



**Ochsner Clinic Foundation  
d/b/a Ochsner Health System  
Annual Financial Information Disclosure**

**For the Year Ended  
December 31, 2017**

## System Overview

Ochsner Clinic Foundation d/b/a Ochsner Health System (“OCF” or “Ochsner”) is a Louisiana-based nonprofit corporation and an organization exempt from taxation under Section 501(c)(3) of the Internal Revenue Code (the “Code”) founded on providing the best patient care, research and education. Ochsner is the largest non-profit, academic, multi-specialty, integrated healthcare delivery system in the Gulf Coast region with nine hospitals, 77 health centers, 14 Urgent Care Clinics and 4 Occupational Health Clinics. When combined with affiliated hospitals, Ochsner owns, provides management assistance and support, or is affiliated with 30 hospitals. It also employs over 1,400 active staff physicians that have 1,200 board certifications in 70 specialties, trains over 275 medical residents and fellows annually, has 473 Doctor of Medicine students enrolled in the University of Queensland, Ochsner Clinical School, and is currently conducting over 1,000 clinical research studies. In 2017, more than 513,000 people from all 50 states and more than 80 countries visited Ochsner.

Ochsner is recognized nationally for quality. Awards and recognitions in 2017 include:

- Ochsner Medical Center, Ochsner Baptist, a campus of Ochsner Medical Center, and Ochsner Medical Center – West Bank Campus were ranked among the best hospitals in the country in four medical specialties, according to *U.S. News and World Report’s* 2017-18 Best Hospitals rankings. Ochsner Medical Center, Ochsner Baptist and Ochsner Medical Center – West Bank Campus were also ranked #1 among the best hospitals in Louisiana and #1 among the best hospitals in the New Orleans metro area as well as being recognized among the Best Hospitals in Southeastern Louisiana.
- Ochsner Medical Center Baton Rouge received the Healthgrades 2017 Distinguished Hospital Award for Clinical Excellence™.
- Ochsner Medical Center, Ochsner Baptist, Ochsner Medical Center – West Bank Campus, Ochsner Medical Center Kenner, Ochsner Medical Center – Baton Rouge and Leonard J. Chabert Medical Center have been recognized for Five-star ratings, Specialty Excellence Awards and are among the top 5 and 10% in the nation by the Healthgrades 2018 Report to the Nation.
- Ochsner Medical Center was recognized as first in the country for liver transplants for the fifth year in a row by CareChex® – a division of Comparion®.
- Ochsner was named the number one transplant center in the country for overall transplant care quality by CareChex® – a division of Comparion®, caring for patients from all over the country and world.
- Ochsner Medical Center, Ochsner Baptist, a campus of Ochsner Medical Center, and Ochsner Medical Center - West Bank Campus were named to the Truven 100 Top Hospitals Award list as one of the 15 U.S. Major Teaching Hospitals.
- Ochsner Medical Center - Baton Rouge became one of only 10 hospitals in the United States to receive both the 2017 100 Top Hospitals® Award by Truven Health Analytics and the 100 Top Hospitals® Everest Award.
- *Becker’s Hospital Review* recognized Ochsner Medical Center as one of the “100 Great Hospitals in America” for 2017. This is the sixth consecutive year that Ochsner Medical has been recognized with this award and is the only Louisiana hospital named to this list.
- Ochsner Hospital for Children was ranked among the top 50 children’s hospitals in the country for pediatric cardiology and heart surgery specialties in the new 2017-18 *U.S. News and World Reports* Best Children’s Hospitals rankings.
- For the 11th consecutive year, Ochsner has been named as a Most Wired Advanced Hospital in the 19th annual Health Care’s Most Wired Survey by Hospitals & Health Networks (H&HN) magazine.



## **Forward-Looking Information:**

*This Financial Information Disclosure contains disclosures, which contain “forward-looking statements” within the meaning of the Federal securities laws. Forward-looking statements include all statements that do not relate solely to historical or current fact and can be identified by the use of words “expect”, “anticipate”, “intend”, “project”, “likely”, “may”, “might”, “estimate”, “budget” and similar words or expressions. These forward-looking statements are based on the current plans and expectations of Ochsner Clinic Foundation d/b/a Ochsner Health System (“OCF” or “Ochsner”) as of the date of this report and are subject to a number of known and unknown risks and uncertainties inherent in the operation of health care facilities, many of which are beyond OCF's control, that could significantly affect current plans and expectations and OCF's future financial position and results of operations.*

*Important factors that could cause results to differ materially from those expected by management include, but are not limited to, general, economic and business, competition from other healthcare facilities in the service areas, an unfavorable pricing environment, inability to achieve expected efficiencies in operations or effectively control health care costs, the efforts of insurers and others to contain health care costs, changes in Medicare or Medicaid reimbursement formulas, the risk that managed care provider arrangements will not be negotiated or renewed on acceptable terms, future divestitures or acquisitions which may have a financial impact, availability and terms of capital to fund future expansion and ongoing capital needs, new laws or regulations, the possible enactment of federal or state health care reform, fines or penalties related to regulatory matters, changes in accounting standards and practices, the outcome of pending and future litigation and government investigations, labor issues and the ability to attract and retain qualified management and other personnel, including physicians, nurses and medical support personnel.*

*Given these uncertainties, bondholders and prospective bondholders are cautioned not to unduly rely on such forward-looking statements when evaluating the information presented in this report. OCF disclaims any obligation, and makes no promise, to update any such factors or forward-looking statements or to disclose any facts, events or circumstances after the date hereof that may affect the accuracy of any forward-looking statements, whether as a result of changes in underlying factors, to reflect new information, as a result of the occurrence of events or developments or otherwise.*

## **Description of Credit Group**

Ochsner's history began when the Ochsner Clinic opened its doors to patients on January 2, 1942 as a physician practice. Alton Ochsner Medical Foundation ("AOMF"), a Louisiana not for profit corporation exempt from taxation under Section 501(c)(3) of the IRS Code, was founded on January 21, 1944 to own and operate Ochsner Foundation Hospital. On August 31, 2001, Ochsner Clinic merged with a wholly-owned subsidiary of AOMF and Ochsner Clinic became a wholly-owned subsidiary of AOMF. As part of the acquisition of Ochsner Clinic, AOMF changed its name to Ochsner Clinic Foundation ("OCF"). Ochsner Community Hospitals ("OCH") and Ochsner Health System ("OHS"), each a Louisiana not for profit corporation exempt from taxation under Section 501(c)(3) of the IRS code, were formed in July 2006. OCH was formed for the purpose of acquiring certain medical facilities from Tenet Healthcare Corporation, and OHS was formed to be the parent company and sole corporate member of OCF and OCH. Effective December 31, 2016, OCH was merged with and into OCF, with OCF continuing as the surviving entity. Effective December 31, 2017, OHS was merged with and into OCF, with OCF continuing as the surviving entity. Ochsner Clinic Foundation still operates under the trade name of Ochsner Health System. All references to "Ochsner," "Ochsner Health System," "OCF," or "OHS" hereinafter refer to Ochsner Clinic Foundation.

OCF is the only Obligated Group Member under the Master Indenture. Certain affiliates of OCF have been designated as Designated Affiliates and Credit Group Members under the Master Indenture. Credit Group or Credit Group Members means all Obligated Group Members and Designated Affiliates. Under the Master Indenture, Obligated Group Members are jointly and severally liable to make payments with respect to Obligations issued under the Master Indenture. Designated Affiliates are not obligated to make payments with respect to Obligations but may be required to transfer to Obligated Group Members, to the extent legally available, amounts necessary to enable the Obligated Group Members to make payments under the Master Indenture. Obligated Group Members may designate entities as Designated Affiliates under the Master Indenture, and may rescind such designation at any time. Designated Affiliates have not changed since the 2017 Official Statement dated May 11, 2017. OCF and Designated Affiliates constituted 97.0% of the total assets of OCF Consolidated as of December 31, 2017 and 99.3% of the total revenue of OCF Consolidated for the year ended December 31, 2017.

## **Obligated Group Member**

OCF is the only Obligated Group Member under the Master Indenture. OCF is headquartered in New Orleans, Louisiana, and, either directly or through its fully owned affiliates or subsidiaries, owns and operates seven hospitals and other healthcare facilities, including:

- OMC, a 555-bed acute care hospital located in New Orleans, Louisiana, which serves as the flagship of Ochsner, and includes an 11-story clinic building, a 137-room hotel and related medical facilities located on a main campus in Jefferson Parish at the western end of New Orleans;
- Ochsner Elmwood Hospital, a 66-bed satellite hospital of OMC, located in Elmwood, Louisiana;
- Ochsner Medical Center – West Bank Campus, a 165-bed acute care satellite hospital of OMC in New Orleans, Louisiana,
- Ochsner Baptist Medical Center, a 139-bed acute care satellite hospital of OMC in New Orleans, Louisiana.
- Ochsner Medical Center - Kenner, a 110-bed acute care hospital in Kenner, Louisiana;
- Ochsner Medical Center – Baton Rouge, a 150-bed acute care hospital in Baton Rouge, Louisiana;
- Ochsner Medical Center – North Shore, a 168-bed acute care hospital in Slidell, Louisiana;
- 77 health centers throughout southeast Louisiana and Mississippi;
- 14 Urgent Care Clinics and 4 Occupational Health Clinics throughout Greater New Orleans; and,
- Several fitness centers that operate as Ochsner Fitness Center.

OCF, through its fully owned subsidiary, operates two hospitals:

- Ochsner St. Anne General Hospital, a 35-bed acute care hospital in Raceland, Louisiana, and
- Effective April 1, 2018, Hancock Medical Center, a 102-bed acute care hospital in Bay St. Louis, Mississippi.

OCF, either directly or through its fully owned affiliates or subsidiaries, provides management assistance and support to three hospitals:

- Leonard J. Chabert Medical Center (“LJCMC”), a 156-bed public, safety net hospital in Houma, Louisiana;
- St. Charles Parish Hospital (“SCPH”), a 59-bed public, safety net hospital in Luling, Louisiana;
- St. Bernard Parish Hospital (“SBPH”), a 40-bed public, safety net hospital in Chalmette, Louisiana.

OCF also has joint operating agreements with three hospitals:

- Terrebonne General Medical Center (“TGMC”), a 321-bed acute care hospital in Houma, Louisiana;
- St. Tammany Parish Hospital (“STPH”), a 232-bed acute care hospital in Covington, Louisiana;
- Slidell Memorial Hospital (“SMH”), a 229-bed public acute care hospital in Slidell, Louisiana

OCF also entered into strategic partnerships to create clinical affiliations with Lafayette General Health, CHRISTUS Health Louisiana, Glenwood Regional Medical Center and Southwest Mississippi Regional Medical Center.

In recent years, OCF has entered into several strategic partnerships, affiliation agreements, and acquisitions that increase local access to care, improve quality, reduce the cost of healthcare, and share best practices and resources in order to improve the health of Louisiana communities. Agreements completed in 2017 are as follows:

- Millennium Healthcare Management, Inc. On January 10, 2017, OCF completed the acquisition of Millennium Healthcare Management, Inc. (“MHM”). The acquisition added 12 Urgent Care and 4 Occupational Health clinic locations to the services OCF provides in the Greater New Orleans area with expanded services and program options and better access to the most appropriate care at a wider range of destinations.
- St. Bernard Parish Hospital Service District. On September 25, 2017, Ochsner announced that the St. Bernard Parish Hospital Service District Board approved a long-term management agreement with OCF, through a wholly-owned subsidiary, to provide management assistance and support to St. Bernard Parish Hospital. The agreement was fully implemented on November 5, 2017. St. Bernard Parish Hospital remains a public hospital owned by St. Bernard Parish and governed by the District board.
- Louisiana State University. In December 2017, OCF, The State of Louisiana (“State”), the Board of Supervisors of Louisiana State University and Agricultural and Mechanical College (“LSU”), and the Biomedical Research Foundation (“BRF”) signed Letters of Intent (LOI) to create a new, long-term, public/private partnership related to certain hospital and healthcare operations in Shreveport and Monroe. Under the proposed arrangement, LSU and OCF will jointly form a new entity to assume overall responsibility for the operations and clinical activities of the former LSU hospitals and clinics in Shreveport and Monroe and coordinate activities between LSU Medical School, both parties’ physicians, and the healthcare operations in Shreveport and Monroe. This agreement will not be effective until 2018.
- Hancock Medical Center. On April 1, 2018, OCF, through a wholly-owned subsidiary, closed an agreement with the Hancock County Board of Supervisors to operate Hancock Medical Center, a 102-bed acute care hospital, under a 25-year lease agreement, and OCF will own the property at the end of the lease term. This lease expands upon the strategic partnership the two organizations created in 2013 through a management agreement under which Ochsner managed Hancock Medical Center. As part of this transaction, OCF acquired the current assets, liabilities and provider number of Hancock. The hospital was renamed Ochsner Hancock Medical Center.

- In March 2018, Ochsner signed a membership interest purchase agreement with CHRISTUS Health (“CHRISTUS”), to acquire a 40% minority ownership interest in CHRISTUS Health Southwestern Louisiana (“SWLA”). SWLA owns and operates healthcare facilities and operations related to physician practices in Lake Charles, Louisiana, including CHRISTUS St. Patrick Hospital, CHRISTUS Lake Area Medical Center and various clinical facilities. CHRISTUS St. Patrick Hospital is a 50-bed hospital and CHRISTUS Lake Area Medical Center is an 88-bed, full-service acute care hospital in Lake Charles, Louisiana. This purchase is expected to close during the 2nd half of 2018, once regulatory approval is received.

