Combined Financial Statements

Memorial Sloan Kettering Cancer Center
and Affiliated Corporations
Years Ended December 31, 2018 and 2017
With Report of Independent Auditors

Ernst & Young LLP

Building a better
working world

Memorial Sloan Kettering Cancer Center
and Affiliated Corporations

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Years Ended December 31, 2018 and 2017

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Report of Independent Auditors

Board of Managers
Memorial Sloan Kettering Cancer Center
and Affiliated Corporations

We have audited the accompanying combined financial statements of Memorial Sloan Kettering Cancer Center and Affiliated Corporations (the Institution), which comprise the combined balance sheets as of December 31, 2018 and 2017, and the related combined statements of activities without donor restrictions, changes in net assets, and cash flows for the years then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of MSK Insurance US, Inc., a wholly owned subsidiary, which statements reflect total assets constituting 2.4% in 2018 and 2.6% in 2017, total liabilities constituting 6.8% in 2018 and 2017, and total revenues constituting 0.2% in 2018 and 0.1% in 2017 of the related combined totals. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for MSK Insurance US, Inc., is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

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

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

Opinion

In our opinion, based on our audits and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the combined financial position of the Institution at December 31, 2018 and 2017, and the combined results of its operations, changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Adoption of ASU No. 2014-09, *Revenue from Contracts with Customers*, and ASU No. 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities*

As discussed in Note 1 to the combined financial statements, Memorial Sloan Kettering Cancer Center changed its method of revenue recognition as a result of the adoption of the amendments to the FASB Accounting Standards Codification resulting from Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers*, effective January 1, 2018 and adopted the amendments to the FASB Accounting Standards Codification resulting from Accounting Standards Update No. 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities*, effective December 31, 2018. Our opinion is not modified with respect to these matters.

Ernst & Young LLP

April 5, 2019

Memorial Sloan Kettering Cancer Center
and Affiliated Corporations

Combined Balance Sheets

	December 31 2018	2017
	(In Thousands)	
Assets		
Current assets:		
Cash and cash equivalents	**$ 677,079**	$ 900,411
Short-term investments – at fair value	**89,184**	239,472
Accounts receivable, net	**615,885**	497,547
Pledges, trusts and estates receivable	**170,148**	170,567
Other current assets	**121,078**	129,786
Total current assets	**1,673,374**	1,937,783
Noncurrent assets:		
Assets whose use is limited:		
Investments in marketable securities – at fair value:		
Construction, debt service and repair reserve funds	**149,799**	212,581
Captive insurance funds	**59,572**	54,770
Employee benefit funds	**80,068**	83,846
Total investments in marketable securities whose use is limited	**289,439**	351,197
Investments – at fair value	**3,343,092**	3,149,107
Investments internally designated for major capital projects	**609,377**	867,658
Investments in nonmarketable securities	**–**	11,900
Property and equipment – net	**4,284,338**	3,855,532
Pledges, trusts and estates receivable	**321,621**	361,550
Other noncurrent assets	**102,326**	101,285
Total noncurrent assets	**8,950,193**	8,698,229
Total assets	**$ 10,623,567**	$ 10,636,012
Liabilities and net assets		
Current liabilities:		
Accounts payable	**$ 580,598**	$ 489,603
Accrued expenses	**414,405**	387,955
Current portion of long-term debt	**52,771**	73,344
Total current liabilities	**1,047,774**	950,902
Noncurrent liabilities:		
Long-term debt, less current portion	**2,348,600**	2,715,704
Other noncurrent liabilities	**799,780**	864,303
Total liabilities	**4,196,154**	4,530,909
Net assets:		
Without donor restrictions:		
Undesignated	**4,608,791**	4,437,167
Board-designated	**420,860**	193,807
Total without donor restrictions	**5,029,651**	4,630,974
With donor restrictions	**1,397,762**	1,474,129
Total net assets	**6,427,413**	6,105,103
Total liabilities and net assets	**$ 10,623,567**	$ 10,636,012

See notes to combined financial statements.

Memorial Sloan Kettering Cancer Center
and Affiliated Corporations

Combined Statements of Activities Without Donor Restrictions

	Year Ended December 31	
	2018	**2017**
	(In Thousands)	
Undesignated operating revenues		
Hospital care and services	**$ 3,973,778**	$ 3,536,976
Grants and contracts	**334,536**	296,493
Contributions	**168,226**	191,843
Net assets released from restrictions	**122,701**	86,800
Royalty and other income	**159,140**	159,458
Investment returns allocated to operations	**151,473**	137,750
Total operating revenues	**4,909,854**	4,409,320
Operating expenses		
Compensation and fringe benefits	**2,587,336**	2,335,132
Purchased supplies and services	**1,756,174**	1,501,935
Depreciation and amortization	**300,239**	287,145
Interest	**47,045**	45,343
Total operating expenses	**4,690,794**	4,169,555
Income from operations	**219,060**	239,765
Nonoperating income and expenses, net		
Net assets released from restrictions for capital purposes	**25,000**	15,000
Investment returns, net of expenses, allocation to operations and amounts recorded in net assets with donor restrictions	**(112,061)**	219,440
Pension settlement cost	**(40,414)**	(33,480)
Other nonoperating income and expenses, net	**(34,927)**	(53,581)
Total nonoperating income and expenses, net	**(162,402)**	147,379
Change in postretirement benefit obligation to be recognized in future periods	**114,966**	(120,481)
Increase in undesignated net assets	**171,624**	266,663
Board-designated		
Board-designated philanthropy	**114,132**	–
Board-designated investment return	**30,626**	3,004
Board-designated other additions	**82,295**	15,000
Increase in Board-designated net assets	**227,053**	18,004
Increase in net assets without donor restrictions	**$ 398,677**	$ 284,667

See notes to combined financial statements.

Memorial Sloan Kettering Cancer Center
and Affiliated Corporations

Combined Statements of Changes in Net Assets

Years Ended December 31, 2018 and 2017

	Total Without Donor Restrictions	With Donor Restrictions: Time Restricted	Purpose Restricted	Endowments	Total With Donor Restrictions	Total Net Assets
	(In Thousands)					
Net assets at January 1, 2017	$ 4,346,307	$ 737,725	$ 20,000	$ 626,945	$ 1,384,670	$ 5,730,977
Increase in net assets without donor restrictions	284,667	–	–	–	–	284,667
Contributions, pledges, and bequests	–	81,741	7,000	37,800	126,541	126,541
Investment return on endowments	–	77,887	–	10,504	88,391	88,391
Impairment of investment	–	(23,673)	–	–	(23,673)	(23,673)
Net assets released from restrictions	–	(101,800)	–	–	(101,800)	(101,800)
Net assets at December 31, 2017	4,630,974	771,880	27,000	675,249	1,474,129	6,105,103
Increase in net assets without donor restrictions	**398,677**	**–**	**–**	**–**	**–**	**398,677**
Contributions, pledges, and bequests	**–**	**73,053**	**2,243**	**25,687**	**100,983**	**100,983**
Investment return on endowments	**–**	**(31,020)**	**–**	**1,371**	**(29,649)**	**(29,649)**
Net assets released from restrictions	**–**	**(147,701)**	**–**	**–**	**(147,701)**	**(147,701)**
Transfers to purpose restricted	**–**	**(4,249)**	**4,249**	**–**	**–**	**–**
Net assets at December 31, 2018	**$ 5,029,651**	**$ 661,963**	**$ 33,492**	**$ 702,307**	**$ 1,397,762**	**$ 6,427,413**

See notes to combined financial statements.

Memorial Sloan Kettering Cancer Center and Affiliated Corporations

Combined Statements of Cash Flows

	Year Ended December 31	
	2018	**2017**
	(In Thousands)	
Operating activities		
Change in net assets	**$ 322,310**	$ 374,126
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	**300,239**	287,145
Equity in earnings of investments, net	**707**	545
Unrealized net losses (gains)	**189,477**	(251,283)
Realized net gains	**(172,297)**	(165,244)
(Amortization) accretion of bond premium and issuance costs	**(5,799)**	37,132
Donor restricted contributions, pledges and bequests transferred to investing activities	**(100,983)**	(126,541)
Pension settlement cost	**40,414**	33,480
Change in postretirement benefit obligation to be recognized in future periods	**(114,966)**	120,481
Changes in assets:		
Accounts receivable, net	**(118,338)**	1,737
Pledges, trusts and estates receivable	**40,348**	18,571
Other current assets	**8,708**	(17,700)
Other noncurrent assets	**(1,748)**	(18,842)
Changes in liabilities:		
Accounts payable and accrued expenses	**89,475**	103,083
Other noncurrent liabilities	**9,781**	(105,106)
Net cash provided by operating activities	**487,328**	291,584
Investing activities		
Net acquisitions of property and equipment	**(700,827)**	(737,965)
Decrease in investments, net	**271,062**	385,419
Donor restricted contributions, pledges and bequests transferred from operating activities	**100,983**	126,541
Net cash used in investing activities	**(328,782)**	(226,005)
Financing activities		
Proceeds from financing	**–**	294,420
Repayment of debt	**(381,878)**	(158,460)
Net cash (used in) provided by financing activities	**(381,878)**	135,960
Net change in cash and cash equivalents	**(223,332)**	201,539
Cash and cash equivalents at beginning of year	**900,411**	698,872
Cash and cash equivalents at end of year	**$ 677,079**	$ 900,411

See notes to combined financial statements.

