1</u>	<u>3,988</u>	<u>1</u>
Total net patient service revenue	<u>\$728,374</u>	<u>100 %</u>	<u>\$685,867</u>	<u>100 %</u>

The self-pay revenue above includes only revenue from patients without insurance. The revenue related to amounts due from patients for co-insurance and deductibles is included with the related primary insurance coverage.

The composition of net patient service revenue by service line for the years ended December 31 is as follows:

	<u>2018</u>		<u>2017</u>	
Hospital inpatient	\$389,975	54 %	\$370,414	54 %
Hospital outpatient	264,816	36	247,940	36
Primary Care	58,300	8	53,399	8
Ambulatory Surgery Center	8,899	1	7,492	1
Other Health Care	<u>6,381</u>	<u>1</u>	<u>6,622</u>	<u>1</u>
Total net patient service revenue	<u>\$728,374</u>	<u>100 %</u>	<u>\$685,867</u>	<u>100 %</u>

The composition of patient accounts receivable by payor as of December 31 is as follows:

	<u>2018</u>		<u>2017</u>	
Commercial and managed care	\$63,865	71 %	\$53,706	60 %
Medicaid and Medicaid HMO	17,517	20	25,671	29
Medicare and other government	745	1	1,024	1
Self pay and other	<u>7,365</u>	<u>8</u>	<u>8,685</u>	<u>10</u>
Total patient accounts receivable	<u>\$89,492</u>	<u>100 %</u>	<u>\$89,086</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.

In certain instances, CHHS will receive payment in advance of the services provided and would consider these amounts to represent contract liabilities. Contract liabilities as of December 31, 2018 and 2017 are not significant.

During 2009, the State of Wisconsin enacted legislation that created a tax assessment on hospital revenue. Funds collected under the tax assessment are used to increase federal funding for the Wisconsin Medicaid program. The Hospital recognized \$65,991 and \$66,339 of Medicaid and Medicaid HMO reimbursement for the years ended December 31, 2018 and 2017, respectively, which is included in net patient service revenue in the consolidated statements of operations and changes in net assets, as well as \$10,751 and \$10,762 of provider tax expense as a result of the law for the years ended December 31, 2018 and 2017, respectively. In 2011, the State of Wisconsin enacted legislation that created a tax assessment on ambulatory surgical centers. This legislation continued until October 1, 2017. As a result, the Surgicenter paid \$0 and \$105 of provider tax and recognized \$0 and \$124 of additional Medicaid reimbursement for the years ended December 31, 2018 and 2017, respectively.

Laws and regulations governing the Medicare and Medical Assistance programs are extremely complex and subject to interpretation. Compliance with such laws and regulations are subject to government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from Medicare and Medical Assistance programs. As a result, there is at least a reasonable possibility that the recorded estimates may change.

11. CHARITY AND UNREIMBURSED CARE

CHHS has a policy of providing free health care services to those unable to pay all or a portion of their charges and who meet certain eligibility criteria established in CHHS' charity care policy.

CHHS maintains records and monitors the level of charity and unreimbursed care it provides. The costs of charity and unreimbursed care, which are estimated using the ratio of total patient care cost to charges, for the years ended December 31, 2018 and 2017, are as follows:

	2018	2017
Medicaid, Medicaid HMO, and other government	\$103,850	\$86,994
Charity care	<u>845</u>	<u>788</u>
Total	<u>\$104,695</u>	<u>\$87,782</u>

12. FUNCTIONAL EXPENSES

CHHS exists for the purpose of providing an organized system for the delivery and management of pediatric health care and related services. Natural expenses attributable to more than one functional expense category are allocated using a variety of cost allocation techniques such as square footage and time and effort.