## **Governance**

On September 25, 2017, OCF announced two newly elected members to the Board of Directors:

**Victoria Smith, MD**, currently serves as Associate Medical Director for St. Charles Parish Hospital and as a primary care physician in Ochsner’s River Region. Dr. Smith is board-certified in family medicine.

**Kenneth Polite, Jr.**, is Vice President of Ethics and Compliance for Entergy Corporation, a local attorney and a public servant. Mr. Polite was sworn in as U.S. Attorney for the Eastern District of Louisiana in September 2013, and served in this position until March of this year. He was a former board member and board chairman for both New Orleans College Preparatory Charter Schools and Breakthrough New Orleans, and currently serves as a board member for Youth Empowerment Project, the Anti-Defamation League of New Orleans and New Schools for New Orleans.

On December 11, 2017, OCF announced the departures of Drs. Dennis Kay and Richard Deichmann from the Board of Directors following expiration of their current terms on December 31, 2017. Effective January 1, 2018, the following two physicians were elected to the Board of Directors:

**Karen Blessey, MD**, currently serves as Director of Primary Care Recruiting and as an internal medicine physician at Ochsner Baptist. Dr. Blessey is board-certified in family medicine.

**Leonardo Seoane, MD**, currently serves as the Head of School for the University of Queensland Ochsner Clinical School and a lung transplant/pulmonary/critical care physician at Ochsner Medical Center. Dr Seoane is board-certified in both pediatrics and pulmonary/critical care.

On April 2, 2018 Steve Stumpf an Ochsner Clinic Foundation board member since 2010 passed away.

## **Executive Leadership**

As of the release date of this document, there have been no changes to the Executive Leadership since the 2017 Official Statement dated May 11, 2017.

## **Management Discussion and Analysis of Financial Results**

### **Executive Summary:**

OCF had Excess Revenue over Expenses of \$140.3 million (4.7% of Total Unrestricted Revenues) for 2017 compared to \$29.1 million (1.1% of Total Unrestricted Revenues) for 2016, Income from Operations of \$70.1 million (2.3% of Total Unrestricted Revenues) for 2017 compared to \$50.4 million (1.8% of Total Unrestricted Revenues) for 2016 and operating EBITDA was \$248.3 million (8.3% of Total Unrestricted Revenues) for 2017 compared to \$219.6 million (7.9% of Total Unrestricted Revenues) for 2016.

### **Statement of Operations:**

OCF achieved Total Unrestricted Revenues of approximately \$3.0 billion for 2017, an increase of \$234.4 million or 8.5% over 2016 primarily due to organic growth as well as an increase in patients referred from affiliates and outlying facilities through OCF's regional referral center. Net Patient Service Revenue Less Provision for Bad Debts increased \$141.0 million or 6.5%. Premium Revenue increased \$12.6 million. When comparing 2017 to 2016, discharges increased 3.7%, patient days increased 5.0%, inpatient surgical procedures increased 5.0%, outpatient surgical procedures increased 8.3%, emergency room visits increased less than 1%, clinic relative value units increased 8.8%, clinic visits increased 10.4%, and unique clinic patient visits increased 15%. OHS continues to see an increase in patients referred from affiliates and outlying facilities through its regional referral center. Inpatient transfers to Ochsner Medical Center in 2017 increased 4.8% over 2016. Revenue received from any of our managed or affiliated hospitals is not included within Net Patient Service Revenue.

Other Operating Revenue for 2017 was \$403.5 million, an \$80.5 million increase over 2016. Other Operating Revenue for 2017 includes a \$33.5 million increase related to pharmacy revenue and a \$29.1 million increase related to funding in 2017 from partners of partially owned subsidiaries formed exclusively for charitable, educational and scientific purposes compared to 2016. Other Operating Revenue for 2017 also includes \$8.9 million of insurance proceeds. Other Operating Revenue includes \$41.1 million in 2017 and \$42.0 million in 2016 of revenue related to management agreements and joint operating agreements.

The Provision for Bad Debt, as a percentage of Patient Service Revenue – Net of Contractual Allowances and Discounts and Premium Revenue net of Medical Services to Outside Providers, was 3.4% for 2017 compared to 3.7% for 2016. A portion of the reduction in bad debt can be attributed to Louisiana expanding Medicaid in July 2016 which increased Medicaid as a percentage of gross revenue from 14% in 2016 to 17% in 2017. Bad Debt and Charity Care combined accounted for 4.4% of Patient Service Revenue – Net of Contractual Allowances and Discounts and Premium Revenue net of Medical Services to Outside Providers for 2017 compared to 5.1% for 2016.

Salaries and Wages for 2017 were \$1.4 billion, a \$100.8 million increase over 2016. The majority of the increase is related to additional staffing and additional providers needed to meet increased patient demand. Total providers increased by 8.7% or 120 full-time equivalents ("FTEs"). That includes a 7.7% increase in physicians, or 71 FTEs, and a 10.7% increase in the number of other providers, or 49 FTEs. Ochsner employs over 1,400 active staff physicians and over 600 Other Providers.

Medical Services to Outside Providers expense for 2017 increased by \$1.4 million from 2016. OCF currently provides services to approximately 35,000 senior members under a capitation contract for both physician and hospital services.

Medical Supplies and Services increased by \$69.4 million when comparing 2017 to 2016. Medical Supplies and Services as a percentage of Total Unrestricted Revenues was 19.0% for 2017 and 18.1% for 2016. Approximately \$19.8 million of the increase is due to increased drug expenses primarily due to an increased volume of chemotherapy and infusion drugs. Ochsner continues to see a continuing shift toward higher acuity patients, causing an approximate \$20.0 million increase in medical supplies and implants related to Transapical Valve replacements, Cath Lab procedures and Electrophysiology Lab procedures.

Other operating expenses which includes building and equipment, insurance, professional services and general and administrative expenses for 2017 increased by \$30.6 million over 2016. \$3.8 million of the increase is related to sales tax due to changes to the Louisiana State Sales Tax legislation that went into effect during April 2016. \$7.6 million of the increase is related to Medicaid Provider Assessment.

OCF had net non-operating gains of \$70.2 million for 2017 compared to net non-operating losses of \$21.3 million for 2016. Non-operating gains and losses include realized gains and losses, as well as changes in the market value of the pooled investment portfolio, and losses on the early extinguishment of debt.

### **Ratings**

As of the release date of this document, there have been no changes to the ratings since the 2017 Official Statement dated May 11, 2017. Moody's Investors Service, Inc. has provided a rating for the Bonds of A3. Fitch Ratings has provided a rating for the Bonds of A-.

### **Liquidity and Cash Position**

At December 31, 2017, OCF had unrestricted cash and investments of \$956.1 million which equates to 124 days cash on hand. Cash and Investments increased \$105.1 million from December 31, 2016 and days cash on hand increased by 7 days from December 31, 2016. The increase includes \$79.4 million of non-operating gains related to the pooled investment portfolio and a \$54.1 million increase in Accounts Payable and Accrued Salaries, Wages and Benefits. The increase also includes reimbursement from the Series 2017 bond proceeds. OCF expects to draw down an additional \$80 million of Series 2017 bond proceeds in 2018. The increase is partially offset by the January 10, 2017 acquisition of Millennium Healthcare Management, Inc.'s 12 Urgent Care and 4 Occupational Health Clinics. As of December 31, 2017, OCF had \$97.4 million of donor restricted investments.

## Cash and Investments; Days Cash on Hand

The table below includes Cash and Investments and Days Cash on Hand. Dollar amounts are in thousands.

	<u>Cash and Investments</u>		<u>Days Cash on Hand</u>	
	<u>Dec. 31,</u> <u>2017</u>	<u>Dec. 31,</u> <u>2016</u>	<u>Dec. 31,</u> <u>2017</u>	<u>Dec. 31,</u> <u>2016</u>
Monthly Liquidity	\$801,840	\$720,629	104	99
Liquidity greater than 30 days and less than one year	139,096	114,000	18	16
Locked Up (liquidity one year or more)	15,181	16,376	2	2
Total	<u>\$956,117</u>	<u>\$851,005</u>	<u>124</u>	<u>117</u>

## Debt and Debt Service Coverage.

As of December 31, 2017, OCF had \$1.1 billion in total long-term debt outstanding, compared to \$1.05 billion at December 31, 2016. The long-term debt to capitalization ratio for OCF was 62.5% in 2017 versus 63.0% in 2016.

### **Debt Service Coverage Calculation:**

	<u>2017</u>	<u>2016</u>
Income Available for Debt Service	\$295,154	\$226,549
Annual Debt Service	\$69,141	\$72,021
Annual Debt Service Coverage Ratio	4.3x	3.2x

<u>Series</u>	<u>Par Amt O/S</u>	<u>Final Maturity</u>	<u>Interest Mode</u>
<b>OCHSNER CLINIC FOUNDATION</b>			
Series 2015 Taxable New Money	252,820,000	5/15/2045	Fixed
Series 2015 Tax Exempt Refunding	110,775,000	5/15/2047	Fixed
Series 2016	154,060,000	5/15/2047	Fixed
Series 2017 New Money	160,645,000	5/15/2046	Fixed
Series 2017 Tax Exempt Refunding	260,910,000	5/15/2042	Fixed
March 2013 Note Payable (1)	5,867,493	3/31/2033	Fixed
December 2013 Note Payable (1)	50,709,165	12/31/2028	Fixed
July 2014 Note Payable (1)	71,622,432	8/15/2034	Fixed
December 2013 Promissory Note	12,622,917	12/30/2020	Variable (3)
October 2014 Promissory Note	17,600,000	10/31/2021	Fixed
September 2015 Promissory Note	24,000,000	9/30/2022	Variable (3)
2006 Working Capital Note(2)	8,731,546	5/1/2026	Variable
Software and Equipment Loans(2)	340,624	N/A	N/A
Capital Lease Obligations(2)	12,219,279	N/A	N/A
SUBTOTAL	<u>1,142,923,457</u>		

Note:

(1) Not an obligation of a credit group member or a supplemental obligation of the Master Indenture.

(2) Not secured by an Obligation issued under the Master Indenture.

(3) Interest on this loan has been fixed through an interest rate swap agreement.

**Ochsner Clinic Foundation and Subsidiaries**  
**Consolidated Statements of Operations**  
**As of December 31, 2017 and 2016**  
**(\$ In Thousands)**

	<u>2017</u>	<u>2016</u>	<u>Difference</u>
Unrestricted revenues:			
Patient service revenue, net of contractual allowances and discounts	2,381,355	2,241,043	\$ 140,312
Provision for bad debts	<u>(87,789)</u>	<u>(88,454)</u>	<u>665</u>
Net patient service revenue, less provision for bad debts	2,293,566	2,152,589	140,977
Premium revenue	298,824	286,186	12,638
Other operating revenue	403,463	322,978	80,485
Net assets released from restriction, used for operations	<u>6,319</u>	<u>6,040</u>	<u>279</u>
Total unrestricted revenues	<u>3,002,172</u>	<u>2,767,793</u>	<u>234,379</u>
Expenses:			
Salaries and wages	1,359,294	1,258,517	100,777
Benefits	138,008	134,859	3,149
Medical services to outside providers	133,952	132,534	1,418
Medical supplies and services	570,155	500,792	69,363
Other operating expenses	552,756	522,155	30,601
Depreciation and amortization	128,098	115,832	12,266
Interest	<u>49,762</u>	<u>52,718</u>	<u>(2,956)</u>
Total expenses	<u>2,932,025</u>	<u>2,717,407</u>	<u>214,618</u>
Income from operations	<u>70,147</u>	<u>50,386</u>	<u>19,761</u>
Non-operating gains (losses):			
Investment and other realized gains - net	47,147	7,613	39,534
Loss on early extinguishment of debt	(9,256)	(39,110)	29,854
Unrealized gains on alternative investments - net	<u>32,290</u>	<u>10,241</u>	<u>22,049</u>
Total non-operating gains (losses)	<u>70,181</u>	<u>(21,256)</u>	<u>91,437</u>
Excess of revenues over expenses	<u>\$ 140,328</u>	<u>\$ 29,130</u>	<u>\$ 111,198</u>

**Ochsner Clinic Foundation and Subsidiaries**  
**Consolidated Balance Sheets**  
**As of December 31, 2017 and 2016**  
**(\$ In Thousands)**

	<u>December 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	186,401	\$ 121,569
Assets limited as to use, required for current liabilities	7,370	5,600
Patient accounts receivable, net	249,299	252,598
Other receivables	104,827	99,516
Inventories	68,608	56,022
Prepaid expenses and other current assets	34,395	32,972
Estimated third-party payor settlements	<u>22,224</u>	<u>19,626</u>
Total current assets	673,124	587,903
Assets limited as to use:		
By Board for capital improvements, charity, research, and other	769,717	729,436
Under bond indenture agreements	95,106	21,477
Under self-insurance trust fund	9,301	9,135
Donor-restricted long-term investments	<u>97,425</u>	<u>78,433</u>
Total assets limited as to use	971,549	838,481
Less assets limited as to use, required for current liabilities	<u>(7,370)</u>	<u>(5,600)</u>
Non-current assets limited as to use	964,179	832,881
Investments in unconsolidated affiliates, real estate, and other	19,644	14,045
Property, net	927,979	821,692
Goodwill	71,195	43,558
Intangible assets	12,354	11,467
Other assets	47,332	39,293
Total assets	<u>\$ 2,715,807</u>	<u>\$ 2,350,839</u>