1. Organization and Significant Accounting Policies

The mission of Memorial Sloan Kettering Cancer Center and Affiliated Corporations is to provide leadership in the prevention, treatment and cure of cancer through excellence, vision and cost effectiveness in patient care, outreach programs, research and education. The accompanying financial statements are presented on a combined basis and include the accounts of the following tax exempt, Section 501(c)(3), incorporated affiliates: Memorial Sloan Kettering Cancer Center (the Center), Memorial Hospital for Cancer and Allied Diseases (the Hospital), Sloan Kettering Institute for Cancer Research (the Institute), S.K.I. Realty, Inc., MSK Insurance US, Inc. (MSKI), the Louis V. Gerstner Jr. Graduate School of Biomedical Sciences, Prostate Cancer Clinical Trials Consortium, LLC, Ralph Lauren Center for Cancer Care and Prevention, and MSK Proton, Inc. All of these entities are collectively referred to as the “Institution”.

The following is a summary of the Institution’s significant accounting policies:

Cash and Cash Equivalents

The Institution considers as cash and cash equivalents, all current investments, cash and certain highly liquid investments with original maturities of less than three months.

Investments

Investments in marketable securities are carried at fair value, based on quoted market prices.

Alternative investments are stated in the accompanying combined balance sheets at fair value, which is estimated using the net asset values (NAV), a practical expedient, of each alternative investment. Financial information used by the Institution to evaluate its alternative investments is provided by the investment manager or general partner and may include fair value valuations (quoted market prices and values determined through other means) of underlying securities and other financial instruments held by the investee, and estimates that require varying degrees of judgment. The financial statements of the investee companies are audited annually by independent auditors, although the timing for reporting the results of such audits does not always coincide with the Institution’s annual financial statement reporting.

1. Organization and Significant Accounting Policies (continued)

Realized gains or losses on investments sold or redeemed, together with unrealized appreciation or depreciation on investments and investment income, are distributed to all categories of net assets, as appropriate. The total investment return (investment income and realized and unrealized gains and losses) is reflected in the accompanying combined statements of activities without donor restrictions in two portions. The investment return allocated to operating revenues is determined by application of a 4% normal return to a three-year average market value of investments, excluding certain endowment assets and certain other funds. In addition, actual investment earnings on short-term fixed income funds are included in investment returns allocated to operations. The investment return classified as nonoperating represents the difference between the actual total investment return and the amount allocated to operating revenues less amounts recorded in net assets with donor restrictions for endowments. Investment expenses, other than fees paid directly to investment managers, amounted to $8.1 million and $8.4 million in 2018 and 2017, respectively, and are included in the combined statements of activities without donor restrictions in investment returns, net of expenses, allocation to operations and amounts recorded in net assets with donor restrictions.

Investment returns, net of investment expenses, consist of the following:

	2018	**2017**
	(In Thousands)	
Investment income	**$ 54,900**	$ 8,385
Realized gains	**172,297**	165,244
Unrealized (losses) gains	**(189,477)**	251,283
Total	**$ 37,720**	$ 424,912

1. Organization and Significant Accounting Policies (continued)

Grants and Contracts Revenues

Grants and contracts revenues represent reimbursements of costs incurred in direct support of research and other sponsored activities related to the prevention and treatment of cancer. The Institution contracts with federal, state, and private agencies which are recorded as conditional contributions for approximately $209.0 million and $199.1 million for 2018 and 2017, respectively. The Institution records conditional contribution revenue upon performance of the conditions stated in the contracts. Additionally, the Institution contracts with industry sponsors which are recorded as exchange transactions for approximately $125.5 million and $97.4 million for 2018 and 2017, respectively. Exchange transactions are recognized as revenue at the amount that reflects the consideration to which the Institution expects to be entitled in exchange for performance under the contract.

Contributions and Unconditional Promises to Give

Contributions represent the utilization of donor funds which are intended to support the current period's operations. Contributions of cash and other assets are reported at fair value at the date the assets are received. Unconditional promises to give are recorded at fair value when the gift intent is made known in writing. A receivable has been established and net assets with donor restrictions have been increased by the time-discounted value of the promises. Irrevocable trusts are recorded at the point of notification and are recorded as net assets with donor restrictions as determined by the trust instruments. Estates are estimated and recorded at the conclusion of probate.

Total contributions, pledges, trusts and estates raised through fund raising efforts were approximately $383.4 million and $318.4 million for 2018 and 2017, respectively.

1. Organization and Significant Accounting Policies (continued)

The Institution is aware of numerous unconditional promises to give and estimates the year of receipt to the extent possible. The anticipated present value of the receivable is as follows (in thousands):

2019	$ 170,148
2020	86,721
2021	58,188
2022	41,973
2023	34,741
Thereafter	99,998
	$ 491,769

The present value discount and allowance for doubtful accounts on unconditional promises to give is approximately $50.8 million and $56.5 million at December 31, 2018 and 2017, respectively.

Net Assets Without Donor Restrictions

Net assets that are not subject to donor-imposed restrictions may be expended for any purpose in fulfilling the Institution's mission. These net assets may be used at the discretion of the Institution's management and Board of Managers (the Board).

The Institution's governing Board, through specific action, has created self-imposed limits on certain net assets without donor restrictions. As of December 31, 2018 and 2017, funds have been established for $420.8 million and $193.8 million, respectively, to support various strategic initiatives. All board-designated net assets function as endowments and follow the Institution's policy of appropriating for spending an annualized percentage of each funds' value. However, unlike endowments, all board-designated net assets are available for general expenditures with Board approval and will not accumulate investment returns in excess or deficit of the spending rate.

1. Organization and Significant Accounting Policies (continued)

Net Assets With Donor Restrictions

Gifts are reported as net assets with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. Some donor restrictions are temporary in nature; those restrictions will be met by the actions of the Institution, or by the passage of time. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity. When a donor restriction expires, that is, when a stipulated time restriction ends or a purpose restriction is accomplished, net assets are reclassified as net assets without donor restrictions and reported in the combined financial statements as net assets released from restrictions or as net assets released from restrictions for capital purposes. Donor restricted contributions whose restrictions are met within the same year as received are reflected as contributions in the accompanying combined statements of activities without donor restrictions.

Gifts that have been restricted by donors to be maintained by the Institution in perpetuity are reflected in the accompanying combined statements of changes in net assets as endowments within the net assets with donor restrictions.

The Institution follows the New York Prudent Management of Institutional Funds Act (NYPMIFA) which was enacted on September 17, 2010. The Institution has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while maintaining the historic dollar value of endowment contributions. The Institution classifies as endowments (a) the original value of the gifts donated, (b) the original value of subsequent gifts, (c) the net realizable value of future payments in accordance with the donor's gift instrument (outstanding pledges, net of applicable discount) and (d) appreciation (depreciation), gains (losses) and income earned on the fund when the donor states that such increases or decreases are to be treated as changes in endowments. The endowment assets are pooled with assets without donor restrictions and invested in various diversified asset classes.

The Institution has a policy of appropriating for spending an annualized percentage of each endowment fund's value, with certain exceptions. In establishing this policy, the Institution considered the long-term expected return on its investment portfolio and the impact of inflation. The spending rate appropriated by the Institution was 4% in 2018 and 2017.

The Institution's endowment investment returns in excess or deficit of the spending rate will be accumulated and added to the endowment fund's value in order to calculate the appropriation for spending.

1. Organization and Significant Accounting Policies (continued)

To satisfy its long-term rate-of-return objectives, the Institution relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Institution targets a diversified asset allocation (see Note 4) to achieve its long-term return objectives within prudent risk constraints. As a result of fluctuations in the investment markets, from time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor requires the Institution to retain as a fund of perpetual duration. There were no deficiencies of this nature as of December 31, 2018 and 2017.