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

2018	Healthcare	Health Plans	Child Welfare Services	Research	Fundraising	Admin	Consolidated Total
Salaries	\$ 251,745	\$ 11,011	\$ 20,526	\$ 724	\$ 3,511	\$ 61,165	348,683
Employee benefits	70,423	3,474	8,530	194	891	15,648	99,160
Medical supplies	89,067	-	2	11	-	163	89,243
Non-medical supplies and other	20,554	1,065	2,513	46	1,052	6,563	31,793
Net medical claims expenses	-	335,916	-	-	-	-	335,916
Purchased services and professional fees	50,620	37,155	6,355	7,207	2,182	30,122	133,641
Operation and maintenance of facilities	30,031	605	129	1,822	33	6,812	39,433
Medical College of Wisconsin and resident fees	53,677	588	-	789	-	464	55,518
Provider tax	10,751	-	-	-	-	-	10,751
Depreciation	59,414	192	544	1,763	68	1,196	63,178
Interest	12,807	-	-	-	-	-	12,807
Total	<u>\$ 649,090</u>	<u>\$ 390,007</u>	<u>\$ 38,600</u>	<u>\$ 12,557</u>	<u>\$ 7,737</u>	<u>\$ 122,133</u>	<u>\$ 1,220,123</u>

Expenses by functional classification for the year ended December 31, 2017 consist of the following:

2017	Healthcare	Health Plans	Child Welfare Services	Research	Fundraising	Admin	Consolidated Total
Salaries	\$ 236,583	\$ 9,547	\$ 19,836	\$ 812	\$ 3,972	\$ 60,360	\$ 331,110
Employee benefits	61,231	2,868	7,599	201	894	14,202	86,995
Medical supplies	81,141	4	2	22	-	156	81,325
Non-medical supplies and other	15,836	766	2,510	30	836	7,964	27,941
Net medical claims expenses	-	214,467	-	-	-	-	214,467
Purchased services and professional fees	50,069	20,239	4,379	6,608	2,202	30,260	113,757
Operation and maintenance of facilities	28,381	609	2,401	1,773	30	4,137	37,332
Medical College of Wisconsin and resident fees	44,764	597	-	708	-	595	46,664
Provider tax	10,867	-	-	-	-	-	10,867
Depreciation	57,041	179	553	1,734	56	989	60,552
Interest	13,374	-	-	-	-	-	13,374
Total	<u>\$ 599,287</u>	<u>\$ 249,277</u>	<u>\$ 37,279</u>	<u>\$ 11,889</u>	<u>\$ 7,990</u>	<u>\$ 118,663</u>	<u>\$ 1,024,384</u>

13. FAIR VALUE OF FINANCIAL INSTRUMENTS

Financial instruments consist primarily of cash and cash equivalents, investments, accounts receivable, pledges receivable, accounts payable, and long-term debt. Except for long-term debt, which is recorded at historic cost, the fair values of these instruments approximate their carrying amounts as of December 31, 2018 and 2017. The fair values of financial assets and liabilities are measured on a recurring basis using quoted prices in active markets for identical assets (Level 1 of the fair value hierarchy), significant other observable inputs (Level 2 of the fair value hierarchy), and significant unobservable inputs (Level 3 of the fair value hierarchy).

The fair values of financial assets that are measured on a recurring basis as of December 31, 2018 and 2017, are as follows:

	Fair Value Measurements Using							
	Total		(Level 1)		(Level 2)		(Level 3)	
	2018	2017	2018	2017	2018	2017	2018	2017
Assets—Investments at fair value:								
Money market funds	\$ 28,369	\$ 60,124	\$ 28,369	\$ 60,124	\$ -	\$ -	\$ -	\$ -
Fixed-income securities:								
U.S. government	243,782	239,180	-	-	243,782	239,180	-	-
U.S. government agency mortgage-backed	148,499	127,759	-	-	148,499	127,759	-	-
Corporate	143,587	154,122	-	-	143,587	154,122	-	-
International	75,863	49,264	-	-	75,863	49,264	-	-
Municipal	3,016	3,165	-	-	3,016	3,165	-	-
Pooled mutual funds	70,702	54,403	70,702	54,403	-	-	-	-
Blended Mutual Fund	40,268	-	40,268	-	-	-	-	-
Equity securities and funds:								
Large cap	301,409	325,786	301,409	325,786	-	-	-	-
Mid cap	48,012	50,703	48,012	50,703	-	-	-	-
Small cap	24,413	27,631	24,413	27,631	-	-	-	-
International	71,901	79,416	71,901	79,416	-	-	-	-
Alternative investments	-	2,511	-	-	-	-	-	2,511
Emerging markets	25,838	31,214	25,838	31,214	-	-	-	-
Total	\$ 1,225,659	\$ 1,205,278	\$ 610,912	\$ 629,277	\$ 614,747	\$ 573,490	\$ -	\$ 2,511
Investments measured at net asset value	11,894							
Total	\$ 1,237,553							

Transfers between Level 1 and Level 2 are recognized at the end of the reporting period. There were no transfers during 2018. During 2017, certain emerging market securities with a total value of \$127 were transferred from a Level 2 to a Level 1 measurement due to a change in pricing technique.