**Ochsner Clinic Foundation and Subsidiaries**  
**Consolidated Balance Sheets**  
**As of December 31, 2017 and 2016**  
**(\$ In Thousands)**

	<u>December 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
<b>Liabilities and net assets</b>		
Current liabilities:		
Accounts payable	190,683	\$ 150,332
Accrued salaries, wages, and benefits	163,218	149,483
Deferred revenue	35,552	9,669
Estimated third-party payor settlements	4,275	3,769
Bonds payable, current portion	2,095	7,030
Notes payable, current	52,430	52,430
Long-term debt, current portion	13,299	15,566
Other current liabilities	33,266	30,927
Total current liabilities	<u>494,818</u>	<u>419,206</u>
Pension and postretirement obligations	147,596	166,532
Bonds payable	986,730	828,408
Long-term debt	175,722	188,693
Other long-term liabilities	38,770	36,982
Total liabilities	<u>1,843,636</u>	<u>1,639,821</u>
Net assets:		
Unrestricted	745,282	596,966
Temporarily restricted	100,206	88,219
Permanently restricted	26,683	25,833
Total net assets	<u>872,171</u>	<u>711,018</u>
Total liabilities and net assets	<u>\$ 2,715,807</u>	<u>\$ 2,350,839</u>

**Ochsner Clinic Foundation and Subsidiaries**  
**Condensed Consolidated Statements of Cash Flows**  
**As of December 31, 2017 and 2016**  
**(\$ In Thousands)**

	<b>2017</b>	<b>2016</b>
<u>Cash Flows from Operating Activities:</u>		
Increase in net assets	\$ 161,153	\$ 55,454
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Pension related changes other than net periodic pension costs	(2,674)	26,449
Depreciation and amortization	128,098	115,832
Provision for bad debts	87,789	88,454
Non-cash portion of loss on early extinguishment of debt	8,793	3,196
Amortization of deferred financing costs and debt discounts	(591)	498
Loss (income) from equity-method investment, net of premiums paid	721	(62)
Net realized and unrealized gains on investments and cash received	(88,705)	(42,653)
Gain on contribution of property to joint venture	(195)	(6,994)
Other, net	(850)	(2,070)
Changes in operating assets and liabilities, net of acquisitions:		
Patient accounts receivable	(84,490)	(115,525)
Other current and noncurrent assets	(27,962)	(41,110)
Accounts payable	38,924	1,189
Accrued expenses and other liabilities	27,332	(17,475)
Net cash provided by operating activities	247,343	65,183
<u>Cash Flows from Investing Activities:</u>		
Purchases of assets whose use is limited and other investments	(389,924)	(256,336)
Sales and maturities of assets whose use is limited and other investments	339,601	192,980
Capital expenditures	(228,542)	(166,159)
Acquisitions of businesses, net of cash acquired	(30,816)	-
Other	313	(948)
Net cash used in investing activities	(309,368)	(230,463)
<u>Cash Flows from Financing Activities:</u>		
Repayment of bonds payable and long-term debt	(323,471)	(175,183)
Proceeds from bonds payable and long-term borrowings	458,024	174,369
Payments of debt financing costs	(4,288)	(2,229)
Payments on capital lease obligations	(4,258)	(2,981)
Proceeds from contributions restricted for long-term investments	850	2,070
Net cash provided by financing activities	126,857	(3,954)
Net Increase (Decrease) in Cash and Cash Equivalents	64,832	(169,234)
Cash and Cash Equivalents, Beginning of Year	121,569	290,803
Cash and Cash Equivalents, End of Period	\$ 186,401	\$ 121,569

## OCHSNER CLINIC FOUNDATION UTILIZATION STATISTICS

	2015	2016	2017
Licensed Beds (1)	1,283	1,284	1,388
Average Number of Beds in Use (2)	1,371	1,372	1,365
Discharges Including Newborn	65,843	67,454	70,052
Discharges Excluding Newborn	60,186	61,341	63,597
Patient Days Including Newborn	313,483	326,145	342,561
Patient Days Excluding Newborn	300,526	312,349	327,929
Average Daily Census (3)	824	853	898
Percent Occupancy (3)	60.04%	62.20%	65.79%
Average Length of Stay	4.8	4.8	4.9
Adjusted Patient Days (3)	612,443	659,409	699,547
Clinic Visits (4)	1,664,978	1,823,527	2,012,588
Clinic RVUs	5,455,838	6,050,375	6,584,475
Unique Clinic Patients (5)	411,988	446,515	513,328
Employed Physician FTEs	875.0	924.1	995.4
Transfers through Regional Referral Center	8,787	10,201	10,691

	Ochsner Medical Center	OMC West Bank	Ochsner St. Anne	OMC Baton Rouge	OMC North Shore	OMC Kenner	Ochsner Baptist Med. Ctr.	TOTAL
	Licensed Beds (1)	621	165	35	150	168	110	
Average Number of Beds in Use (2)	576	181	35	159	168	110	136	1,365
Discharges Including Newborn	28,105	8,132	1,973	8,745	5,147	7,640	10,310	70,052
Discharges Excluding Newborn	28,105	7,118	1,676	7,341	5,147	6,690	7,520	63,597
Patient Days Including Newborn	175,080	34,607	7,224	30,172	22,018	27,697	45,763	342,561
Patient Days Excluding Newborn	175,080	32,191	6,564	27,243	22,018	25,458	39,375	327,929
Average Daily Census (3)	480	88	18	75	60	70	108	898
Percent Occupancy (3)	83.33%	48.62%	52.68%	47.17%	35.58%	63.64%	79.56%	65.79%
Average Length of Stay	6.2	4.3	3.7	3.5	4.3	3.6	4.4	4.9
Adjusted Patient Days (3)	323,217	68,195	31,743	85,469	45,418	63,664	81,840	699,547

(1) Data excludes NICU and Nursery Beds.

(2) Data excludes Nursery beds, but includes NICU beds, a large number of beds in use will yield an amount greater than the number of licensed beds.

(3) Data excludes Normal Newborn Days.

(4) Data includes physician visits and resident visits. 2015-2016 were restated to conform to the 2017 presentation.

(5) Data includes the numbers of patients seen in a 12 months rolling period.

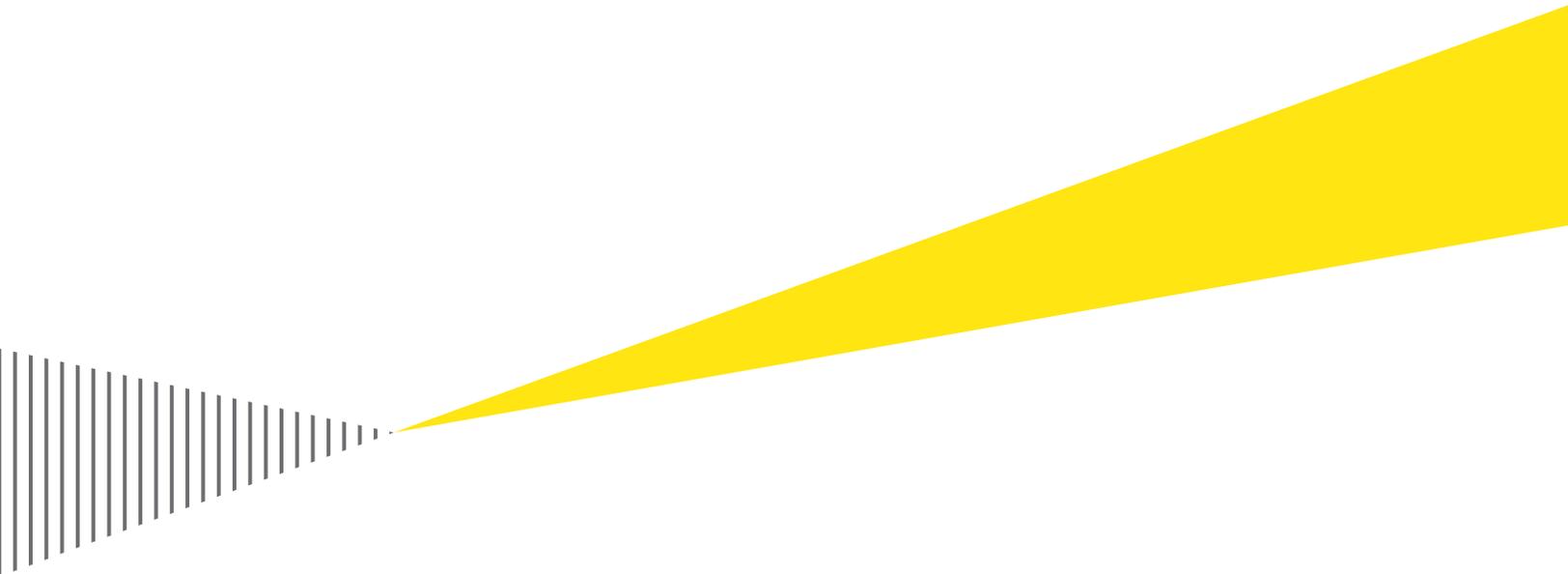
**OCHSNER CLINIC FOUNDATION GROSS REVENUE BY PAYOR  
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016**

<b>Payor Groupings</b>	<b>12/31/2016</b>	<b>12/31/2017</b>
Managed Care and Commercial	38%	36%
Medicare Managed Care	24%	24%
Medicare - Traditional	21%	21%
Medicaid	14%	17%
Other	3%	2%
<b>TOTAL</b>	<b>100%</b>	<b>100%</b>

CONSOLIDATED FINANCIAL STATEMENTS

Ochsner Clinic Foundation and Subsidiaries  
Years Ended December 31, 2017 and 2016  
With Report of Independent Auditors

Ernst & Young LLP



Ochsner Clinic Foundation and Subsidiaries

Consolidated Financial Statements

Years Ended December 31, 2017 and 2016

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## Report of Independent Auditors

The Board of Directors  
Ochsner Clinic Foundation and Subsidiaries

We have audited the accompanying consolidated financial statements of Ochsner Clinic Foundation and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of operations, changes in net assets, and 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 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 consolidated financial statements based on our audits. 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 consolidated financial statements are free from 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, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Ochsner Clinic Foundation and its subsidiaries at December 31, 2017 and 2016, and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

*Ernst + Young LLP*

April 23, 2018

Ochsner Clinic Foundation and Subsidiaries

Consolidated Balance Sheets  
(In Thousands)

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<i>(As Adjusted)</i>	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 186,401	\$ 121,569
Assets limited as to use required for current liabilities	7,370	5,600
Patient accounts receivable – net	249,299	252,598
Accounts receivable other	104,827	99,516
Inventories	68,608	56,022
Prepaid expenses and other current assets	34,395	32,972
Estimated third-party payor settlements	22,224	19,626
Total current assets	<u>673,124</u>	<u>587,903</u>
Assets limited as to use:		
By Board for capital improvements, charity, research, and other	769,717	729,436
Under bond indenture agreements	95,106	21,477
Under self-insurance trust fund	9,301	9,135
Donor-restricted long-term investments	97,425	78,433
Total assets limited as to use	<u>971,549</u>	<u>838,481</u>
Less assets limited as to use required for current liabilities	<u>(7,370)</u>	<u>(5,600)</u>
Non-current assets limited as to use	964,179	832,881
Investments in unconsolidated affiliates, real estate, and other	19,644	14,045
Property – net	927,979	821,692
Goodwill	71,195	43,558
Intangible assets	12,354	11,467
Other assets	47,332	39,293
Total assets	<u><u>\$ 2,715,807</u></u>	<u><u>\$ 2,350,839</u></u>

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<i>(As Adjusted)</i>	
<b>Liabilities and net assets</b>		
Current liabilities:		
Accounts payable	\$ 190,683	\$ 150,332
Accrued salaries, wages, and benefits	163,218	149,483
Deferred revenue	35,552	9,669
Estimated third-party payor settlements	4,275	3,769
Bonds payable – current portion	2,095	7,030
Notes payable – current	52,430	52,430
Long-term debt – current portion	13,299	15,566
Other current liabilities	33,266	30,927
Total current liabilities	494,818	419,206
Pension and postretirement obligations	147,596	166,532
Bonds payable	986,730	828,408
Long-term debt	175,722	188,693
Other long-term liabilities	38,770	36,982
Total liabilities	1,843,636	1,639,821
Commitments and contingencies <i>(Notes 5 and 17)</i>		
Net assets:		
Unrestricted	745,282	596,966
Temporarily restricted	100,206	88,219
Permanently restricted	26,683	25,833
Total net assets	872,171	711,018
Total liabilities and net assets	<u>\$ 2,715,807</u>	<u>\$ 2,350,839</u>

*See notes to financial statements.*

Ochsner Clinic Foundation and Subsidiaries

Consolidated Statements of Operations  
(In Thousands)

	<b>Year Ended December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<i>(As Adjusted)</i>	
Unrestricted revenues:		
Patient service revenue – net of contractual allowances and discounts	\$ 2,381,355	\$ 2,241,043
Provision for bad debts	(87,789)	(88,454)
Net patient service revenue, less provision for bad debts	2,293,566	2,152,589
Premium revenue	298,824	286,186
Other operating revenue	403,463	322,978
Net assets released from restrictions used for operations	6,319	6,040
Total unrestricted revenues	3,002,172	2,767,793
Expenses:		
Salaries and wages	1,359,294	1,258,517
Benefits	138,008	134,859
Medical services to outside providers	133,952	132,534
Medical supplies and services	570,155	500,792
Other operating expenses	552,756	522,155
Depreciation and amortization	128,098	115,832
Interest	49,762	52,718
Total expenses	2,932,025	2,717,407
Operating income	70,147	50,386
Non-operating gains (losses):		
Investment and other realized gains – net	47,147	7,613
Loss on early extinguishment of debt	(9,256)	(39,110)
Unrealized gains on alternative investments	32,290	10,241
Total non-operating gains (losses)	70,181	(21,256)
Excess of revenues over expenses	<u>\$ 140,328</u>	<u>\$ 29,130</u>

See notes to financial statements.