Changes in donor endowment funds for the years ended December 31, 2018 and 2017 consisted of the following:

	Without Donor Restrictions	**Time Restricted**	**Endowments**
	(In Thousands)		
Balance at December 31, 2017	**$ –**	**$ 279,210**	**$ 675,249**
Investment return on endowments	**49,354**	**(31,020)**	**1,371**
Contributions	**–**	**–**	**25,687**
Appropriations	**(49,354)**	**–**	**–**
Balance at December 31, 2018	**$ –**	**$ 248,120**	**$ 702,307**

	Without Donor Restrictions	**Time Restricted**	**Endowments**
	(In Thousands)		
Balance at January 1, 2017	$ –	$ 201,323	$ 626,945
Investment return on endowments	47,972	77,887	10,504
Contributions	–	–	37,800
Appropriations	(47,972)	–	–
Balance at December 31, 2017	$ –	$ 279,210	$ 675,249

1. Organization and Significant Accounting Policies (continued)

Included in endowments are amounts that represent the Institution's beneficial interest in certain perpetual trusts which are held by third-party trustees. The underlying assets of the perpetual trusts are included in other noncurrent assets on the combined balance sheets and consist of equity securities and mutual funds. The fair value at December 31, 2018 and 2017 was approximately $19.6 million and $20.5 million, respectively. The change in fair value of the beneficial interest in perpetual trusts held by third parties is included in the change in net assets with donor restrictions.

Property and Equipment

Property and equipment is carried at cost, less accumulated depreciation and amortization. Depreciation on building components and equipment is computed on the straight-line method over the estimated useful service lives. Leasehold improvements are being amortized over the lesser of the term of the lease or estimated useful service life, based on the straight-line method.

The carrying amount of assets and the related accumulated depreciation or amortization are removed from the accounts when such assets are disposed of and any resulting gain or loss is included in operations.

All eligible costs incurred for the development of computer software for internal use are capitalized and carried at cost, less accumulated amortization. Amortization of capitalized internal use software cost is based on the straight-line method over the estimated useful life of the software.

Use of Estimates

The preparation of the combined financial statements in conformity with U.S. generally accepted accounting principles requires management to make prudent and conservative estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the combined financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

1. Organization and Significant Accounting Policies (continued)

Tax Status

The entities comprising the Institution are Section 501(c)(3) organizations exempt from Federal income taxes under Section 501(a) of the Internal Revenue Code. The entities are also exempt from New York State and City income taxes.

The Tax Cuts and Jobs Act (TCJA) was enacted on December 22, 2017. For tax-exempt entities, TCJA requires organizations to categorize certain fringe benefit expenses as a source of unrelated business income subject to tax, pay an excise tax on compensation above certain thresholds, and record income or losses for tax determination purposes from unrelated business activities on an activity-by-activity basis, among other provisions. Regulations necessary to implement certain aspects of TCJA are expected to be promulgated by the Internal Revenue Service (IRS) in 2019. As of and for the year ended December 31, 2018, the Institution has made reasonable estimates of the provision for income taxes, the compensation excise tax, and the effects on existing deferred tax balances based on accounting guidance included in Accounting Standards Codification 740, *Income Taxes*. The Institution will continue to refine its calculations in future periods as additional regulations and guidance are issued by the IRS.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The provisions of ASU 2014-09 became effective for the Institution for annual reporting periods beginning after December 15, 2017. The Institution adopted ASU 2014-09 effective January 1, 2018 for its combined financial statements as of and for the years ended December 31, 2018 and 2017, following the full retrospective method of application. As a result of implementing ASU 2014-09, certain patient activity where collection is uncertain (representing approximately $35.1 million and $43.5 million for the years ended December 31, 2018 and 2017, respectively) previously reported within the provision for bad debts and regulatory assessments in the Institution's combined statements of activities without donor restrictions, no longer meets the criteria for revenue recognition and, accordingly, the provision for bad debts and regulatory assessments after the adoption date is significantly reduced, with a

1. Organization and Significant Accounting Policies (continued)

corresponding reduction to hospital care and services revenue. Such patient activity is now classified as an implicit price concession (see Note 3). Additionally, regulatory assessments and bad debt expenses arising from adverse changes in a party's ability to pay have been included within purchased supplies and services (representing approximately $12.2 million and $10.8 million for the years ended December 31, 2018 and 2017, respectively) in the combined statements of activities without donor restrictions. Other aspects of the Institution's implementation of ASU 2014-09 impacting hospital care and services revenue, which include judgments regarding collection analyses and estimates of variable consideration and the addition of certain qualitative and quantitative disclosures, are reflected in Note 3. The adoption of ASU 2014-09 in relation to other applicable revenue activity did not have a material impact to the Institution's accompanying combined financial statements.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for Profit Entities*, which eliminates the requirement for not-for-profits (NFPs) to classify net assets as unrestricted, temporarily restricted and permanently restricted. Instead, NFPs are required to classify net assets as net assets with donor restrictions or without donor restrictions. Among other things, the guidance also modifies required disclosures and reporting related to net assets, investment expenses and qualitative information regarding liquidity. NFPs are also required to report all expenses by both functional and natural classification in one location. The provisions of ASU 2016-14 are effective for the Institution for annual periods beginning after December 15, 2017 and interim periods thereafter. As such, the Institution adopted ASU 2016-14 for the year ended December 31, 2018. The effects of the adoption of ASU 2016-14 were applied retrospectively. As a result of the adoption of ASU 2016-14, the net asset categories have been updated as described above. Additionally, the addition of quantitative and qualitative disclosures related to the analysis of expenses by both natural and functional classifications and liquidity and availability of resources can be found in Notes 4 and 14. The adoption of ASU 2016-14 had no impact on the total net assets previously reported by the Institution as of December 31, 2017.

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* (ASU 2018-08). ASU 2018-08 clarifies existing guidance in order to address diversity in practice in classifying grants (including governmental grants) and contracts received by not-for-profit entities, and requires entities to evaluate whether the resource provider receives commensurate value. In addition, the standard clarifies the guidance on how entities determine when a contribution is conditional, including whether the agreement includes a barrier (or barriers) that must be overcome for the recipient to be entitled to the transferred assets and a right of return of the transferred assets

1. Organization and Significant Accounting Policies (continued)

(or a right of release of the promisor's obligation to transfer the assets). The standard should be applied on a modified prospective basis to agreements that are not completed as of the effective date and to agreements entered into after the effective date. Retrospective application is permitted. The Institution early adopted ASU 2018-08 in the combined financial statements for the year ended December 31, 2018 on a modified prospective basis without significant impact to its combined financial statements.

In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*, which addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. This guidance allows an entity to choose, investment-by-investment, to report an equity investment that neither has a readily determinable fair value, nor qualifies for the practical expedient for fair value estimation using net asset value (NAV), at its cost minus impairment (if any), plus or minus changes resulting from observable price changes in orderly transactions for the identical or similar investment of the same issue. Impairment of such investments must be assessed qualitatively at each reporting period. Entities must disclose their financial assets and liabilities by measurement category and form of asset either on the face of the balance sheet or in the accompanying notes. The ASU is effective for annual reporting periods beginning after December 15, 2018 or for the year ended December 31, 2019 for the Institution. Early adoption is permitted for annual periods beginning after December 15, 2017. Additionally, immediate early application of certain provisions are permitted. The Institution early applied the provision to eliminate the requirement to disclose the fair value of debt during the year ended December 31, 2018.

In February 2016, the FASB ASU 2016-02, *Leases (Topic 842).* ASU 2016-02 requires the rights and obligations arising from the lease contracts, including existing and new arrangements, to be recognized as assets and liabilities on the balance sheets. ASU 2016-02 will require disclosures to help the financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. The recognition, measurement and presentation of expenses and cash flows arising from a lease will primarily depend on its classification as a finance or operating lease. ASU 2016-02 is effective for the Institution beginning January 1, 2019 and will be applied using a modified retrospective approach. The Institution is currently in the process of evaluating its lease contracts, as well as certain service contracts that may include embedded leases. Additionally, the Institution is finalizing its analysis of certain key assumptions that will be utilized at the transition date, including the incremental borrowing rate. The primary effect of the new standard will be to record right-of-use assets and obligations for current operating leases, which will have a material

1. Organization and Significant Accounting Policies (continued)

impact on the combined balance sheets and significant incremental disclosures in the notes to the combined financial statements. The transition adjustment is not expected to have a material impact on the combined statements of activities without donor restrictions.