Money Market and Mutual Funds—Valued at net asset value (NAV) of shares held at year-end. For funds that are publicly traded, quoted market prices are used. Mutual funds are classified based on the underlying assets of the fund.

Fixed-Income Securities—Valued based on a compilation of observable market information or broker quote in an inactive market.

Equity Securities—Valued at the closing price reported on the active markets on which the individual securities are traded. Certain equities are valued at the bid price.

Alternative Investments – Valued based on the net asset value (NAV) per share. The NAV is used as a practical expedient to estimate fair value. The NAV is based on the fair value of the underlying investments held by the fund less its liabilities. The following table sets forth a summary of CHHS' investments whose values were estimated using a reported NAV at December 31, 2018.

Investments Measured at Net Asset Value—Certain investments that are measured using the NAV per share practical expedient have not been classified in the fair value hierarchy. The NAV amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amount presented in Note 3.

**Fair Value Estimated Using Net Asset Value per Share
December 31, 2018**

Investment	Fair Value*	Unfunded Commitment
US Private Equity	\$ 4,864	\$ 24,967
US Venture Capital	5,377	21,599
Opportunistic Strategies	<u>1,653</u>	<u>11,133</u>
	<u>\$ 11,894</u>	<u>\$ 57,699</u>

* The fair values of the investments have been estimated using the net asset value of the investment.

The Foundation invests in various long-life partnerships. As of December 31, 2018, the portfolio included 18 partnerships with total commitments of \$69,800. Of this total, \$12,101 has been funded as of December 31, 2018, with unfunded commitments of \$57,699 remaining. The partnerships have an expected life of between 8 and 13 years. The return of capital and additional income will occur over the life of the partnerships with no periodic redemption. The partnerships include buyout/growth equity, venture capital and opportunistic strategies. Of the total, 11 are focused within the information technology sector, 2 in healthcare and 5 in other market sectors such as industrial, retail, consumer products and business services.

14. LIQUIDITY AND AVAILABILITY OF FINANCIAL ASSETS

CHHS's financial assets available within one year of the balance sheet date for general expenditures such as operating expenses, scheduled principal payments on debt and construction costs not financed with debt are as follows:

	2018
Cash and cash equivalents	\$ 216,475
Patient accounts receivable	89,492
Other receivables	36,213
Investments	<u>934,581</u>
Total financial assets	1,276,761
Receivables scheduled to be collected in more than one year	(3,185)
Contractual restrictions:	
Alternative investment unfunded commitments	(57,699)
Health plan minimum statutory capital	(36,320)
Board designations:	
Operating/capital reserves	<u>(356,983)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 822,574</u>

CHHS has commitments to funding various alternative investments. As of December 31, 2018, those unfunded commitments totaled \$57.7 million. In addition, CCHP is required by the National Association of Insurance Commissioners (NAIC) to maintain minimum capital levels. As of December 31, 2018, the minimum capital amount required was \$36.3 million. CHHS also has board of directors' designated funds of \$357.0 million that are available for general expenditure with board approval as of December 31, 2018. The availability of certain amounts within the board designated investments may change in accordance with Board policies at any time.

As part of CHHS' liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities and other obligations come due. In addition, CHHS invests cash in excess of daily requirements in short-term investments. CHHS has a goal to maintain financial assets, which consists of cash and short-term investments, on hand to meet normal operating expenses.

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SUPPLEMENTARY CONSOLIDATING INFORMATION



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INDEPENDENT AUDITORS' REPORT ON SUPPLEMENTARY CONSOLIDATING INFORMATION

To the Board of Directors of
Children's Hospital and Health System, Inc. and Affiliates:

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The 2018 supplementary consolidating information on pages 35-37 is presented for the purpose of additional analysis, and is not a required part of the consolidated financial statements. This supplementary information is the responsibility of Children's Hospital and Health System, Inc. and Affiliates' management and was derived from and relates directly to the underlying accounting and other records used to prepare the 2018 consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audit of the 2018 consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, such information is fairly stated in all material respects in relation to the 2018 consolidated financial statements as a whole.