Ochsner Clinic Foundation and Subsidiaries

Consolidated Statements of Changes in Net Assets  
(In Thousands)

	<b>Year Ended December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<i>(As Adjusted)</i>	
<b>Unrestricted net assets</b>		
Excess of revenues over expenses	\$ 140,328	\$ 29,130
Net unrealized gains on investments excluding alternative investments	4,678	28,251
Net assets released from restrictions used for capital acquisitions	636	918
Pension-related changes other than net periodic pension costs	2,674	(26,449)
Increase in unrestricted net assets	<u>148,316</u>	<u>31,850</u>
<b>Temporarily restricted net assets</b>		
Contributions	13,002	25,892
Investment income	5,940	2,601
Net assets released from restrictions used for:		
Operations	(6,319)	(6,041)
Capital acquisitions	(636)	(918)
Increase in temporarily restricted net assets	<u>11,987</u>	<u>21,534</u>
<b>Permanently restricted net assets</b>		
Contributions	850	2,070
Increase in permanently restricted net assets	<u>850</u>	<u>2,070</u>
Increase in net assets	161,153	55,454
Net assets – beginning of year	711,018	655,564
Net assets – end of year	<u>\$ 872,171</u>	<u>\$ 711,018</u>

*See notes to financial statements.*

# Ochsner Clinic Foundation and Subsidiaries

## Consolidated Statements of Cash Flows (In Thousands)

	<b>Year Ended December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<i>(As Adjusted)</i>	
<b>Operating activities</b>		
Increase in net assets	\$ 161,153	\$ 55,454
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Pension-related changes other than net periodic pension costs	(2,674)	26,449
Depreciation and amortization	128,098	115,832
Provision for bad debts	87,789	88,454
Non-cash portion of loss on early extinguishment of debt	8,793	3,196
Amortization of deferred financing costs and debt premiums and discounts	(591)	498
Income (loss) from equity-method investments, net of cash received	721	(62)
Net realized and unrealized gains on investments	(88,705)	(42,653)
Gain on contribution of property to joint venture	(195)	(6,994)
Other, net	(850)	(2,070)
Changes in operating assets and liabilities, net of acquisitions:		
Patient accounts receivable	(84,490)	(115,525)
Other current and non-current assets	(27,962)	(41,110)
Accounts payable	38,924	1,189
Accrued expenses and other liabilities	27,332	(17,475)
Net cash provided by operating activities	247,343	65,183
<b>Investing activities</b>		
Purchases of assets whose use is limited and other investments	(389,924)	(256,336)
Sales and maturities of assets whose use is limited and other investments	339,601	192,980
Capital expenditures	(228,542)	(166,159)
Acquisition of businesses, net of cash acquired	(30,816)	-
Other	313	(948)
Net cash used in investing activities	(309,368)	(230,463)
<b>Financing activities</b>		
Repayment of bonds payable and long-term debt	(323,471)	(175,183)
Proceeds from long-term borrowings	458,024	174,369
Payments of debt financing costs	(4,288)	(2,229)
Payments on capital lease obligations	(4,258)	(2,981)
Proceeds from contributions restricted for long-term investments	850	2,070
Net cash provided by (used in) financing activities	126,857	(3,954)
Net increase (decrease) in cash and cash equivalents	64,832	(169,234)
Cash and cash equivalents – beginning of year	121,569	290,803
Cash and cash equivalents – end of year	\$ 186,401	\$ 121,569

*See notes to financial statements.*

# Ochsner Clinic Foundation and Subsidiaries

## Notes to Consolidated Financial Statements

December 31, 2017

### **1. Summary of Significant Accounting Policies**

#### **Organization**

Ochsner Clinic Foundation (OCF or Ochsner) d/b/a Ochsner Health System (OHS), located in New Orleans, Louisiana, is a not-for-profit institution that, either directly or through its fully owned subsidiaries, owns and operates an acute care hospital known as Ochsner Medical Center (OMC), an 11-story clinic building, a 143-room hotel, and related medical facilities located on a main campus in Jefferson Parish at the western end of New Orleans. OCF also owns 100% of the outstanding common stock of Ochsner System Protection Company (OSPC), a captive insurance company domiciled in Louisiana. OCF owns Ochsner Medical Center West Bank and Ochsner Baptist Medical Center, which are operated as remote campuses of OMC. It also owns and operates health centers throughout southeast Louisiana; owns a hospital in Baton Rouge, Louisiana, that operates as Ochsner Medical Center Baton Rouge; owns a hospital in Slidell, Louisiana, that operates as Ochsner Medical Center – North Shore; owns a hospital in Kenner, Louisiana, that operates as Ochsner Medical Center – Kenner; operates a hospital in Raceland, Louisiana, known as Ochsner St. Anne General Hospital; and owns several fitness centers that operate as Ochsner Fitness Center. OCF also provides management assistance and support for a hospital in Houma, Louisiana, known as Leonard J. Chabert Medical Center (Chabert); for a hospital in Luling, Louisiana, known as St. Charles Parish Hospital (SCPH); for a hospital in Chalmette, Louisiana, known as St. Bernard Parish Hospital (SBPH); and for a hospital in Bay St. Louis, Mississippi, known as Hancock Medical Center (Hancock).

# Ochsner Clinic Foundation and Subsidiaries

## Notes to Consolidated Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

Prior to December 31, 2017, OHS was a not-for-profit, non-stock membership corporation and the parent company of OCF. Effective December 31, 2017, OHS was merged with and into OCF, with OCF as the surviving entity. Ochsner Clinic Foundation still operates under the trade name of Ochsner Health System. As a result of the merger, the 2016 OCF consolidated financial statements presented as prior year information in the 2017 consolidated financial statements mirror the amounts originally presented in the 2016 OHS consolidated financial statements. The amounts below display the changes compared to the 2016 OCF consolidated audit report (in thousands):

	<b>Year Ended</b>	
	<b>December 31, 2016</b>	
	<b>OCF as</b>	<b>OCF as</b>
	<b>Originally</b>	<b>OCF as</b>
	<b>Reported</b>	<b>Adjusted</b>
Total assets	\$ 2,303,785	\$ 2,350,839
Total liabilities	1,575,767	1,639,821
Total net assets	728,018	711,018
Total unrestricted revenues	2,814,370	2,767,793
Total operating expenses	2,756,973	2,717,407
Total operating income	57,397	50,386
Excess of revenues over expenses	36,139	29,130

### Basis of Presentation and Principles of Consolidation

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP). The consolidated financial statements include the accounts of Ochsner and its wholly owned subsidiaries.

All intercompany accounts and transactions have been eliminated upon consolidation. The assets of any member of the consolidated group may not be available to meet the obligations of other members in the group, except as disclosed in Notes 7, 8, and 9.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Use of Estimates

The preparation of the 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 at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

##### Cash and Cash Equivalents

Cash and cash equivalents include investments with a maturity of three months or less when purchased, excluding amounts whose use is limited by board designation, under bond indenture agreements, or under self-insurance agreements.

##### Inventories

Inventories are stated at the lower of first-in, first-out cost or market value.

##### Pledges Receivable

Unconditional promises to give are recognized as revenues at their fair values in the period received. Pledges receivable are recorded net of necessary discounts and allowances. The current portion of pledges receivable is recorded in accounts receivable other and the non-current portion is recorded in other assets in the consolidated balance sheets.

Pledges receivable as of December 31 are expected to be realized as follows (in thousands):

	<u>2017</u>	<u>2016</u>
In one year or less	\$ 7,772	\$ 11,302
Between one and five years	22,103	13,217
Greater than five years	7,519	11,761
	<u>37,394</u>	<u>36,280</u>
Less discount (ranging from 0.72%–4.25% at December 31, 2017 and 2016) and allowance for uncollectible pledges	<u>(3,270)</u>	<u>(2,478)</u>
Pledges receivable – net	<u>\$ 34,124</u>	<u>\$ 33,802</u>

# Ochsner Clinic Foundation and Subsidiaries

## Notes to Consolidated Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### Investments

Investments held by Ochsner are included in assets limited as to use in the consolidated balance sheets. Substantially all of Ochsner's investments are designated as other-than-trading investments. Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheets. Investments also include investments in private equity funds, hedge funds, real estate funds, offshore fund vehicles, and funds of funds structured as limited liability corporations or partnerships or trusts. These investments are termed alternative investments in the notes to the consolidated financial statements and are accounted for under the equity method, which approximates fair value. These funds invest in certain types of financial instruments, including, among others, futures and forward contracts, options, and securities sold not yet purchased, intended to hedge against changes in the market value of investments. These financial instruments, which involve varying degrees of risk, may result in loss due to changes in the market (market risk).

Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in excess of revenues over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments, other than alternative investments, are excluded from excess of revenues over expenses. If management believes a decline in the value of a particular investment is temporary, the decline is included in change in net unrealized gains (losses) excluding alternative investments on the consolidated statements of changes in net assets.

If the decline is evaluated as being other than temporary, the carrying value of the investment is written down and an impairment loss is recorded in non-operating gains and losses in the consolidated statements of operations. Ochsner did not record impairment losses on investment securities for the year ended December 31, 2017. Ochsner recorded impairment losses on investment securities of approximately \$1.6 million for the year ended December 31, 2016.

#### Assets Limited as to Use

Assets limited as to use primarily include assets held by trustees under indenture agreements, self-insurance trust agreements, investments restricted by donors, and designated assets set aside by the Board of Trustees (the Board) primarily for future capital improvements, over which the Board retains control and may, at its discretion, subsequently use for other purposes. Amounts required to meet current liabilities have been classified in the consolidated balance sheets as current assets.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Property – Net

Property improvements and additions are recorded at cost and capitalized and depreciated on the straight-line basis over the following estimated useful lives of the assets:

	<u>Years</u>
Land improvements	5–25
Buildings and building improvements	10–40
Leasehold improvements	12–20
Equipment, furniture, and fixtures	2–20

##### Impairment of Long-Lived Assets

Ochsner evaluates the carrying value of long-lived assets to be held and used when events and circumstances warrant such a review. The carrying value of a long-lived asset is considered impaired when the anticipated undiscounted cash flow from such asset is separately identifiable and is less than its carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair value of the long-lived asset. Fair value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved. There were no impairment charges on long-lived assets recognized for the years ended December 31, 2017 or 2016.

##### Capitalization of Interest

Ochsner capitalizes interest expense on qualifying construction-in-progress expenditures based on an imputed interest rate estimating Ochsner's average cost of borrowed funds. Such capitalized interest becomes part of the cost of the related asset and is depreciated over its estimated useful life. Capitalized interest costs totaled approximately \$4.6 million and \$2.2 million for the years ended December 31, 2017 and 2016, respectively.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 1. Summary of Significant Accounting Policies (continued)

##### Goodwill and Intangible Assets

Goodwill and intangible assets, consisting primarily of trade name and employment contracts, were recorded mainly as a result of the merger of Alton Ochsner Medical Foundation with Ochsner Clinic LLC in 2001, which resulted in the creation of OCF. Goodwill represents the excess of the fair value of the consideration conveyed in the acquisition over the fair value of net assets acquired. Goodwill and indefinite-lived intangible assets arising from business combinations are not amortized, but rather are tested for impairment at least annually at the reporting unit level. Impairment is the condition that exists when the carrying amount of goodwill or intangible assets exceeds its implied fair value. Additional impairment assessments may be performed on an interim basis if OCF encounters events or changes in circumstances that would indicate that it is more likely than not that the carrying value of goodwill or intangible assets has been impaired. OCF has selected October 31 as its annual testing date and has determined that its reporting unit is the consolidated entity.

For purposes of the October 31, 2017 and 2016 annual impairment tests, OCF applied the optional provisions of Accounting Standards Update (ASU) No. 2011-08, *Intangibles – Goodwill and Other (Topic 350): Testing Goodwill for Impairment*, which provides for a qualitative impairment analysis. A qualitative impairment analysis concluded that it was more likely than not that the fair value exceeded the carrying value of the applicable reporting units. Therefore, the two-step impairment analysis was not required, and no impairment charge was recorded as of the October 31, 2017 or 2016 annual impairment tests.

Due to the merger of OHS with and into OCF, OCF performed an additional quantitative impairment assessment as of December 31, 2017. The first step in the impairment process is to estimate the fair value of the reporting unit and then compare it to the carrying value, including goodwill. If the fair value exceeds the carrying value, no further action is required and no impairment loss is recognized. OCF determined that the use of the income and market approaches were the most appropriate methods of measuring fair value of the reporting units. These are considered Level 3 valuations in the valuation hierarchy described in Note 2.