Reclassifications

Certain reclassifications have been made to the 2017 amounts previously reported in order to conform to updated methodology utilized in the current year presentation. These reclassifications have no impact on the net assets previously reported.

2. Community Benefit Programs

Consistent with its mission, the Institution invests significant amounts for the benefit of the worldwide community that is served through its patient care, education and research activities. Listed below are quantifiable benefits provided.

Charity care represents the cost of services provided to patients who cannot afford health care services due to inadequate resources and/or are uninsured or underinsured. A patient is classified as a charity care patient in accordance with the Institution's established policies and where insufficient payment for such services is anticipated. For the periods presented, the Institution considers patients for charity care if household income is less than 500% of the federal poverty guidelines. Services provided as charity care are not reported as revenue in the combined statements of activities without donor restrictions. Costs of providing charity care are estimated by multiplying the total charges incurred by patients that qualify for charity care by a ratio of historical expenses to charges as derived from the Institution's accounting records. The Institution receives payments from the New York State Public Goods Pool for charity care and such amounts totaled approximately $11.3 million and $11.9 million for the years ended December 31, 2018 and 2017, respectively. Payments made into the pool by the Institution were approximately $9.9 million and $8.3 million for the years ended December 31, 2018 and 2017, respectively.

The Institution provides services to patients who participate in government-sponsored health programs, such as Medicare and Medicaid. Payments received by the Institution for patient services provided under these programs are less than the actual cost of providing such services. Therefore, to the extent Medicare and Medicaid payments are less than the cost of care provided, the uncompensated cost of that care is considered to be a community benefit.

2. Community Benefit Programs (continued)

Research community benefit costs represent the Institution's costs for basic, translational and clinical research.

The Institution is a preeminent provider of health training to health professionals who desire training in the skills necessary to treat cancer patients. The Institution trains physicians, radiology students, nursing students, social work students and individuals looking to create a career in the field of cancer research. The amounts shown below represent costs in excess of amounts reimbursed by third-party payors such as training grant revenues and direct medical education payments from the Medicare and Medicaid program.

The following is a summary of the Institution's estimated costs of providing community benefit program services:

	Year Ended December 31	
	2018	**2017**
	(In Thousands)	
Charity care	**$ 21,342**	$ 21,652
Unpaid cost of government sponsored health care	**490,085**	440,052
Research supported by governmental/voluntary agencies	**208,987**	193,933
Other research	**446,056**	422,518
Health training	**233,401**	224,158
Other	**21,664**	21,607
Community benefit programs	**$ 1,421,535**	$ 1,323,920

3. Hospital Care and Services Revenue

Hospital Care and Services Revenue and Accounts Receivable

Hospital care and services revenue is reported at the amount that reflects the consideration to which the Hospital expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others and includes variable consideration (reductions to revenue) in determining a transaction price.

3. Hospital Care and Services Revenue (continued)

The Hospital 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 historical collection trends and other analyses, the Hospital 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 Hospital's initial estimate of the transaction price for services provided to patients subject to revenue recognition is determined by reducing the total standard charges related to the patient services provided by various elements of variable consideration, including contractual allowances, discounts, implicit price concessions, and other reductions to the Hospital's standard charges. The Hospital determines the transaction price associated with services provided to patients who have third-party payor coverage on the basis of contractual or formula-driven rates for the services rendered (see description of third-party payor payment programs below). The estimates for contractual allowances and discounts are based on contractual agreements, the Hospital's discount policies and historical experience. For uninsured and under-insured patients who do not qualify for charity care, the Hospital determines the transaction price associated with services on the basis of charges reduced by implicit price concessions. Implicit price concessions included in the estimate of the transaction price are based on the Hospital's historical collection experience for applicable patient portfolios. Patients who meet the Hospital's criteria for charity care are provided care without charge; such amounts are not reported as revenue.

Generally, the Hospital bills patients and third-party payors several days after the services are performed and/or the patient is discharged. Hospital care and services revenue is recognized as performance obligations are satisfied. Performance obligations are determined based on the nature of the services provided by the Hospital. Hospital care and services revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total charges. The Hospital believes that this method provides a reasonable depiction of the transfer of services over the term of the performance obligation based on the services needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients receiving inpatient acute care services or patients receiving services in the Hospital's outpatient and ambulatory care centers. The Hospital measures the performance obligation from admission into the hospital or the commencement of an outpatient service to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge or the completion of the outpatient visit.

3. Hospital Care and Services Revenue (continued)

As substantially all of its performance obligations relate to contracts with a duration of less than one year, the Hospital has elected to apply the optional exemption provided in ASU 2014-09 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 for patients who remain admitted at that time (in-house patients). The performance obligations for in-house patients are generally completed when the patients are discharged, which for the majority of the Hospital's in-house patients occurs within days or weeks after the end of the reporting period.

Subsequent changes to the estimate of the transaction price (determined on a portfolio basis when applicable) are generally recorded as adjustments to patient service revenue in the period of the change (see third-party payment programs below). Portfolio collection estimates are updated monthly based on collection trends. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay (determined on a portfolio basis when applicable) are recorded as bad debt expense. Bad debt expense for the years ended December 31, 2018 and 2017 was not significant.

The Hospital has determined that the nature, amount, timing and uncertainty of revenue and cash flows are affected by the following factors: payors, lines of business and timing of when revenue is recognized. Tables providing details of these factors are presented below.

The percent of hospital care and services revenue for the years ended December 31, 2018 and 2017, by payor, is as follows:

	2018	**2017**
Medicare	**27%**	26%
Medicaid	**2**	3
Contracted managed care	**65**	63
Non-contracted managed care and self-pay	**6**	8
	100%	100%

3. Hospital Care and Services Revenue (continued)

Deductibles, copayments and coinsurance under third-party payment programs which are the patient's responsibility are included within the non-contracted managed care and self-pay category above.

The Hospital provides pharmaceuticals and related support services to patients through a retail and specialty pharmacy. Revenue is recognized at the point in time of the transaction.

Hospital care and services revenue for the years ended December 31, 2018 and 2017 by line of business is as follows (in thousands):

	2018	2017
Hospital	**$ 3,203,428**	$ 2,901,401
Physician services	**625,887**	563,661
Retail and specialty pharmacy	**144,463**	71,914
	$ 3,973,778	$ 3,536,976

The Hospital has elected the practical expedient allowed under ASU 2014-09 and does not adjust the expected amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Hospital's 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. However, the Hospital does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Third-Party Payment Programs

Settlements with third-party payors for cost report filings and retroactive adjustments due to ongoing and future audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor and the Hospital's historical settlement activity (for example, cost report final settlements or repayments related to recovery audits), including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized

3. Hospital Care and Services Revenue (continued)

will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Such estimates are determined through either a probability-weighted estimate or an estimate of the most likely amount, depending on the circumstances related to a given estimated settlement item. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available), or as years are settled or are no longer subject to such audits, reviews, and investigations.

Non-Medicare Reimbursement

In New York State, hospitals and all non-Medicare payors, except Medicaid, workers' compensation and no-fault insurance programs, negotiate hospitals' payment rates. If negotiated rates are not established, payors are billed at hospitals' established charges. Medicaid pays hospital rates promulgated by the New York State Department of Health. Payments to the Hospital for Medicaid inpatient services are based on a prospective payment system, with retroactive adjustments. Outpatient services are paid based on a statewide prospective system. Medicaid rate methodologies are subject to approval at the Federal level by the Centers for Medicare & Medicaid Services (CMS), which may routinely request information about such methodologies prior to approval. Revenue related to specific rate components that have not been approved by CMS are not recognized until the Hospital is reasonably assured that such amounts are realizable. Adjustments to the current and prior years' payment rates for those payors will continue to be made in future years.

Medicare Reimbursement

The Hospital is exempt from the national prospective payment system used to reimburse hospitals for inpatient services provided to Medicare beneficiaries and instead is paid using a cost-based methodology. These payments are subject to a limit that is based on costs from the mid 2000s for rate years beginning on or subsequent to January 1, 2007, which are then updated based on annual trend factors calculated by CMS. Prior to January 1, 2007, the limit was based on costs from the early 1990s. The Hospital is paid for outpatient services under the national prospective payment system and other methodologies of the Medicare program for certain other services. The outpatient payments are subject to a floor that ensures the Hospital receives a percentage of its Medicare defined allowable outpatient costs equal to all non-exempt hospitals reimbursed under the national prospective payment system. Federal regulations provide for certain adjustments to current and prior years' payment rates, based on hospital-specific data.