Deloitte & Touche LLP

April 24, 2019

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATING STATEMENT OF FINANCIAL POSITION INFORMATION

AS OF DECEMBER 31, 2018

(Dollars in thousands)

	Obligated Group				Children's Hospital and Health System, Inc.	Children's Medical Group, Inc.	Children's Service Society of Wisconsin	Children's Community Health Plan, Inc.	Surgicenter of Greater Milwaukee, LLC	Eliminations	Consolidated
	Children's Hospital of Wisconsin, Inc.	Children's Hospital of Wisconsin Foundation, Inc.	Eliminations	Combined							
ASSETS											
CURRENT ASSETS:											
Cash and cash equivalents	\$ 83,185	\$ 13,464	\$ -	\$ 96,649	\$ 1,146	\$ 463	\$ 904	\$ 115,071	\$ 2,242	\$ -	\$ 216,475
Patient accounts receivable	90,652	-	-	90,652	1,421	3,718	127	-	1,264	(7,690)	89,492
Other receivables	7,428	47	-	7,475	547	78	4,731	23,382	-	-	36,213
Inventory of supplies	8,779	-	-	8,779	-	1,254	-	-	566	-	10,599
Prepaid expenses	8,097	349	-	8,446	8,618	551	210	426	7	-	18,258
Intercompany receivable	72,411	-	(32,356)	40,055	-	-	-	-	2,839	(42,894)	-
Total current assets	<u>270,552</u>	<u>13,860</u>	<u>(32,356)</u>	<u>252,056</u>	<u>11,732</u>	<u>6,064</u>	<u>5,972</u>	<u>138,879</u>	<u>6,918</u>	<u>(50,584)</u>	<u>371,037</u>
INVESTMENTS	<u>327,562</u>	<u>573,149</u>	<u>-</u>	<u>900,711</u>	<u>14,396</u>	<u>-</u>	<u>-</u>	<u>22,110</u>	<u>11,760</u>	<u>(14,396)</u>	<u>934,581</u>
ASSETS LIMITED AS TO USE:											
Limited under bond indentures for capital additions	93,085	-	-	93,085	-	-	-	-	-	-	93,085
Restricted by donors for specific purpose	-	53,638	-	53,638	-	-	-	-	-	-	53,638
Restricted by donors in perpetuity	-	174,533	-	174,533	-	-	-	-	-	-	174,533
Total assets limited as to use	<u>93,085</u>	<u>228,171</u>	<u>-</u>	<u>321,256</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>321,256</u>
PROPERTY AND EQUIPMENT—Net	<u>399,183</u>	<u>698</u>	<u>-</u>	<u>399,881</u>	<u>29,534</u>	<u>13,665</u>	<u>2,907</u>	<u>887</u>	<u>9,255</u>	<u>-</u>	<u>456,129</u>
OTHER ASSETS	<u>2,806</u>	<u>32</u>	<u>-</u>	<u>2,838</u>	<u>10,117</u>	<u>5,317</u>	<u>-</u>	<u>153</u>	<u>-</u>	<u>-</u>	<u>18,425</u>
BENEFICIAL INTEREST IN NET ASSETS OF CHILDREN'S HOSPITAL OF WISCONSIN FOUNDATION, INC.	<u>627,587</u>	<u>-</u>	<u>(627,587)</u>	<u>-</u>	<u>2,460</u>	<u>-</u>	<u>2,338</u>	<u>-</u>	<u>-</u>	<u>(4,798)</u>	<u>-</u>
TOTAL	<u>\$ 1,720,775</u>	<u>\$ 815,910</u>	<u>\$(659,943)</u>	<u>\$ 1,876,742</u>	<u>\$ 68,239</u>	<u>\$ 25,046</u>	<u>\$ 11,217</u>	<u>\$ 162,029</u>	<u>\$ 27,933</u>	<u>\$(69,778)</u>	<u>\$ 2,101,428</u>

(Continued)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

CONSOLIDATING STATEMENT OF FINANCIAL POSITION INFORMATION

AS OF DECEMBER 31, 2018

(Dollars in thousands)