Under the income approach, fair value is estimated using a discounted cash flow analysis. Under the market approach, fair value is estimated using a guideline company method and a comparable transaction method. Both the income approach and the market approach require significant assumptions to determine the fair value of each reporting unit. The significant assumptions used

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

in the income approach include estimates of future revenues, profits, capital expenditures, working capital requirements, operating plans, industry data, and an appropriate discount rate for each reporting unit. The significant assumptions used in the market approach include the determination of appropriate market comparables and estimated multiples of net revenue and earnings before interest, taxes, depreciation, and amortization. OCF engaged a third-party valuation firm to assist in these fair value calculations. OCF performed Step 1 of the impairment test using a quantitative impairment analysis as of December 31, 2017, and concluded the fair value exceeded the carrying value, and no further action was required.

#### **Deferred Revenue**

Ochsner engages in research activities funded by contracts from U.S. Government agencies and other private sources. Revenue related to grants and contracts is recognized as the related costs are incurred. Amounts received from grant and contract sponsors for which Ochsner has not yet fulfilled its obligations are included in deferred revenue in the accompanying consolidated balance sheets and recognized in future periods once the obligations have been satisfied.

Deferred revenue also includes amounts related to Medicaid supplemental payments which are yet to be recognized as revenue, as well as payments received in advance of services rendered for Ochsner's electronic health records (EHR) services agreements (see Note 14).

In June 2017, Ochsner entered into a series of agreements with a third-party vendor for the construction, installation, and management of energy facilities used to process and distribute chilled water and steam at OMC. Under the terms of a concession agreement, the third-party vendor obtained the right to use, control, and manage the energy assets and associated building space. Ochsner, in turn, purchases chilled water and steam generated from the third-party vendor. As part of the concession agreement, Ochsner received a payment of approximately \$20.9 million from the third-party vendor. Ochsner recorded this payment as deferred revenue within the consolidated balance sheets. The associated revenue is being amortized and recognized over the life of the agreement and is included in other operating revenue in the accompanying consolidated statements of operations.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

##### **Deferred Financing Costs**

In connection with the issuance of bonds and long-term debt, certain financing costs are being amortized over the respective lives of the bonds and long-term debt. These costs are approximately \$12.3 million and \$11.5 million net of accumulated amortization at December 31, 2017 and 2016, respectively, and are included as a reduction to bonds payable and long-term debt in the accompanying consolidated balance sheets.

##### **Derivative Financial Instruments**

Ochsner utilizes interest rate swap agreements to manage its interest rate exposure. Changes in the fair value of Ochsner's swaps not designated as hedges are recorded as non-operating gains and losses in the consolidated statements of operations. Changes in the fair value of Ochsner's swaps that are designated as hedges are recorded as changes in unrestricted net assets in the consolidated statements of changes in net assets.

##### **Estimated Workers' Compensation, Professional and General Liability, and Employee Health Claims**

Ochsner is self-insured for workers' compensation, professional and general liability, and employee health claims. The provisions for estimated workers' compensation, professional liability, and employee health claims include estimates for the ultimate costs for both reported claims and claims incurred but not reported. These estimates incorporate Ochsner's past experience, as well as other considerations, including the nature of claims, industry data, relevant trends, and the use of actuarial information.

##### **Accounting for Pension and Other Postretirement Plans**

Ochsner recognizes the overfunded or underfunded status of its pension and other postretirement plans as an asset or liability in its consolidated balance sheets. Changes in the funded status of the pension and other postretirement plans are reported as a change in unrestricted net assets presented below the excess of revenues over expenses financial statement line item in the consolidated statement of changes in net assets in the year in which the changes occur.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

##### **Reinsurance**

OSPC relies on reinsurance to limit its retained property insurance risk. In entering into reinsurance agreements, management considers a variety of factors, including the creditworthiness of reinsurers. In preparing its financial statements, management makes estimates of amounts receivable from reinsurers, which includes consideration of amounts, if any, estimated to be uncollectible by management based on an assessment of factors including an assessment of the creditworthiness of the reinsurers. OSPC cedes 100% of the underlying risk, and as a result, OSPC retains no insurance risk. However, OSPC is not relieved of its primary obligation and is subject to credit risk of its reinsurers. OSPC's last reinsurance contract ended on May 31, 2014. Its expiration coincided with the expiration of the last policy written by OSPC.

##### **Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are those whose use by Ochsner has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by Ochsner in perpetuity.

##### **Consolidated Statements of Operations**

For purposes of presentation, all revenues and expenses are reported as operating except for investment income, the loss from early extinguishment of debt, and other gains and losses – net, which are reported as non-operating.

##### **Excess of Revenues Over Expenses**

The consolidated statements of operations include excess of revenues over expenses, which represents Ochsner's performance indicator. Changes in unrestricted net assets, which are excluded from excess of revenues over expenses, consistent with industry practice, include unrealized gains and losses on other-than-trading investments, contributions used to acquire property and equipment, and pension-related changes other than net periodic pension costs.

# Ochsner Clinic Foundation and Subsidiaries

## Notes to Consolidated Financial Statements (continued)

### **1. Summary of Significant Accounting Policies (continued)**

#### **Net Patient Service Revenue**

Net patient service revenue is recognized as services are performed and is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Amounts Ochsner receives for treatment of patients covered by governmental programs such as Medicare and Medicaid and other third-party payors such as health maintenance organizations, preferred provider organizations, and other private insurers are generally less than Ochsner's established billing rates. Additionally, to provide for accounts receivable that could become uncollectible in the future, Ochsner establishes an allowance for doubtful accounts to reduce the carrying value of such receivables to their estimated net realizable value. Third-party accounts are pursued until all payments and adjustments are posted to the patient account. For those accounts with a patient balance after third-party liability is finalized or accounts for uninsured patients, the patient receives statements and collection letters. Patients who express an inability to pay are reviewed for potential sources of financial assistance, including Ochsner's charity care policy. If the patient is deemed unwilling to pay, the account is written off as bad debt and transferred to an outside collection agency for additional collection efforts.

Accordingly, the revenues and accounts receivable reported in Ochsner's consolidated financial statements are recorded at the net amount expected to be received. Retroactively calculated contractual adjustments arising under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and are adjusted as final settlements are determined.

During the current year, Ochsner determined that approximately \$44.4 million was recognized in 2016 as net patient service revenues and offsetting benefits expenses related to Ochsner's self-insured employees, which should have been eliminated in consolidation. Management evaluated the impact of the adjustment, which had no impact to operating income or excess of revenues over expenses, and determined that the amount was immaterial to the consolidated financial statements. As such, the prior year amounts have been adjusted to conform with the current year presentation.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

##### *Charity Care*

Ochsner provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Records of charges foregone for services and supplies furnished under the charity care policy are maintained to identify and monitor the level of charity care provided. Because Ochsner does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Ochsner estimates its costs of care provided under its charity care programs by applying a ratio of direct and indirect costs to charges to the gross foregone charges associated with providing care to charity patients. Ochsner's gross charity care charges include only services provided to patients who are unable to pay and qualify under Ochsner's charity care policies. The ratio of cost to charges is calculated based on Ochsner's total expenses divided by gross patient revenue. During the years ended December 31, 2017 and 2016, the estimated costs incurred by Ochsner to provide care to patients who met certain criteria under its charity care policy were approximately \$29.2 million and \$42.2 million, respectively.

##### *Community Benefit*

Since December 2010, Ochsner and four other health care providers have formed nonprofit organizations with the purpose to create a vehicle to provide services to low-income and needy patients. Expenditures recorded by Ochsner to fund the organizations for the years ended December 31, 2017 and 2016, were approximately \$28.4 million and \$40.7 million, respectively, and are included in other operating expenses in the consolidated statements of operations.

##### *Provision and Allowance for Doubtful Accounts*

To provide for accounts receivable that could become uncollectible in the future, Ochsner establishes an allowance for doubtful accounts to reduce the carrying value of such receivables to their estimated net realizable value. The primary uncertainty lies with uninsured patient receivables and deductibles, co-payments, or other amounts due from individual patients. Payment pressure from managed care/indemnity payors also affects Ochsner's provision for doubtful accounts.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

There are various factors that can impact collection trends, such as changes in the economy, which in turn have an impact on unemployment rates and the number of uninsured and underinsured patients, the volume of patients through Ochsner's emergency departments, the increased burden of co-payments and deductibles to be made by patients with insurance, and business practices related to collection efforts. These factors continuously change and can have an impact on collection trends and the estimation process.

Ochsner has an established process to determine the adequacy of the allowance for doubtful accounts that relies on a number of analytical tools and benchmarks to arrive at a reasonable allowance. No single statistic or measurement determines the adequacy of the allowance for doubtful accounts. Some of the analytical tools that Ochsner utilizes include, but are not limited to, historical cash collection experience, revenue trends by payor classification, and revenue days in accounts receivable. Accounts receivable are written-off after collection efforts have been followed in accordance with Ochsner's policies.

#### **Other Operating Revenue**

Other operating revenue includes pharmacy revenue, rental revenue, durable medical equipment rentals and sales, gift shop revenues, EHR incentive payments, revenue from joint operating agreements and management agreements, income from equity-method investees, fitness center revenue, hotel revenue, and revenues from other miscellaneous sources.

#### **HIT Incentive Payments and Other Benefits**

Beginning in 2012, Ochsner achieved compliance with certain of the health information technology (HIT) requirements under the American Recovery and Reinvestment Act of 2009. As a result, Ochsner recognized approximately \$4.3 million and \$9.4 million in other operating revenue in the accompanying consolidated statements of operations for 2017 and 2016, respectively, for EHR incentives related to Medicaid and Medicare programs. These incentives partially offset the operating expenses Ochsner has incurred and continues to incur from its investment in HIT systems. Ochsner did not have any accounts receivable related to these incentives at December 31, 2017. At December 31, 2016, Ochsner had approximately \$0.6 million included in accounts receivable other in the accompanying consolidated balance sheet related to these incentives. Ochsner accounts for EHR incentive payments under the grant accounting model as grants related to income.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

Medicare and Medicaid EHR incentive payments are recognized as revenue after Ochsner has determined it is reasonably assured to comply with the meaningful use criteria over the entire applicable compliance period. Ochsner's compliance with the meaningful use criteria is subject to audit by the federal government.

#### **Donor-Restricted Gifts**

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, which is then treated as cost. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Contributions for which restrictions are met in the same period in which the unconditional promise to give is received are recorded as unrestricted revenue.

#### **Fair Value of Financial Instruments Other Than Investments**

The following methods and assumptions were used by Ochsner in estimating the fair value of its financial instruments:

##### *Current Assets and Liabilities*

Ochsner considers the carrying amounts of financial instruments classified as current assets and liabilities to be a reasonable estimate of their fair values.

##### *Bonds Payable*

The fair values of Ochsner's revenue bonds are based on currently traded values of similar financial instruments as disclosed in Note 8.

##### *Notes Payable and Long-Term Debt*

Ochsner considers the carrying value of its notes payable and long-term debt to approximate fair value at December 31, 2017, due to the variable nature of the interest rate or based on a comparison of its fixed rates to current market rates.

# Ochsner Clinic Foundation and Subsidiaries

## Notes to Consolidated Financial Statements (continued)

### 1. Summary of Significant Accounting Policies (continued)

#### Income Taxes

Ochsner and its subsidiaries qualify as tax-exempt organizations under Section 501(a) and are described in Section 501(c)(3) of the Internal Revenue Code and are exempt from federal and state income taxes. Management annually reviews its tax positions and has determined that there are no material uncertain tax positions that require recognition in the accompanying consolidated balance sheets. The statute of limitations remains open for tax years 2014 through 2017 in Ochsner's main tax jurisdictions. The Tax Cuts and Jobs Act (Act) was enacted on December 22, 2017. The Act reduces the U.S. federal corporate tax rate from 35% to 21%, requires companies to pay a one-time transition tax on earnings of certain foreign subsidiaries that was previously tax deferred and creates new taxes on certain foreign sourced earnings. For tax-exempt entities, the Act also requires organizations to categorize certain fringe benefit expenses as a source of unrelated business income, pay an excise tax on remuneration above certain thresholds that is paid to executives by the organization, and report income or loss from unrelated business activities on an activity-by-activity basis, among other provisions. Certain regulatory guidance provides for a measurement period of up to one year during which the accounting for the tax effects of the Act may be completed. Ochsner may record further adjustments in future periods upon obtaining, preparing, or analyzing additional information about facts and circumstances that existed as of the date of enactment that would have affected the income tax effects initially reported. Ochsner will continue to revise and refine the calculations as additional IRS guidance is issued.

#### Concentration of Credit Risk

Ochsner grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements.

#### Risks and Uncertainties

Ochsner's business could be impacted by continuing price pressure on new and renewal business, Ochsner's ability to effectively control health care costs, additional competitors entering Ochsner's markets, and federal and state legislation in the area of health care reform. Changes in these areas could adversely impact its operations in the future.

#### Reclassification

Certain prior year amounts have been reclassified to conform to the 2017 presentation. These reclassifications had no impact on total assets, liabilities, or changes in net assets.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

##### **New Accounting Pronouncements**

In May 2015, the FASB issued ASU 2015-07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. Accounting Standards Codification Topic (ASC) 820, *Fair Value Measurement*, permits a reporting entity, as a practical expedient, to measure the fair value of certain investments using the net asset value per share of the investment. ASU 2015-07 removes the requirement to categorize investments within the fair value hierarchy for which fair values are measured using the net asset value per share practical expedient. It also limits disclosures to investments for which the entity has elected to measure the fair value using the practical expedient. Ochsner adopted the provisions of ASU 2015-07 effective January 1, 2017. The adoption resulted in disclosure changes as discussed in Note 10.