3. Hospital Care and Services Revenue (continued)

The Hospital has established estimates, based on information presently available, of amounts due to or from Medicare and non-Medicare payors for adjustments to current and prior years' payment rates. The current Medicaid, Medicare and other third-party payor programs are based upon extremely complex laws and regulations that are subject to interpretation. Medicare cost reports, which serve as the basis for final settlement with the Medicare program, have been audited by the Medicare fiscal intermediary and settled through the year ended December 31, 2013. Other years remain open for audit and subsequent settlement, as are numerous issues related to the New York State Medicaid program for prior years. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount when open years are settled, audits are completed and additional information is obtained. Changes in these estimates could also affect the amounts reported as the unpaid cost of government sponsored health care (see Note 2). Approximately 1.07% of operating revenues in 2018 and (0.16)% of operating revenues in 2017 are due to adjustments of prior year operating revenues. Additionally, noncompliance with such laws and regulations could result in fines, penalties and exclusion from such programs. The Hospital is not aware of any allegations of noncompliance that could have a material adverse effect on the combined financial statements and believes that it is in compliance with all applicable laws and regulations.

There are various Federal and State proposals that could, among other things, reduce payment rates or modify payment methods. The ultimate outcome of these proposals and other market changes, including the potential effects of health care reform by the Federal or State government, cannot presently be determined. Future changes in Medicare and Medicaid programs could have an impact, positive or negative, on the Hospital. Additionally, Medicare payment rates for various years have been appealed by the Hospital. If the appeals are successful, additional income applicable to those years might be realized.

Significant concentrations of accounts receivable at December 31, 2018 include 28% from government-related programs, 19% from Empire Health Choice and 15% from UnitedHealthcare (24%, 17% and 16%, respectively, at December 31, 2017).

4. Cash, Cash Equivalents, and Investments at Fair Value

For assets and liabilities required to be measured at fair value, the Institution measures fair value based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are applied based on the unit of account from the Institution's perspective. The unit of account determines what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated) for purposes of applying other accounting pronouncements.

The Institution follows a valuation hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

- *Level 1:* Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

- *Level 2:* Observable inputs are based on inputs not quoted in active markets, but corroborated by market data.

- *Level 3:* Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. In determining fair value, the Institution uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers nonperformance risk in its assessment of fair value. Any investments valued based upon the NAV are not subject to classification in the valuation hierarchy.

Mutual funds are valued based on the quoted market prices of the securities as reported on national securities exchanges.

United States-based and international equities consist of individually held securities and commingled funds. Individual securities and certain commingled funds are valued based on the quoted market prices of the securities as reported on national securities exchanges. Commingled funds primarily are valued based on the NAV of shares held by the Institution at year end.

4. Cash, Cash Equivalents, and Investments at Fair Value (continued)

Fixed income securities include corporate bonds, U.S. government securities, and commingled funds. Corporate bonds and U.S. government securities are valued based on readily available market quotations received from commercial pricing services. Such pricing services and brokers will generally provide bid-side quotations. Commingled funds are valued based on quoted market prices as reported on national securities exchanges, if applicable, or the NAV of shares held by the Institution at year end.

Alternative investments include absolute return funds, long/short funds, global macro funds, inflation hedging funds, opportunistic funds, hard assets, private equity funds and venture capital. Alternative investment interests generally are structured such that the Institution holds a limited partnership interest. The Institution's ownership structure does not provide for control over the related investees and the Institution's financial risk is limited to the funded and unfunded commitment for each investment. As of December 31, 2018, the Institution had outstanding commitments to provide additional capital of approximately $529.5 million to various alternative investment managers.

Individual investment holdings within the alternative investments include nonmarketable and market-traded debt and equity securities and interests in other alternative investments. The Institution may be exposed indirectly to securities lending, short sales of securities and trading in futures and forward contracts, options and other derivative products. Alternative investments often have liquidity restrictions under which the Institution's capital may be divested only at specified times. The Institution's liquidity restrictions range from several months to ten years for certain private equity investments. Liquidity restrictions may apply to all or portions of a particular invested amount.

There is uncertainty in determining fair values of alternative investments arising from factors such as lack of active markets (primary and secondary), lack of transparency into underlying holdings, time lags associated with reporting by the investee companies and the subjective evaluation of liquidity restrictions. As a result, the estimated fair values reported in the accompanying combined balance sheets might differ from the values that would have been used had a ready market for the alternative investment interests existed and there is at least a reasonable possibility that those estimates will change.

4. Cash, Cash Equivalents, and Investments at Fair Value (continued)

The following is a description of the Institution's valuation methodologies for assets measured at fair value. Fair value for Level 1 is based upon quoted market prices. Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Fair value for Level 3 is based on unobservable inputs when little or no market data is available, which include estimates and risk-adjusted value ranges. Inputs are obtained from various sources, including market participants, dealers and brokers. The methods described above may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Institution believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

4. Cash, Cash Equivalents, and Investments at Fair Value (continued)

Financial instruments, other than pension plan assets (see Note 8), carried at fair value as of December 31, 2018, are classified in the table below as described above:

	Level 1	Level 2	Level 3	Total
	(In Thousands)			
Investments measured at fair value				
Cash, cash equivalents, and short-term investments	$ 895,346	$ –	$ –	$ 895,346
Mutual funds	80,068	–	–	80,068
United States-based equity securities	92,680	204,757	–	297,437
International equity securities	285,381	9,585	–	294,966
Fixed income investments:				
Corporate bonds	–	609,480	–	609,480
U.S. government and other	150,707	68,084	–	218,791
	$ 1,504,182	$ 891,906	$ –	2,396,088
Investments measured at NAV as a practical expedient				
Commingled funds:				
United States-based equity				211,618
International equity				270,031
Alternative investments:				
Marketable:				
Absolute return funds				282,402
Long/short funds				609,691
Global macro funds				216,583
Inflation hedging funds				43,768
Nonmarketable:				
Venture capital				474,313
Private equity				224,717
Opportunistic funds				131,297
Hard assets				147,663
Total investments at fair value				$ 5,008,171

4. Cash, Cash Equivalents, and Investments at Fair Value (continued)

Financial instruments, other than pension plan assets (see Note 8), carried at fair value as of December 31, 2017, are classified in the table below as described above:

	Level 1	Level 2	Level 3	Total
	(In Thousands)			
Investments measured at fair value				
Cash, cash equivalents, and short-term investments	$ 1,588,348	$ –	$ –	$ 1,588,348
Mutual funds	83,846	–	–	83,846
United States-based equity securities	40,256	244,803	–	285,059
International equity securities	220,744	11,261	–	232,005
Fixed income investments:				
Corporate bonds	–	554,541	–	554,541
U.S. government and other	201,295	64,825	–	266,120
	$ 2,134,489	$ 875,430	$ –	3,009,919
Investments measured at NAV as a practical expedient				
Commingled funds:				
United States-based equity				239,488
International equity				242,905
Alternative investments:				
Marketable:				
Absolute return funds				327,030
Long/short funds				569,650
Global macro funds				201,228
Inflation hedging funds				72,785
Nonmarketable:				
Venture capital				343,531
Private equity				206,402
Opportunistic funds				143,002
Hard assets				151,905
Total investments at fair value				$ 5,507,845

Other financial instruments that are not required to be carried at fair value include debt, pledges and mortgages receivable. Debt, pledges and mortgages receivable are recorded at carrying value, net of applicable discounts in the accompanying combined balance sheets which approximates fair value.

4. Cash, Cash Equivalents, and Investments at Fair Value (continued)

As part of the Institution's liquidity management, it has a practice to structure its financial assets to be available for its operating and capital needs. Working capital requirements are held in cash and cash equivalents and short-term investments. Accounts receivable, net and the current portion of pledges, trusts and estates receivable on the combined balance sheets represent amounts expected to be collected within one year. Investments internally designated for major capital projects represent assets set aside for capital expenditures, but could be made available immediately if necessary. Additionally, to help manage unanticipated liquidity needs, the Institution has committed lines of credit which it could draw upon.

Additionally, the Institution invests in a diversified long-term investment portfolio (the Unified Pool). Although the Institution does not intend to spend from the Unified Pool other than amounts appropriated for spending as part of its annual budget approval and appropriation process discussed in Note 1, amounts from the Unified Pool could be made available if necessary. However, the Unified Pool contains investments with lock-up provisions that would reduce the total investments that could be made available.