	Obligated Group				Children's Hospital and Health System, Inc.	Children's Medical Group, Inc.	Children's Service Society of Wisconsin	Children's Community Health Plan, Inc.	Surgicenter of Greater Milwaukee, LLC	Eliminations	Consolidated
	Children's Hospital of Wisconsin, Inc.	Children's Hospital of Wisconsin Foundation, Inc.	Eliminations	Combined							
LIABILITIES AND NET ASSETS											
CURRENT LIABILITIES:											
Accounts payable	\$ 33,306	\$ 317	\$ -	\$ 33,623	\$ 7,954	\$ 2,987	\$ 619	\$ 3,525	\$ 333	\$ -	\$ 49,041
Intercompany payable	-	32,356	(32,356)	-	31,435	6,177	4,847	435	-	(42,894)	-
Accrued expenses:											
Salaries and benefits	38,422	281	-	38,703	6,259	4,112	1,049	644	90	-	50,857
Personal leave benefits	16,389	281	-	16,670	5,531	1,095	1,347	415	193	-	25,251
Interest	4,958	-	-	4,958	-	-	-	-	-	-	4,958
Estimated third-party payor settlements	1,145	-	-	1,145	-	-	-	-	-	-	1,145
Current installments of long-term debt	6,690	-	-	6,690	-	-	-	-	-	-	6,690
Claims payable and other current liabilities	863	-	-	863	863	877	743	82,642	188	(7,690)	78,486
Total current liabilities	101,773	33,235	(32,356)	102,652	52,042	15,248	8,605	87,661	804	(50,584)	216,428
OTHER LONG-TERM LIABILITIES	33,536	593	-	34,129	13,737	9,763	90	4	-	-	57,723
ACCRUED PENSION	34,765	-	-	34,765	-	-	2,522	-	-	-	37,287
LONG-TERM DEBT—Less current installments	351,906	-	-	351,906	-	-	-	-	-	-	351,906
Total liabilities	521,980	33,828	(32,356)	523,452	65,779	25,011	11,217	87,665	804	(50,584)	663,344
NET ASSETS:											
Without donor restrictions	975,422	553,911	(404,214)	1,125,119	-	35	(2,338)	74,364	27,129	(14,396)	1,209,913
With donor restrictions											
Restricted by purpose	49,911	53,638	(49,911)	53,638	2,183	-	1,544	-	-	(3,727)	53,638
Restricted in perpetuity	173,462	174,533	(173,462)	174,533	277	-	794	-	-	(1,071)	174,533
Total net assets	223,373	228,171	(223,373)	228,171	2,460	-	2,338	-	-	(4,798)	228,171
Total net assets	1,198,795	782,082	(627,587)	1,353,290	2,460	35	-	74,364	27,129	(19,194)	1,438,084
TOTAL	\$ 1,720,775	\$ 815,910	\$ (659,943)	\$ 1,876,742	\$ 68,239	\$ 25,046	\$ 11,217	\$ 162,029	\$ 27,933	\$ (69,778)	\$ 2,101,428

See notes to supplementary consolidating information.

(Concluded)

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

**CONSOLIDATING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS WITHOUT DONOR RESTRICTIONS INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2018
(Dollars in thousands)**