##### **Pending Accounting Pronouncements**

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU 2014-09 provides for a single comprehensive principles-based standard for the recognition of revenue across all industries through the application of the following five-step process:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

Among other provisions and in addition to expanded disclosure about the nature, amount, timing, and uncertainty of revenue, as well as certain additional quantitative and qualitative disclosures, ASU 2014-09 changes the health care industry specific presentation guidance under ASU 2011-07, *Health Care Entities (Topic 954): Presentation and Disclosure of Patient Service Revenue, Provision for Bad Debts, and the Allowance for Doubtful Accounts for Certain Health Care Entities*. The provisions of ASU 2014-09 were effective for OHS starting January 1, 2018, including interim periods within that reporting period. Early application is permitted only for annual periods beginning after December 15, 2016, including interim periods within that reporting period.

Ochsner has evaluated the requirements of ASU 2014-09 to ensure that processes, systems, and internal controls are in place to collect the necessary information to implement the standard effective January 1, 2018. Ochsner is also in the process of drafting the new disclosures required post-implementation. Ochsner used a full retrospective method of application to adopt ASU 2014-09 on January 1, 2018. For patient service revenue, net of contractual allowances and discounts, Ochsner used a portfolio approach to apply the new model to classes of payors with similar characteristics based on historical payment trends. For other operating revenue, Ochsner reviewed the revenue streams within this category and analyzed contracts for material classes of transactions to determine the application of the revenue recognition criteria.

Adoption of ASU 2014-09 will result in changes to Ochsner's presentation and disclosure of revenue related to uninsured or underinsured patients. Prior to the adoption of ASU 2014-09, a significant portion of Ochsner's provision for doubtful accounts related to self-pay patients, as well as co-pays and deductibles owed to Ochsner by patients with insurance in patient service revenue, net of contractual allowances and discounts. Under ASU 2014-09, the estimated uncollectible amounts due from these patients are generally considered a direct reduction to net operating revenues and, correspondingly, result in a material reduction in the amounts presented separately as provision for doubtful accounts.

Ochsner also assessed the impact of the new standard on various reimbursement programs that represent variable consideration, including settlements with third-party payors, disproportionate share payments, supplemental state Medicaid programs, and other reimbursement programs in which Ochsner hospitals participate. Industry guidance is continuing to develop around these issues, and any conclusions in the final industry guidance that is inconsistent with Ochsner's application could result in changes to Ochsner's expectations regarding the impact that this new

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 1. Summary of Significant Accounting Policies (continued)

accounting standard could have on Ochsner's financial statements. If changes were to be warranted, quarterly reporting might be impacted, but we do not believe it would have a significant impact on Ochsner's financial position. Final drafts of industry guidance on these and other reimbursement programs unique to the health care industry are expected later in 2018. Ochsner is monitoring the development of such guidance.

While the adoption of ASU 2014-09 will change the presentation of net operating revenues in Ochsner's consolidated statements of operations and will impact certain disclosures, it will not materially impact its consolidated financial position, results of operations, or cash flows. There was no cumulative effect of a change in accounting principle recorded related to the adoption of ASU 2014-09 on January 1, 2018.

In January 2016, the FASB issued ASU 2016-01, *Financial Instrument – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01 requires that investments in equity securities, and other ownership interests in an entity that do not result in consolidation and are not accounted for under the equity method, be measured at fair value at the end of each reporting period, and the resulting changes in fair value be recognized in excess of revenues over expenses. Ochsner will no longer be able to recognize unrealized holding gains and losses on equity securities it classifies today as available for sale in other changes in unrestricted net assets. The provisions of ASU 2016-01 are effective for Ochsner starting January 1, 2018, including interim periods within that reporting period. The adoption of ASU 2016-01 will result in a reclassification of unrealized holding gains and losses on equity securities from other changes in unrestricted net assets to excess of revenues over expenses.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. ASU 2016-02 requires companies that lease assets to recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, in its balance sheet. The pronouncement will also require additional disclosures about the amount, timing, and uncertainty of cash flows arising from leases. The provisions of ASU 2016-02 are effective for Ochsner starting January 1, 2019, including interim periods within that reporting period, and early adoption is permitted. Management is currently evaluating the impact of this pronouncement on OHS' consolidated financial statements.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **1. Summary of Significant Accounting Policies (continued)**

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. Under the new standard, the presentation of financial information for not-for-profits, specifically with respect to liquidity, financial performance, and cash flows, will be simplified and provide more relevant information to donors, grantors, creditors, and other users. This includes areas such as net asset classification, investment return, expenses, liquidity and availability of resources, and a change in the presentation of operating cash flows. The provisions of ASU 2016-14 were effective for Ochsner for the fiscal year starting January 1, 2018, and for interim periods starting January 1, 2019, and early adoption is permitted. Management is currently evaluating the impact of this pronouncement on Ochsner's consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, which is intended to reduce diversity in practice on how certain transactions are classified in the statement of cash flows. The new standard addresses eight issues: debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments; 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 investments; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. The provisions of ASU 2016-15 are effective for Ochsner starting January 1, 2018, including interim periods within that reporting period, and early adoption is permitted. Management is currently evaluating the impact of this pronouncement on Ochsner's consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. The amendments in ASU 2017-07 require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. It also requires the other components of net periodic pension cost and net periodic postretirement benefit cost to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations. The provisions of ASU 2017-07 are effective for Ochsner starting January 1, 2019, including interim periods within that reporting period, and early adoption is permitted. Management is currently evaluating the impact of this pronouncement on Ochsner's consolidated financial statements.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **2. Assets Limited as to Use and Related Fair Value Measurements and Disclosures**

Accounting Standards Codification (ASC) 820, *Fair Value Measurement*, establishes a common definition for fair value to be applied to U.S. GAAP requiring use of fair value, establishes a framework for measuring fair value, and expands disclosures about such fair value measurements. ASC 820 establishes a hierarchy for ranking the quality and reliability of the information used to determine fair values. ASC 820 requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

*Level 1* – Unadjusted quoted market prices in active markets for identical assets or liabilities.

*Level 2* – Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices are observable for the asset or liability.

*Level 3* – Unobservable inputs for the asset or liability.

Ochsner endeavors to utilize the best available information in measuring fair value. Financial assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurement. Transfers into and transfers out of the hierarchy levels are recognized as if they had taken place at the end of the reporting period. In the year ended December 31, 2017, a publicly-traded security was de-listed; therefore, at December 31, 2017, this is accounted for as an alternative investment and is not included in the fair value tables below. There were no transfers between Level 1 and Level 2 in the year ended December 31, 2016.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**2. Assets Limited as to Use and Related Fair Value Measurements and Disclosures  
(continued)**

**Assets and Liabilities Measured at Fair Value**

*Recurring Fair Value Measurements*

The fair values of assets measured at estimated fair value on a recurring basis are estimated as described in the preceding section. These estimated fair values and their corresponding fair value hierarchy in accordance with ASC 820 are summarized as follows (in thousands):

	<b>Fair Value Measurements at Reporting Date Using</b>			
	<b>Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)<sup>(a)</sup></b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	<b>Total Estimated Fair Value</b>
<b>December 31, 2017</b>				
Money market funds	\$ 113,938	\$ –	\$ –	\$ 113,938
Fixed income investments	264,626	–	–	264,626
Marketable equity securities	126,981	–	–	126,981
Diversifiers	101,232	–	–	101,232
Natural resources and other	34,139	–	–	34,139
<b>Total</b>	<b>\$ 640,916</b>	<b>\$ –</b>	<b>\$ –</b>	<b>\$ 640,916</b>
<b>December 31, 2016</b>				
Money market funds	\$ 58,464	\$ –	\$ –	\$ 58,464
Fixed income investments	244,057	–	–	244,057
Marketable equity securities	166,667	–	–	166,667
Diversifiers	69,344	–	–	69,344
Natural resources and other	31,345	–	–	31,345
<b>Total</b>	<b>\$ 569,877</b>	<b>\$ –</b>	<b>\$ –</b>	<b>\$ 569,877</b>

<sup>(a)</sup> Valuation of these securities classified as Level 1 is based on unadjusted quoted prices in active markets that are readily and regularly available. Investments classified as Level 1 include mutual funds that are publicly traded.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **2. Assets Limited as to Use and Related Fair Value Measurements and Disclosures (continued)**

Alternative investments and other investments of approximately \$325.8 million and \$265.7 million at December 31, 2017 and 2016, respectively, are not included in these tables since they are accounted for using the equity method of accounting and not measured at fair value. Real estate investments of approximately \$7.6 million and \$5.7 million at December 31, 2017 and 2016, respectively, are not included in these tables since they are accounted for at cost.

Investment income and other gains and losses are classified as non-operating and comprise interest and dividend income of approximately \$17.2 million and \$11.7 million (net of expenses of approximately \$1.7 million and \$1.5 million for the years ended December 31, 2017 and 2016, respectively) and realized net gains (losses) on sales of securities of approximately \$29.9 million and \$(4.1) million for 2017 and 2016, respectively. Unrealized gains (losses) on alternative investments were approximately \$32.3 million and \$(10.2) million during 2017 and 2016, respectively. Unrealized gains (losses) on investments other than alternative investments are recorded at fair value and are included in other changes in unrestricted net assets.

#### **3. Net Patient Service Revenue**

Net patient service revenue is recognized when services are provided. Ochsner has agreements with third-party payors that provide for payments at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered.

A summary of the significant payment arrangements with major third-party payors follows:

##### **Medicare and Medicaid**

Inpatient acute care services and defined capital costs related to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Medicare inpatient rehabilitation services are also paid at prospectively determined rates per discharge, based on a patient classification system. Psychiatric services rendered to Medicare beneficiaries are reimbursed on a prospectively determined rate per day. Outpatient services to Medicare beneficiaries are paid on a prospectively determined amount per procedure. Medicare skilled nursing care is paid on a prospectively determined amount per diem based on a patient classification system. The Medicare program's share of indirect medical education costs is reimbursed based on a stipulated formula.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **3. Net Patient Service Revenue (continued)**

The Medicare program's share of direct medical education costs is reimbursed based on a prospectively determined amount per resident. Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined per diem rates. Outpatient services rendered to Medicaid program beneficiaries are reimbursed on a cost basis subject to certain limits.

Ochsner records retroactive Medicare and Medicaid settlements based upon estimates of amounts that are ultimately determined through annual cost reports filed with and audited by the fiscal intermediary. The difference between estimated and audited settlements is recorded as an adjustment to net patient service revenue in the year a determination is made. The favorable resolution of reimbursement issues under appeal by Ochsner is reported as an increase in net patient service revenue in the year the issue is resolved.

As a result of retroactive settlements of certain prior year cost reports, Ochsner recorded changes in estimates during the years ended December 31, 2017 and 2016. As a result of changes in prior year estimates, net patient service revenues increased approximately \$1.9 million and \$1.6 million in 2017 and 2016, respectively.

#### **Medicaid Supplemental Payment Program**

Since December 2010, Ochsner's hospitals and eight other hospitals (Baton Rouge General Medical Center, CHRISTUS Schumpert Health System, CHRISTUS St. Frances Cabrini Hospital, CHRISTUS St. Patrick Hospital, Lakeview Regional Medical Center, Women's & Children's Hospital, Rapides Regional Medical Center, and Tulane University Hospital and Clinic) entered into collaborations with the State and several units of local government in Louisiana (Jefferson Parish Hospital Service District No. 2, Natchitoches Hospital District No. 1, Jefferson Parish Human Services Authority, Terrebonne Parish Hospital Service District #1, Southern Regional Medical Corporation, Hospital Service District No. 3 of the Parish of Allen, The Parish Hospital Service District for the Parish of Orleans – District A, Savoy Medical Center, Hospital Service District No. 1 of Iberia Parish, St. Tammany Parish Hospital Service District No. 1, St. Tammany Parish Hospital Service District No. 2, and Vermilion Parish Hospital Service District #2) to more fully fund the Medicaid program (the Program) to ensure services remain available to low-income and needy patients in the respective communities.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **3. Net Patient Service Revenue (continued)**

These collaborations enable the governmental entities to increase support for the Uncompensated Care Cost (UCC) program for hospital services to the Medicaid and uninsured populations, the Medicaid Upper Payment Limits (UPL) programs for hospital and physician services to the Medicaid fee-for-service population, and the Full Medicaid Payment (FMP) program for physician services to the Medicaid managed care population. Each State's UCC and UPL methodology must comply with its State plan and be approved by the Centers for Medicare & Medicaid Services (CMS). Under the UCC and UPL programs, federal matching funds are not available for Medicaid payments that exceed a provider's individual UPL or UCC entitlement.

Under the FMP program, Medicaid Managed Care Organizations contracted to pay increased reimbursement for physician services that more closely aligns the reimbursement rates for the Medicaid managed care population with the equivalent total reimbursement rates for the Medicaid fee-for-service population.

In 2017 and 2016, Ochsner recognized approximately \$172.4 million and \$195.6 million, respectively, in net patient service revenue related to the Program and recorded accounts receivable of approximately \$2.2 million and \$15.1 million at December 31, 2017 and 2016, respectively. Such amounts are included in accounts receivable other in the accompanying consolidated balance sheets.