The following represents assets that could be made available within one year:

	December 31 2018	December 31 2017
	(*In Thousands*)	
Cash and cash equivalents	**$ 677,079**	$ 900,411
Short-term investments – at fair value	**89,184**	239,472
Accounts receivable, net	**615,885**	497,547
Pledges, trusts and estates receivable, current portion	**170,148**	170,567
Investments internally designated for major capital projects	**609,377**	867,658
Investments – at fair value	**2,205,490**	2,238,060
Undrawn lines of credit	**250,000**	300,000
	$ 4,617,163	$ 5,213,715

5. Property and Equipment

Property and equipment consists of the following:

	December 31	
	2018	**2017**
	(In Thousands)	
Land	**$ 380,703**	$ 380,703
Buildings and leasehold improvements	**3,962,458**	3,754,578
Equipment	**1,720,147**	1,563,597
Construction-in-progress	**1,411,505**	1,058,869
	7,474,813	6,757,747
Less accumulated depreciation and amortization	**3,190,475**	2,902,215
	$ 4,284,338	$ 3,855,532

The Institution disposed of approximately $16.3 million and $27.4 million of fully depreciated assets in 2018 and 2017, respectively.

6. Long-Term Debt

Long-term debt consists of the following:

	December 31 2018	2017
	(In Thousands)	
DASNY Series 1998, tax-exempt bonds maturing through 2023 at various fixed interest rates ranging from 5.50% to 5.75%	**$ 122,900**	$ 135,400
DASNY Series 2008, tax-exempt bonds maturing through 2036 at various fixed interest rates ranging from 4.00% to 5.00%	**–**	333,730
DASNY Series 2010, tax-exempt bonds maturing through 2023 at a fixed interest rate of 2.18%	**38,000**	46,000
Series 2011A taxable bonds maturing in 2042 at a fixed interest rate of 5.00%	**400,000**	400,000
DASNY Series 2012, tax-exempt bonds maturing through 2041 at various fixed interest rates ranging from 3.00% to 5.00%	**80,380**	82,350
DASNY 2012 Series 1, tax-exempt bonds maturing through 2034 at various fixed interest rates ranging from 4.00% to 5.00%	**262,265**	262,265
Series 2012A taxable bonds maturing in 2052 at a fixed interest rate of 4.125%	**400,000**	400,000
Series 2015A taxable bonds maturing in 2055 at a fixed interest rate of 4.20%	**550,000**	550,000
DASNY Series 2016-1, tax-exempt bonds repaid through 2028 at a fixed interest rate of 1.97%	**102,389**	105,944
NJEDA Series 2016-2, tax-exempt bonds maturing through 2026 at a fixed rate interest rate of 1.43%	**112,375**	130,500
DASNY Series 2017-1, tax-exempt bonds maturing through 2047 at various fixed interest rates ranging from 4.00% to 5.00%	**290,420**	294,420
Unamortized bond premiums, discounts and issuance costs	**42,642**	48,439
	2,401,371	2,789,048
Less current portion	**52,771**	73,344
	$ 2,348,600	$ 2,715,704

In July 2018, the Institution redeemed the remaining balance of the outstanding Dormitory Authority of the State of New York (DASNY) Series 2008 tax-exempt bonds for approximately $333.7 million.

6. Long-Term Debt (continued)

In December 2017, the Institution issued $294.4 million of Series 2017-1 tax-exempt bonds (the 2017 Bonds) through the DASNY. The 2017 Bonds mature between 2018 and 2047 at fixed interest rates ranging from 4.00% to 5.00%. A portion of the proceeds were used to advance refund the DASNY 2015 Series 1 tax-exempt bonds. The remaining proceeds will be used to pay costs for ambulatory care expansion, equipment and to pay for costs of issuance of the 2017 Bonds. The new debt was issued at a premium of approximately $41.1 million, which lowered the Institution's effective interest rates and the all-in yield.

Annual maturities on all long-term debt as of December 31, 2018 for the years 2019 through 2023 are as follows (in thousands):

2019	$ 52,771
2020	78,823
2021	80,198
2022	83,234
2023	88,951

Total interest paid in 2018 and 2017 (including portions supporting capitalized costs) was approximately $105.2 million and $104.1 million, respectively. Interest expense related to the Series 2011A, the Series 2012A and the 2015 Bonds will be included in other nonoperating income and expenses, net until the related capital projects are placed into service. Nonoperating interest expense was approximately $18.2 million and $30.2 million during 2018 and 2017, respectively. The Institution capitalized interest of approximately $40.4 million and $29.8 million during 2018 and 2017, respectively.

Certain of the above debts are secured by a pledge of revenues from certain facilities, bond insurance and springing collateral, which would require the Institution to mortgage a substantial portion of real property if certain financial covenants and ratios are not maintained. The Institution was in compliance with all such financial requirements during 2018 and 2017.

At December 31, 2018 and 2017, the Institution had unsecured lines of credit available with banks totaling $250.0 million and $300.0 million, respectively, with varying renewable terms and interest. There were no amounts drawn at December 31, 2018 and 2017.

7. Other Noncurrent Liabilities

Other noncurrent liabilities consist of the following:

	December 31	
	2018	**2017**
	(In Thousands)	
Pension obligations *(Note 8)*	**$ 265,433**	$ 301,464
Postretirement obligation *(Note 8)*	**125,551**	134,738
Insurance reserves *(Note 9)*	**279,617**	292,601
Deferred compensation *(Note 8)*	**65,895**	70,299
Asset retirement obligations *(Note 13)*	**38,868**	38,621
Deferred gift annuity	**17,268**	19,187
All other	**7,148**	7,393
	$ 799,780	$ 864,303

8. Retiree Pension and Health Plans

The Institution has a retirement annuity plan which provides eligible staff members with retirement income through individual deferred annuity contracts purchased in each participant's name. In addition, the Institution maintains a nonqualified deferred compensation plan which is used for employer contributions in excess of those allowed by the retirement annuity plan. The effective date of this plan was January 1, 1983, and it has been grandfathered from the changes made by the Tax Reform Act of 1986. The plans' assets are included in assets whose use is limited in the combined balance sheets and consist of money market and mutual funds. The Institution contributes a fixed percentage of an individual's compensation to these plans.

Effective January 1, 2013, the Institution amended an existing 403(b) plan (composed of the basic plan and the voluntary plan) to have a new plan design and be renamed as the Memorial Sloan Kettering Cancer Center Retirement Savings Plan (the RSP). Under the RSP, all Institution employees are eligible to make voluntary employee contributions (salary deferrals), subject to IRS limits. Mandatory employee contributions are not required.

8. Retiree Pension and Health Plans (continued)

The Institution makes base contributions to the RSP for eligible employees, which depend on the employee's age (determined as of the preceding December 31). Additionally, the Institution matches contributions for voluntary employee contributions made by eligible employees. The Institution's cost for these plans was approximately $83.6 million and $72.9 million in 2018 and 2017, respectively.

The Institution also maintains a trusteed defined benefit plan (the Plan) for employees not covered by the above retirement annuity plan. The benefits are based on years of service, the employee's average compensation during the highest five of the last ten years of employment and a pension formula. The Plan has been amended and is frozen to new participants hired on or after December 16, 2012.

In October 2017, the Institution entered into a contract and sold approximately $100.0 million of its anticipated defined benefit pension liabilities to an insurance company via an annuity buy-out. The funding was paid from the Plan assets and only impacted a select group of retirees. These affected participants had no impact to their retirement benefits. In addition, certain participants of the Plan were offered the opportunity to receive the present value of their accrued plan benefits in a single lump-sum payment. The payments reflected a full settlement of all plan liabilities to such participants. These combined activities resulted in a reduction of the Plan liability of approximately $149.6 million and an approximate $33.5 million settlement cost for 2017.

In June 2018, the Institution entered into a contract and sold approximately $214.1 million of its anticipated defined benefit pension liabilities to an insurance company via an annuity buy-out. The funding was paid from the Plan assets and only impacted a select group of retirees. These affected participants had no impact to their retirement benefits. This resulted in a reduction of the Plan liability of approximately $238.0 million and an approximate $40.4 million settlement cost for 2018.

The Institution offers retirees and their spouses hospital and basic medical coverage which supplements any available Medicare coverage. The plan pays the balance of charges not paid by Medicare up to Medicare allowable charges. All employees become eligible for postretirement health care if they retire at age 60 or older, with at least 10 years of service, or under age 60 with 30 years of service. The accounting for the health care plans anticipates future retiree contributions increasing by annual health care cost increases plus 2%. Employees hired after December 31, 2006 are required to pay 100% of the coverage cost.