	Obligated Group				Children's Hospital and Health System, Inc.	Children's Medical Group, Inc.	Children's Service Society of Wisconsin	Children's Community Health Plan, Inc.	Surgicenter of Greater Milwaukee, LLC	Eliminations	Consolidated
	Children's Hospital of Wisconsin, Inc.	Children's Hospital of Wisconsin Foundation, Inc.	Eliminations	Combined							
OPERATING REVENUE:											
Net patient service revenue	\$ 685,540	\$ -	\$ -	\$ 685,540	\$ 9,573	\$ 61,622	\$ 1,951	\$ 6	\$ 9,558	\$ (39,876)	\$ 728,374
Premium revenue and other capitated arrangements	-	-	-	-	2,981	-	-	458,427	-	-	461,408
Other	48,670	27,729	(6,763)	69,636	106,959	858	34,762	1,141	1,184	(112,266)	102,274
Total operating revenue	734,210	27,729	(6,763)	755,176	119,513	62,480	36,713	459,574	10,742	(152,142)	1,292,056
OPERATING EXPENSES:											
Salaries	201,117	3,511	-	204,628	72,779	40,780	20,526	7,589	2,381	-	348,683
Employee benefits	59,113	891	-	60,004	18,867	8,825	8,530	2,298	636	-	99,160
Medical supplies	76,349	1	-	76,350	378	11,479	2	1	1,920	(887)	89,243
Non-medical supplies and other	18,396	18,091	(6,763)	29,724	7,604	1,265	2,522	1,009	227	(10,558)	31,793
Net medical claims expenses	-	-	-	-	(30)	-	-	375,822	-	(39,876)	335,916
Purchased services and professional fees	137,229	2,981	-	140,210	42,771	4,827	6,355	36,950	1,913	(99,385)	133,641
Operation and maintenance of facilities	23,174	33	-	23,207	7,507	6,536	2,259	403	957	(1,436)	39,433
Medical College of Wisconsin and resident fees	52,953	-	-	52,953	1,359	724	-	482	-	-	55,518
Provider tax	10,751	-	-	10,751	-	-	-	-	-	-	10,751
Depreciation	56,336	68	-	56,404	3,155	2,083	544	119	873	-	63,178
Interest	12,807	-	-	12,807	-	-	-	-	-	-	12,807
Total operating expenses	648,225	25,576	(6,763)	667,038	154,390	76,519	40,738	424,673	8,907	(152,142)	1,220,123
OPERATING INCOME (EXPENSE)	85,985	2,153	-	88,138	(34,877)	(14,039)	(4,025)	34,901	1,835	-	71,933
NONOPERATING INCOME (EXPENSES):											
Investment income	6,858	44,410	-	51,268	-	-	6	635	320	-	52,229
Change in net unrealized gains and losses on investments	(2,126)	(78,556)	-	(80,682)	-	-	-	6	(345)	-	(81,021)
Other	(167)	-	-	(167)	283	(75)	-	(2,809)	-	-	(2,768)
Net nonoperating income (expenses)	4,565	(34,146)	-	(29,581)	283	(75)	6	(2,168)	(25)	-	(31,560)
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	90,550	(31,993)	-	58,557	(34,594)	(14,114)	(4,019)	32,733	1,810	-	40,373
INCREASE (DECREASE) IN BENEFICIAL INTEREST IN NET ASSETS WITHOUT DONOR RESTRICTIONS OF CHILDREN'S HOSPITAL OF WISCONSIN FOUNDATION, INC.	6,621	-	(6,621)	-	-	-	-	-	-	-	-
TRANSFERS (TO) FROM AFFILIATED ORGANIZATIONS	(76,953)	26,000	-	(50,953)	34,436	14,135	2,382	-	-	-	-
NET ASSETS RELEASED FROM RESTRICTIONS—Capital acquisitions	1,648	-	-	1,648	58	-	-	-	-	-	1,706
PENSION-RELATED CHANGES OTHER THAN NET PERIODIC PENSION COST	(4,114)	-	-	(4,114)	-	-	(119)	-	-	-	(4,233)
INCREASE (DECREASE) IN NET ASSETS WITHOUT DONOR RESTRICTIONS	\$ 17,752	\$ (5,993)	\$ (6,621)	\$ 5,138	\$ (100)	\$ 21	\$ (1,756)	\$ 32,733	\$ 1,810	\$ -	\$ 37,846

See notes to supplementary consolidating information.

CHILDREN'S HOSPITAL AND HEALTH SYSTEM, INC., AND AFFILIATES

NOTE TO SUPPLEMENTARY CONSOLIDATING INFORMATION AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2018 (Dollars in thousands)

OBLIGATED GROUP AND BASIS OF REPORTING

Obligated Group—Children's Hospital of Wisconsin, Inc., and Children's Hospital of Wisconsin Foundation, Inc., are the only members of the obligated group (the "Obligated Group") for purposes of the issuance of bonds through the Wisconsin Health and Educational Facilities Authority.

Basis of Reporting—In accordance with financial statement presentation under the bond agreements, the consolidating statement of financial position information and consolidating statement of operations and changes in net assets without donor restrictions information as of and for the year ended December 31, 2018, exclude the effects of consolidating subsidiaries controlled by members of the Obligated Group and the effects of recording the beneficial interest in the net assets held by certain affiliated entities on behalf of members of the Obligated Group.

Parent-Only Financial Statements—The primary financial statements of Children's Hospital and Health System, Inc., are the consolidated financial statements. The amounts reflected in the supplementary consolidating information for Children's Hospital and Health System, Inc., are the financial position and operations of only the parent corporation and do not reflect the parent's interest in controlled entities.

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