#### **Humana Inc.**

Ochsner entered into a provider contract with Humana Inc. to provide services for its commercial and senior members on a fee-for-service basis for physician services and at prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates for hospital services. Also, Ochsner provided services to approximately 35,000 senior members under a capitation contract for both physician and hospital services. Premium revenue from Humana Inc. under the capitation contract approximated \$298.8 million and \$286.2 million in 2017 and 2016, respectively, and is included in premium revenue in the accompanying consolidated statements of operations. Expenses for medical services to outside providers under the capitation contract approximated \$134.0 million and \$132.5 million in 2017 and 2016, respectively, and are included in medical services to outside providers in the accompanying consolidated statements of operations. Net revenue from Humana Inc. on a fee-for-service basis approximated \$208.5 million and \$197.7 million in 2017 and 2016, respectively, and is included in net patient service revenue in the accompanying consolidated statements of operations.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 3. Net Patient Service Revenue (continued)

##### Managed Care

Ochsner has also entered into contractual arrangements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. Inpatient and outpatient services rendered to managed care subscribers are reimbursed at prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Ochsner recognizes net patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients who are not eligible for charity care, Ochsner recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). Based on historical experience, a significant portion of Ochsner's uninsured and underinsured patients will be incapable or reluctant to pay for the services provided. Therefore, Ochsner records a significant provision for bad debts in the period the services are provided related to patient receivables and deductibles, co-payments, or other amounts due from individual patients who have been deemed unwilling to pay.

The table below shows the sources of patient service revenue (net of contractual allowances and discounts), before the provision for bad debts, for the years ended December 31 (in thousands).

	<u>2017</u>	<u>2016</u>
Government agencies	\$ 869,350	\$ 797,771
Patients	22,894	29,405
Managed care/indemnity	1,489,111	1,413,867
Patient service revenue, net of contractual allowances and discounts	<u>\$ 2,381,355</u>	<u>\$ 2,241,043</u>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**4. Patient Accounts Receivable**

At December 31, Ochsner's patient accounts receivable balances were due from the following sources (in thousands):

	<u>2017</u>	<u>2016</u>
Managed care/indemnity	\$ 199,894	\$ 186,105
Government agencies	78,572	87,735
Patients	18,005	25,330
Total	<u>296,471</u>	<u>299,170</u>
Less allowance for doubtful accounts	<u>(47,172)</u>	<u>(46,572)</u>
Patient accounts receivable – net	<u>\$ 249,299</u>	<u>\$ 252,598</u>

The allowance for doubtful accounts due from patients was 3.5% and 4.5% of the accounts receivable balance at December 31, 2017 and 2016, respectively. The allowance for doubtful accounts due from managed care/indemnity payors was 11.8% and 10.4% of the accounts receivable balance at December 31, 2017 and 2016, respectively.

A summary of activity in the allowance for doubtful accounts is as follows (in thousands):

	<u>Balance at Beginning of Year</u>	<u>Provision for Doubtful Accounts</u>	<u>Accounts Written Off, Net of Recoveries</u>	<u>Balance at End of Year</u>
Year ended December 31, 2016	\$ 52,914	\$ 88,454	\$ (94,796)	\$ 46,572
Year ended December 31, 2017	46,572	87,789	(87,189)	47,172

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 5. Property – Net

Ochsner’s investment in property at December 31 is as follows (in thousands):

	<b>2017</b>	<b>2016</b>
Land and improvements	\$ 107,014	\$ 97,599
Buildings and leasehold improvements	832,485	745,580
Equipment, furniture, and fixtures	1,142,190	1,058,700
Construction-in-progress	124,664	99,906
Total property – at cost	2,206,353	2,001,785
Less accumulated depreciation	1,278,374	1,180,093
Property – net	\$ 927,979	\$ 821,692

Depreciation and amortization expense totaled approximately \$128.1 million and \$115.8 million for the years ended December 31, 2017 and 2016, respectively.

At December 31, 2017 and 2016, Ochsner has purchase commitments totaling approximately \$105.7 million and \$87.0 million, respectively, toward additional capital expenditures.

Ochsner leases certain software and equipment under capital leases. Capital lease assets are included in equipment, furniture, and fixtures in the accompanying consolidated balance sheets as of December 31 and are as follows (in thousands):

	<b>2017</b>	<b>2016</b>
Software and equipment	\$ 26,158	\$ 23,668
Accumulated amortization	(10,322)	(7,675)
Net carrying value of capital lease assets	\$ 15,836	\$ 15,993

Amortization expense applicable to the capital lease asset is included in depreciation and amortization in the accompanying consolidated statements of operations.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 6. Goodwill and Intangible Assets

On August 31, 2001, Alton Ochsner Medical Foundation and Ochsner Clinic LLC effected a merger transaction resulting in the creation of OCF and the net assets of Ochsner Clinic LLC being acquired by Alton Ochsner Medical Foundation.

The cost to acquire Ochsner Clinic LLC was allocated to the assets acquired and liabilities assumed according to their estimated fair values. In addition, the carrying values of certain other assets and liabilities of Ochsner Clinic LLC were changed to reflect management's estimate of fair value under purchase accounting.

On May 2, 2016, Ochsner acquired 100% of the equity interest in Sculpting Center of New Orleans, LLC. As part of this transaction, Ochsner recorded approximately \$0.5 million of goodwill related to the acquisition.

On January 9, 2017, Ochsner completed the acquisition of Millennium Healthcare Management, Inc. (MHM). Approximately \$28.0 million of goodwill and approximately \$0.9 million of other intangible assets related to this acquisition are included in the December 31, 2017 balance sheet.

Amounts recorded as goodwill and other indefinite and definite-lived intangible assets as of December 31 are as follows (in thousands):

	<u>2017</u>	<u>2016</u>
Goodwill	\$ 71,195	\$ 43,558
Trade name – intangible assets	\$ 11,433	\$ 11,433
Other – intangible assets	921	34
	<u>\$ 12,354</u>	<u>\$ 11,467</u>

#### 7. Notes Payable

Ochsner has a loan agreement with a bank that provides a credit line with maximum borrowings of \$53.0 million. The line of credit currently expires on June 8, 2018. Borrowings under the arrangement are unsecured; however, Ochsner must meet certain financial covenants. Management believes Ochsner was in compliance with these covenants at December 31, 2017 and 2016. At December 31, 2017 and 2016, Ochsner had borrowings outstanding under this

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 7. Notes Payable (continued)

arrangement of approximately \$52.4 million. The interest rate on outstanding borrowings is based on the London Interbank Offered Rate (LIBOR) and, consequently, fluctuates from month to month. The rate on outstanding indebtedness under this arrangement was 2.86% and 2.12% at December 31, 2017 and 2016, respectively. All amounts are classified as current at December 31, 2017 and 2016.

#### 8. Bonds Payable

At December 31, bonds payable consisted of the following tax-exempt and taxable bonds (in thousands). The tax-exempt revenue bonds were issued by the Louisiana Public Facilities Authority (LPFA) on behalf of Ochsner. The taxable bonds were issued by Ochsner.

	<b>2017</b>	<b>2016</b>
Series 2017 tax-exempt bonds issued by the LPFA May 2017, due serially 2019–2037, then on term in 2042 and 2046, annual interest rates ranging from 4.00% to 5.00%	\$ 421,555	\$ –
Series 2016 tax-exempt bonds issued by the LPFA May 2016, due serially 2023–2036, then on term in 2041 and 2047, annual interest rates ranging from 3.00% to 5.00%	154,060	155,660
Series 2015 tax-exempt bonds issued by the LPFA August 2015, due serially 2016–2035, then on term in 2040 and 2047, annual interest rates ranging from 2.00% to 5.00%	110,775	112,815
Series 2015 taxable bonds issued June 2015, due in 2045, annual interest rate at 5.90%	252,820	252,820
Series 2007-A tax-exempt bonds issued by the LPFA September 2007, due serially 2009–2047, annual interest rates ranging from 5.00% to 5.50%	–	250,805
Series 2007-B tax-exempt bonds issued by the LPFA September 2007, due serially 2009–2047 annual interest rates ranging from 5.00% to 5.50%	–	53,445
Unamortized net bond premium	59,416	18,768
Total	998,626	844,313
Less deferred financing costs	9,801	8,875
Less current portion	2,095	7,030
Non-current portion of bonds payable	\$ 986,730	\$ 828,408

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **8. Bonds Payable (continued)**

All of the bonds included in the table above are general obligations of Ochsner. The security includes a pledge of all present and future accounts receivable of Ochsner and a mortgage of certain property.

Also, under the terms of the bond indenture, Ochsner is required to make certain deposits of principal and interest with a trustee. Such deposits are included with assets limited as to use in the consolidated financial statements. The bond indenture also places limits on the incurrence of additional borrowings by Ochsner and requires that it satisfy certain measures of financial performance as long as the bonds are outstanding. Management is not aware of any noncompliance with these requirements.

In May 2016, the Louisiana Public Facilities Authority issued tax-exempt revenue bonds in the amount of \$155.7 million under a loan agreement with Ochsner. Ochsner used the proceeds to pay the cost of refunding the Series 2011 bonds in the amount of \$150.0 million, resulting in a loss on extinguishment of approximately \$39.1 million.

In May 2017, the Louisiana Public Facilities Authority issued tax-exempt revenue bonds in the amount of \$421.6 million under a loan agreement with Ochsner. Ochsner used a portion of the proceeds to pay the cost of refunding the Series 2007-A and 2007-B bonds in the amounts of approximately \$246.6 million and \$52.7 million, respectively, resulting in a loss on extinguishment of approximately \$9.1 million. The remainder of the bonds are being used to provide funding for various Ochsner capital projects.

At December 31, 2017, scheduled repayments of principal and sinking fund installments to retire the bonds payable for the next five fiscal years are as follows (in thousands):

Years ending December 31:	
2018	\$ 2,095
2019	4,060
2020	5,590
2021	7,210
2022	7,580

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 8. Bonds Payable (continued)

The estimated fair value of the Series 2007-A tax-exempt bonds, Series 2007-B tax-exempt bonds, Series 2015 tax-exempt bonds, Series 2015 taxable bonds, Series 2016 tax-exempt bonds, and Series 2017 tax-exempt bonds as of December 31, 2017 and 2016, is approximately \$1.1 billion and \$875.9 million, respectively. This fair value is based on quoted market prices for similarly rated health care revenue bond issues, a Level 2 input.

#### 9. Long-Term Debt

A summary of long-term debt at December 31 is as follows (in thousands):

	<b>2017</b>	<b>2016</b>
Working capital note, due May 2026 (subject to six additional 5-year extensions), including accrued interest at rates varying from 1.12% to 1.80% during 2017 with a rate of 1.76% as of December 31, 2017	\$ 8,732	\$ 8,604
Note payable 4.61% Senior Secured Note, entered into March 2013, due March 2033	5,868	6,127
Note payable 5.26% Senior Secured Note, entered into December 2013, due December 2028	50,709	54,028
Promissory note entered into December 2013, due December 2020 with interest synthetically fixed at 3.97%	12,623	14,698
Note payable 5.09% Senior Secured Note, entered into July 2014, due August 2034	71,622	74,286
Promissory note entered into October 2014, due October 2021 with interest at 3.75%	17,600	19,067
Promissory note entered into September 2015, due September 2022 with interest synthetically fixed at 4.13%	24,000	27,000
Software and equipment loans, due varying dates in 2016–2019	341	3,131
Total long-term debt	191,495	206,941
Less deferred financing costs	2,470	2,658
Less unamortized discount	4	24
Less current portion	13,299	15,566
Non-current portion of long-term debt	\$ 175,722	\$ 188,693

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **9. Long-Term Debt (continued)**

##### **St. Anne**

On May 1, 2006, Ochsner entered into lease and management services agreements with Lafourche Parish Hospital Service District No. 2 (Lafourche), which owns and operates St. Anne General Hospital and related facilities (St. Anne) of Raceland, Louisiana. Under the agreements, Ochsner leases the St. Anne buildings and facilities, purchased working capital and certain equipment of St. Anne, and operates the hospital for a specified period of time. As part of the agreement, Ochsner entered into an unsecured note payable with Lafourche for the purchase of its working capital and equipment for \$7.1 million. On June 1, 2015, Ochsner and Lafourche executed an amendment in which the aggregate principal and accrued interest amount of approximately \$8.4 million was extended to 2026 with six 5-year renewal options, to coincide with the lease agreement. The interest rate on the working capital note, based on the 5-Year Yield Tax Exempt Insured Revenue Bond Rate published by Bloomberg, was 1.76% and 1.85% at December 31, 2017 and 2016, respectively. All amounts are classified as non-current at December 31, 2017 and 2016, and are included in long-term debt on the consolidated balance sheets.

##### **March 2013 Note Payable**

Pursuant to its purchase of two Medical Office Buildings on November 15, 2012, OCF entered into a loan in the principal amount of \$7.0 million on March 12, 2013. The loan is secured by first mortgage liens on medical office building properties at 1850 East Gause Boulevard (North Shore Medical Office Building 1) and 105 Medical Center Drive (North Shore Medical Office Building 2), both in Slidell, Louisiana, and both in close proximity to Ochsner Medical Center – North Shore. The loan is in the form of a Senior Secured Note bearing interest at the fixed annual rate of 4.61%. Principal and interest payments are due monthly based upon a 20-year (240-month) amortization period and actual/360-day interest period.