8. Retiree Pension and Health Plans (continued)

Effective January 1, 2016, the Institution provides each Medicare-eligible retiree and spouse with a defined contribution amount that can be used to purchase individual Medicare supplemental coverage. This defined contribution replaces the Institution's hospital and basic medical coverage for all Medicare-eligible participants who retire subsequent to December 31, 2006.

The Institution recognizes the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of the defined benefit plans in its combined balance sheets. Net unrecognized actuarial losses and the net unrecognized prior service costs at the reporting date will be subsequently recognized in the future as net periodic benefit cost pursuant to the Institution's accounting policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods and are not recognized as net periodic benefit cost in the same periods will be recognized as a component of net assets without donor restrictions. Included in net assets without donor restrictions at December 31, 2018 and 2017 are the following amounts that have not yet been recognized in net periodic benefit cost: unrecognized prior service credit of $47.7 million and $56.7 million, respectively, and unrecognized actuarial losses of $296.2 million and $420.2 million, respectively. The prior service credit and actuarial loss included in net assets without donor restrictions and expected to be recognized in net periodic benefit cost during the year ending December 31, 2019 are approximately $9.0 million and $10.0 million, respectively.

8. Retiree Pension and Health Plans (continued)

The following tables provide a reconciliation of the change in the benefit obligations and fair value of plan assets and funded status of the Institution's pension and postretirement plans:

	Pension Benefits		Postretirement Health	
	December 31		December 31	
	2018	2017	2018	2017
	(In Thousands)			
Reconciliation of benefit obligations				
Benefit obligations at beginning of year	**$ 1,687,892**	$ 1,443,274	**$ 139,171**	$ 146,486
Service cost	**76,543**	65,762	**3,835**	3,997
Interest cost	**64,302**	67,477	**5,361**	6,023
Plan participants' contributions	**682**	625	**1,565**	1,582
Actuarial (gains) losses	**(148,271)**	291,469	**(16,859)**	(14,399)
Plan amendment	**–**	(2,143)	**–**	–
Plan settlements	**(238,020)**	(149,613)	**–**	–
Benefits paid	**(13,992)**	(26,630)	**(3,914)**	(4,518)
Expenses paid	**(1,335)**	(2,329)	**–**	–
Benefit obligations at end of year	**$ 1,427,801**	$ 1,687,892	**$ 129,159**	$ 139,171

8. Retiree Pension and Health Plans (continued)

	Pension Benefits		Postretirement Health	
	December 31		December 31	
	2018	2017	2018	2017
	(In Thousands)			
Reconciliation of fair value of plan assets				
Fair value of plan assets at beginning of year	**$ 1,386,428**	$ 1,186,178	**$ –**	$ –
Actual return on plan assets	**(21,395)**	193,197	**–**	–
Employer contributions	**50,000**	185,000	**2,349**	2,936
Plan participants' contributions	**682**	625	**1,565**	1,582
Plan settlements	**(238,020)**	(149,613)	**–**	–
Benefits paid	**(13,992)**	(26,630)	**(3,914)**	(4,518)
Expenses paid	**(1,335)**	(2,329)	**–**	–
Fair value of plan assets at end of year	**1,162,368**	1,386,428	**–**	–
Unfunded status at end of year	**$ (265,433)**	$ (301,464)	**$ (129,159)**	$ (139,171)
Current portion of obligation	**$ –**	$ –	**$ (3,608)**	$ (4,433)
Noncurrent portion of obligation	**(265,433)**	(301,464)	**(125,551)**	(134,738)
Total	**$ (265,433)**	$ (301,464)	**$ (129,159)**	$ (139,171)

The accumulated benefit obligation for the plans as of December 31, 2018 and 2017 was approximately $1.20 billion and $1.45 billion, respectively.

8. Retiree Pension and Health Plans (continued)

The following table provides the components of the net periodic benefit cost for pension and postretirement benefit cost for the plans for the years ended December 31:

	Pension Benefits		Postretirement Health	
	2018	**2017**	**2018**	**2017**
	(In Thousands)			
Components of net periodic benefit cost				
Service cost	**$ 76,543**	$ 65,762	**$ 3,835**	$ 3,997
Interest cost	**64,302**	67,477	**5,361**	6,023
Expected return on assets	**(72,825)**	(73,141)	**–**	–
Settlement cost	**40,414**	33,480	**–**	–
Amortization of net loss	**10,741**	7,132	**1,923**	2,431
Amortization of prior service cost (credit)	**288**	657	**(9,310)**	(9,310)
Total net periodic benefit cost	**$ 119,463**	$ 101,367	**$ 1,809**	$ 3,141

Actuarial Assumptions

Weighted-average assumptions used to determine benefit obligations are as follows:

	Pension Benefits December 31		Postretirement Health December 31	
	2018	**2017**	**2018**	**2017**
Discount rate	**4.55%**	4.00%	**4.40%**	3.80%
Rate of compensation increase	**3.83**	3.83	**–**	–

8. Retiree Pension and Health Plans (continued)

Weighted-average assumptions used to determine net periodic benefit cost are as follows:

	Pension Benefits December 31		Postretirement Health December 31	
	2018	**2017**	**2018**	**2017**
Discount rate	**4.50%**	4.75%	**3.80%**	4.30%
Rate of compensation increase	**3.83**	3.83	**–**	–
Expected long-term return on plan assets	**5.65**	5.90	**–**	–

The expected return of the portfolio was arrived at using the weighted-average of the expected returns of the underlying benchmark asset classes.

The health care cost trend rate assumptions for the postretirement hospital and basic medical coverage plan at December 31 are as follows:

	2018	**2017**
Health care cost trend rate assumed for next year	**7.00%**	7.25%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	**5.00**	5.00
Year that the rate reaches the ultimate trend rate	**2025**	2025

8. Retiree Pension and Health Plans (continued)

Effect of Change in Health Care Trends

Assumed health care cost trend rates have a significant effect on the postretirement health amounts reported. A 1% change in assumed health care cost trend rates would have the following effects on postretirement benefit costs:

	2018		**2017**	
	1% Increase	**1% Decrease**	**1% Increase**	**1% Decrease**
	(In Thousands)			
Effect on total of service and interest cost components of net periodic postretirement health care benefit cost	**$ 1,942**	**$ (1,508)**	$ 2,215	$ (1,720)
Effect on the health care component of the accumulated postretirement benefit obligation	**21,848**	**(17,510)**	24,718	(19,591)

Plan Assets

The following table presents the weighted-average long-term target asset allocations and the percentages of the fair value of pension plan assets as of December 31:

	Target Allocation	**Percentage of Plan Assets**	
	2018	**2018**	**2017**
U.S.-based equity securities	**25%**	**27%**	25%
International equity investments	**10**	**11**	19
Fixed income investments	**25**	**28**	33
Alternative investments	**40**	**34**	23

8. Retiree Pension and Health Plans (continued)

The Plan assets consist of cash and cash equivalents, U.S. equities, fixed income securities, commingled funds, and alternative investments. Alternative investments are listed by their corresponding strategy and holdings include relative value funds, long/short equity funds, merger arbitrage/event driven funds, real estate, credit funds, private debt, and private equity. These investments pursue multiple strategies to diversify risk and reduce volatility.

Equities and real estate investment trusts are valued based on the quoted market prices of the securities as reported on national securities exchanges. Fixed income securities are valued based on readily available market quotations received from commercial pricing services. Such pricing services and brokers will generally provide bid-side quotations. Commingled funds are valued based on the NAV of shares held by the pension plan at year end. Alternative investments are stated at fair value as determined by Morgan Guaranty Trust Company of New York or by the investees. Value may be based on historical cost, appraisals, or other estimates that require varying degrees of judgment. Generally, fair value is stated at NAV, which reflects net contributions to the investee and an ownership share of realized and unrealized investment income and expenses.

The financial statements of the investees are audited annually by independent auditors. These investments may indirectly expose the pension plan to securities lending, short sales of securities, and trading in futures and forward contracts, options, swap contracts and other derivative products. While these financial instruments may contain varying degrees of risk, the pension plan's risk with respect to such transactions is limited to its capital balance in each investment.

Certain Plan assets could have liquidity restrictions that range from several months to ten years for certain alternative investments. Liquidity restrictions may apply to all or portions of a particular invested amount. Unfunded commitments for the alternative investments in the pension plan at December 31, 2018 are approximately $298.3 million.

8. Retiree Pension and Health Plans (continued)

Financial instruments of the Plan of the Institution, carried at fair value as of December 31, 2018, are classified in the table below as described in Note 4:

	Level 1	Level 2	Level 3	Total
		(In Thousands)		
Investments measured at fair value				
Cash, cash equivalents, and money market funds	$ **18,610**	$ **–**	$ **–**	$ **18,610**
U.S. equity investments:				
Equity securities	**30,958**	**–**	**–**	**30,958**
Real estate investment trusts	**2,274**	**–**	**–**	**2,274**
Fixed income investments:				
U.S. government and other	**7,758**	**–**	**–**	**7,758**
Private equity funds	**–**	**–**	**11,343**	**11,343**
	$ **59,600**	$ **–**	$ **11,343**	**70,943**
Investments measured at NAV as a practical expedient				
Commingled funds:				
U.S. equity				**265,296**
International equity				**132,767**
Fixed income				**312,575**
Alternative investments:				
Relative value funds				**2,042**
Long/short equity funds				**34,170**
Merger arbitrage/event driven funds				**47**
Real estate				**21,043**
Credit funds				**169,635**
Private debt				**20,180**
Private equity funds				**133,670**
Total investments at fair value				$ **1,162,368**

8. Retiree Pension and Health Plans (continued)

Financial instruments of the Plan of the Institution, carried at fair value as of December 31, 2017, are classified in the table below as described in Note 4:

	Level 1	Level 2	Level 3	Total
		(In Thousands)		
Investments measured at fair value				
Cash, cash equivalents, and money market funds	$ 31,972	$ –	$ –	$ 31,972
U.S. equity investments:				
Equity securities	55,933	–	–	55,933
Real estate investment trusts	2,811	–	–	2,811
Fixed income investments:				
U.S. government and other	13,100	–	–	13,100
Private equity funds	–	–	7,528	7,528
	$ 103,816	$ –	$ 7,528	111,344
Investments measured at NAV as a practical expedient				
Commingled funds:				
U.S. equity				261,536
International equity				268,575
Fixed income				440,986
Alternative investments:				
Relative value funds				4,233
Long/short equity funds				36,208
Merger arbitrage/event driven funds				7,323
Real estate				18,743
Credit funds				121,758
Private debt				17,096
Private equity funds				98,626
Total investments at fair value				$ 1,386,428

8. Retiree Pension and Health Plans (continued)

The following table represents a rollforward of the total plan assets classified by the Institution within Level 3 of the valuation hierarchy defined in Note 4:

	2018	2017
	(In Thousands)	
Fair value at beginning of year	**$ 7,528**	$ 3,199
Acquisitions	–	3,523
Unrealized gains	**3,815**	806
Fair value at end of year	**$ 11,343**	$ 7,528

Plan Objectives and Guidelines

The overall investment objective of the pension trust fund is to outperform a composite benchmark (an asset-weighted series of market indices used to measure the performance of each asset class) over a market cycle, while maintaining similar risk to the benchmark.

The portfolio is diversified to reduce the impact of losses in individual investments in a manner that is responsive to fiduciary standards. Single issuers are limited to 5% of the portfolio's aggregate market value at time of purchase, with the exception of U.S. government and agency securities and commingled funds. The underlying products that comprise a diversified portfolio may have exposure to derivatives which are managed and controlled.

Cash Flows

Contributions: The Institution expects to contribute $25.0 million to its pension plan in 2019.

8. Retiree Pension and Health Plans (continued)

Estimated future benefit payments: The Institution expects to pay the following benefit payments, which reflect expected future service, as appropriate:

	Pension Benefits	Postretirement Health
	(In Thousands)	
2019	$ 23,567	$ 3,608
2020	27,938	4,400
2021	33,920	4,941
2022	38,209	5,531
2023	43,955	5,998
2024 to 2028	309,485	35,614

9. Insurance Programs

MSKI, a domestic tax-exempt corporation, is the primary insurance company for certain insurable risks of the Institution. The primary coverages provided by MSKI to the Institution are health care professional liability, warranty coverage for covered health care equipment, terrorism and assumed coverage for workers' compensation, general liability and certain employee benefits of long-term disability and life insurance. The Institution's liability is limited, with catastrophic risk insured by commercial insurance carriers, or in the case of terrorism risk, by the U.S. Government under a formula established by Federal law.

Insurance reserves of MSKI represent estimated unpaid losses and loss adjustment expenses. Such amounts are established using management's estimates on the basis of claims records and independent actuarial reviews and include an amount for the adverse development of reported claims. Adjustments to the estimate of the liability for losses are reflected in earnings in the period in which the adjustment is determined. The insurance reserves are necessarily based on estimates and, while management believes that the amount is adequate, the ultimate liability may vary significantly from the amount provided. The estimated unpaid professional liability losses and loss adjustment expenses, including losses incurred but not reported at December 31, 2018 and 2017, were approximately $251.7 million and $262.2 million, respectively, and are recorded at the actuarially determined present value of approximately $228.4 million and $245.9 million, respectively, based on a discount rate of 2.1% in each year.

10. Operating Leases

The Institution leases certain facilities and equipment which are accounted for as operating leases. Total rent expense for operating leases aggregated approximately $37.5 million and $37.0 million for 2018 and 2017, respectively. The future minimum lease commitments for noncancelable leases in excess of one year are as follows (in thousands):

2019	$ 40,768
2020	38,614
2021	35,360
2022	32,450
2023	25,124
Thereafter	79,516
	$ 251,832

There are provisions in certain leases which provide for rent escalation for inflation and other items.

In August 2017, the Institution entered into an agreement to lease a building for a 30-year term. The Institution will become liable to make payments upon possession, which is expected to take place in 2019. Total lease payments are approximately $250.1 million and are excluded from the table above.

11. Grant Awards

The accompanying combined financial statements do not include amounts related to research grants (or portions thereof) that have been awarded to the Institute for which expenditures have not been incurred or cash has not been received. Such grant awards approximated $113.5 million and $116.2 million at December 31, 2018 and 2017, respectively.

12. Royalty and Other Income

Royalty and other income consists of the following:

	Year Ended December 31	
	2018	**2017**
	(In Thousands)	
Royalty income	**$ 75,679**	$ 81,491
Housing and parking	**38,021**	38,425
Cafeteria and food service	**7,376**	6,339
Services provided	**4,987**	5,776
Other	**33,077**	27,427
	$ 159,140	$ 159,458

13. Commitments and Contingencies

The Institution is involved in various litigation and claims that are not considered unusual given the complexity and size of the Institution's business. Management believes that the ultimate resolution of these matters will not have a material impact on the Institution's combined financial statements.

The Institution recognizes a liability for the future cost of conditional asset retirement obligations, including building modifications and lease end costs. The Institution removes contained asbestos and any applicable radioactive materials from facilities as facilities are being repaired and/or replaced. The Institution has recorded the estimated liability for the cost of asbestos remediation and radiation decommissioning for the Institution's current plans for building modifications and lease end costs of approximately $38.9 million and $38.6 million at December 31, 2018 and 2017, respectively.

14. Functional Expenses

The functional expenses related to the fulfillment of the Institution's mission for the years ended December 31, 2018 and 2017 are as follows (in thousands):

	Patient Care	Research	Education	Fundraising	Management and General	2018 Total
Compensation and fringe benefits	**$ 2,012,926**	**$ 332,338**	**$ 197,111**	**$ 33,676**	**$ 11,285**	**$ 2,587,336**
Purchased supplies and services	**1,429,456**	**236,147**	**37,229**	**35,627**	**17,715**	**1,756,174**
Depreciation and amortization	**206,478**	**76,368**	**10,505**	**1,217**	**5,671**	**300,239**
Interest	**31,213**	**10,190**	**–**	**–**	**5,642**	**47,045**
Total	**$ 3,680,073**	**$ 655,043**	**$ 244,845**	**$ 70,520**	**$ 40,313**	**$ 4,690,794**

	Patient Care	Research	Education	Fundraising	Management and General	2017 Total
Compensation and fringe benefits	$ 1,801,427	$ 306,223	$ 187,002	$ 31,005	$ 9,475	$ 2,335,132
Purchased supplies and services	1,193,363	221,796	37,688	32,631	16,457	1,501,935
Depreciation and amortization	195,753	75,493	9,442	1,437	5,020	287,145
Interest	27,991	12,483	–	–	4,869	45,343
Total	$ 3,218,534	$ 615,995	$ 234,132	$ 65,073	$ 35,821	$ 4,169,555

15. Subsequent Events

Subsequent events have been evaluated through April 5, 2019, which is the date the combined financial statements were issued. No subsequent events have occurred that require disclosure in or adjustment to the combined financial statements.

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