##### **December 2013 Note Payable**

Ochsner entered into a loan in the principal amount of \$63.0 million on December 30, 2013. The loan is secured by first mortgage liens on Ochsner facilities at 2005 Veterans Memorial Boulevard, Metairie, Louisiana, and 1950 Gause Boulevard, Slidell, Louisiana. The loan is in the form of a Senior Secured Note bearing interest at the fixed annual rate of 5.26%. Principal and interest payments are due monthly based upon a 15-year (180-month) amortization period and actual/360-day interest period.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **9. Long-Term Debt (continued)**

##### **December 2013 Promissory Note**

Ochsner entered into a loan with a financial institution (the 2013 Loan) in the principal amount of \$20.8 million on December 31, 2013. The 2013 Loan is in the form of a promissory note bearing stated interest of 30-day LIBOR plus 2.00%. The security includes a pledge of all present and future accounts receivable of Ochsner and a mortgage of certain property. Principal and interest payments are due monthly based upon a 15-year (180-month) fixed principal payment amortization period with the balance of the outstanding principal due on a 7-year maturity date of December 30, 2020, and actual/360-day interest period. As part of a program to manage interest rate risk, OHS entered into an interest rate swap agreement on December 19, 2013, effective as of December 30, 2013. Ochsner pays a 1.97% fixed interest rate on the outstanding notional amount based on the outstanding principal balance of the 2013 Loan to the counterparty and receives the floating amount of 30-day LIBOR as of the date of rate-set. The effect of the swap agreement is to fix Ochsner's interest rate on the 2013 Loan at 3.97%. At December 31, 2017, the fair value of the interest rate swap agreement was an asset of \$8,000 and is included within other assets in the consolidated balance sheet. At December 31, 2016, the fair value of the interest rate swap agreement was a liability of \$171,000, and is included in other long-term liabilities in the consolidated balance sheet.

##### **July 2014 Note Payable**

Ochsner entered into a loan in the principal amount of \$80.0 million on July 31, 2014. The loan is secured by first mortgage liens on Ochsner facilities at 17000 Medical Center Drive, Baton Rouge, Louisiana, and 16777 Medical Center Drive, Baton Rouge, Louisiana. The loan is in the form of a Senior Secured Note bearing interest at the fixed annual rate of 5.09%. Principal and interest payments are due monthly based upon a 20-year (240-month) amortization period and actual/360-day interest period.

##### **October 2014 Promissory Note**

Ochsner entered into a loan with a financial institution (the 2014 Loan) in the principal amount of \$22.0 million on October 30, 2014. The 2014 Loan is in the form of a promissory note bearing stated interest of 3.75%. The security includes a pledge of all present and future accounts receivable of Ochsner and a mortgage of certain property. Principal and interest payments are due quarterly with the first payment due on February 1, 2015, and based upon a 15-year fixed principal payment amortization period. The balance of the outstanding principal is due on a 7-year maturity date of October 31, 2021, and actual/360-day interest period.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 9. Long-Term Debt (continued)

##### September 2015 Promissory Note

Ochsner entered into a loan with a financial institution (the 2015 Loan) in the principal amount of \$30.0 million on September 30, 2015. The 2015 Loan is in the form of a promissory note bearing stated interest of 3-month LIBOR plus 2.25%. The security includes a pledge of all present and future accounts receivable of Ochsner and a mortgage of certain property. Principal and interest payments are due quarterly beginning January 1, 2016, based upon a 10-year fixed quarterly principal payment amortization period, with the balance of the outstanding principal due on a 7-year maturity date of September 30, 2022, and actual/360-day interest period. As part of a program to manage interest rate risk, OHS entered into an interest rate swap agreement on September 1, 2015, effective as of September 30, 2015. Ochsner pays a 1.88% fixed interest rate on the outstanding notional amount based on the outstanding principal balance of the 2015 Loan to the counterparty and receives the floating amount of 3-month LIBOR as of the date of rate-set. The effect of the swap agreement is to fix Ochsner's interest rate on the 2015 Loan at 4.13%. The fair value of the interest rate swap agreement was an asset of \$212,000 and \$7,000 at December 31, 2017 and 2016, respectively, and is included within other assets in the consolidated balance sheets.

At December 31, 2017, scheduled repayments of long-term debt for the next five fiscal years are as follows (in thousands):

Years ending December 31:	
2018	\$ 13,299
2019	13,616
2020	20,224
2021	23,870
2022	20,075

#### 10. Employee Benefit Plans

##### Defined Benefit Pension Plan

Certain employees of Ochsner and its subsidiaries are covered under a defined benefit pension plan (the Defined Benefit Plan). The Defined Benefit Plan is non-contributory and provides benefits that are based on the participants' credited service and average compensation during the

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 10. Employee Benefit Plans (continued)

last five years of covered employment. As of December 31, 2006, benefit accruals ceased for all plan participants under age 40 and those over age 40 who elected to freeze their retirement plan benefits. Ochsner made an additional change to the Defined Benefit Plan, and as of December 31, 2009, benefit accruals ceased for all plan participants under age 55 with less than 10 years of service (rounded to the nearest 6 months). Physician/executive participants are frozen as of December 31, 2009, regardless of age or service. Participants who were not frozen as of December 31, 2009, accrue benefits until the earlier of age 65 or December 31, 2015. No new participants are allowed to enter the Defined Benefit Plan. Ochsner makes contributions to its qualified plan that satisfy the minimum funding requirements under the Employee Retirement Income Security Act of 1974. These contributions are intended to provide not only for benefits attributed to services rendered to date but also those expected to be earned in the future.

The following table sets forth the changes in benefit obligations, changes in plan assets, and components of net periodic benefit cost (in thousands):

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
Change in benefit obligation:		
Benefit obligation – beginning of year	\$ 553,815	\$ 542,801
Service cost	–	–
Interest cost	22,477	23,619
Actuarial loss	27,296	22,379
Benefits paid	(25,662)	(34,984)
Benefit obligation – end of year	577,926	553,815
Change in plan assets:		
Fair value of plan assets – beginning of year	404,409	406,618
Actual return on plan assets	52,514	22,165
Employer contributions	15,091	10,610
Benefits paid	(25,662)	(34,984)
Fair value of plan assets – end of year	446,352	404,409
Funded status	\$ (131,574)	\$ (149,406)

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**10. Employee Benefit Plans (continued)**

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
Amounts recognized in the consolidated balance sheets consist of:		
Pension and postretirement obligations – current portion	\$           –	\$           –
Pension and postretirement obligations – non-current portion	(131,574)	(149,406)
Unrestricted net assets	N/A	N/A
Amounts recognized in unrestricted net assets:		
Net actuarial loss	251,647	253,845
Prior service credit	–	–
Total amounts recognized	<u>251,647</u>	<u>253,845</u>
Other changes in plan assets and benefit obligations recognized in unrestricted net assets:		
Net loss	5,518	32,623
Recognized loss	(7,716)	(6,840)
Recognized prior service credit	–	–
Total amounts recognized	<u>\$ (2,198)</u>	<u>\$ 25,783</u>

Weighted average assumptions used to determine projected benefit obligations at December 31 were as follows:

	<b>2017</b>	<b>2016</b>
Weighted average discount rate	3.70%	4.15%
Rate of compensation increase	N/A	N/A

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**10. Employee Benefit Plans (continued)**

Net periodic pension cost (benefit) for the years ended December 31 includes the following components (in thousands):

	<u>2017</u>	<u>2016</u>
Service cost	\$ —	\$ —
Interest cost	22,477	23,619
Expected return on plan assets	(30,735)	(32,409)
Amortization of net loss	7,716	6,840
Recognized prior service credit	—	—
Net periodic pension benefit	<u>\$ (542)</u>	<u>\$ (1,950)</u>

Weighted average assumptions used to determine net periodic pension cost for the years ended December 31 were as follows:

	<u>2017</u>	<u>2016</u>
Weighted-average discount rate	4.15%	4.35%
Expected return on plan assets	7.70%	7.70%
Rate of compensation increase	N/A	N/A

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**10. Employee Benefit Plans (continued)**

The fair values of the Defined Benefit Plan assets at December 31 are included in the tables below (in thousands).

	<b>Fair Value Measurements at Reporting Date Using</b>			
	<b>Quoted Prices in Active Markets for Observable Identical Assets and Liabilities (Level 1)<sup>(a)</sup></b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	<b>Total Estimated Fair Value</b>
<b>2017</b>				
Money market funds	\$ 22,960	\$ –	\$ –	\$ 22,960
Fixed income investments	17,649	–	–	17,649
Marketable equity securities	48,531	–	–	48,531
Absolute return	28,411	–	–	28,411
Natural resources	28,029	–	–	28,029
Total	<u>\$ 145,580</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 145,580</u>
<b>2016</b>				
Money market funds	\$ 28,126	\$ –	\$ –	\$ 28,126
Fixed income investments	16,994	–	–	16,994
Marketable equity securities	71,874	–	–	71,874
Absolute return	10,807	–	–	10,807
Natural resources	27,731	–	–	27,731
Total	<u>\$ 155,532</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 155,532</u>

<sup>(a)</sup> Valuation of these securities classified as Level 1 is based on unadjusted quoted prices in active markets that are readily and regularly available.

These tables do not include Level 2 or 3 alternative investments of \$300.8 million and \$248.9 million at December 31, 2017 and 2016, respectively, which are measured at fair value using net asset value as a practical expedient. In the year ended December 31, 2017, a publicly traded security was de-listed; therefore, at December 31, 2017, this is accounted for as an alternative investment and is not included in these tables.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 10. Employee Benefit Plans (continued)

The Defined Benefit Plan asset allocation as of the measurement dates (December 31, 2017 and 2016) and the target asset allocation, presented as a percentage of total plan assets, were as follows:

	2017	2017 Target Allocation	2016
Debt securities	13%	15%	16%
Equity securities	42	40	40
Private equity/venture capital	3	2	4
Hedge funds	27	33	25
Natural resources/REITs	10	10	8
Other	5	–	7

Asset allocations and investment performance are formally reviewed at regularly scheduled meetings several times during the year by the Investment Committee of Ochsner. Ochsner utilizes an investment consultant and multiple managers for different asset classes. The Investment Committee takes into account liquidity needs of the plan to pay benefits in the short term and the anticipated long-term obligations of the Defined Benefit Plan.

The primary financial objectives of the Defined Benefit Plan are to (1) provide a stream of relatively predictable, stable, and constant earnings in support of the Defined Benefit Plan's annual benefit obligations and (2) preserve and enhance the real (inflation-adjusted) value of the assets of the Defined Benefit Plan. The long-term investment objectives of the Defined Benefit Plan are to (1) attain the average annual total return assumed in the Defined Benefit Plan's most recent actuarial assumptions (net of investment management fees) over rolling five-year periods, (2) outperform the Defined Benefit Plan's custom benchmark, and (3) outperform the median return of a pool of retirement funds to be identified in conjunction with Ochsner's investment consultant.

The asset allocation is designed to provide a diversified mix of asset classes, including U.S. and foreign equity securities, fixed income securities, real estate investment trusts (REITs), natural resources, cash, and funds to hedge against deflation and inflation. Risk management practices include various criteria for each asset class, including measurement against several benchmarks, achievement of a positive risk-adjusted return, and investment guidelines for each class of assets that enumerate types of investment allowed in each category.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 10. Employee Benefit Plans (continued)

The Ochsner Retirement Plan Statement of Investment Policies and Objectives provides for a range of minimum and maximum investments in each asset class to allow flexibility in achieving the expected long-term rate of return. Historical return patterns and correlations, consensus return forecast, and other relevant financial factors are analyzed to check for reasonableness and appropriateness of the asset allocation to ensure that the probability of meeting actuarial assumptions is reasonable. Ochsner Treasury staff oversees the day-to-day activities involving assets of the Defined Benefit Plan and the implementation of any changes adopted by the Investment Committee.

Ochsner currently expects to make a contribution to the Defined Benefit Plan of approximately \$17.6 million in 2018.

For 2017 and 2016, Ochsner's Defined Benefit Plan had accumulated benefit obligations of approximately \$577.9 million and \$553.8 million, respectively.

The estimated net loss for the Defined Benefit Plan that will be amortized from accumulated unrestricted net assets into net periodic benefit cost over the next fiscal year is approximately \$7.7 million.

Future benefit payments expected to be paid in each of the next five fiscal years and in the aggregate for the following five years as of December 31, 2017, are as follows (in thousands):

Years ending December 31:	
2018	\$ 27,787
2019	29,347
2020	30,681
2021	31,973
2022	33,079
2023–2027	176,725
	<u>\$ 329,592</u>

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **10. Employee Benefit Plans (continued)**

##### **Defined Contribution Plans**

All employees of Ochsner meeting eligibility requirements may participate in the Ochsner Clinic Foundation 401(k) Plan (the Plan). Ochsner may annually elect to make a retirement contribution on behalf of eligible employees in an amount up to 2% of the participant's annual eligible compensation. In addition, Ochsner may annually elect to make a match for eligible employees of 50% of the first 4% the employees contribute into the Plan. At December 31, 2017 and 2016, OHS has accrued approximately \$30.2 million and \$28.1 million, respectively, for matching contributions to the Plan for the 2017 and 2016 fiscal years, respectively.

Certain Ochsner employees are also covered under a 457(f) plan. The 457(f) plan was created to replace 100% of the benefit target for employees under age 65 as of December 31, 2009, whose benefits in the Defined Benefit Plan were frozen. The participant pays taxes at vesting and payout occurs at the later of age 65 or retirement. Participants of the 457(f) plan also participate in the 401(k) contributions. OHS' accompanying consolidated balance sheets reflect a liability of approximately \$13.9 million and \$13.6 million for the 457(f) plan at December 31, 2017 and 2016, respectively.

##### **Other Postretirement Benefits**

Ochsner also provides certain health care and life insurance benefits for retired employees. Ochsner funds these benefits on a pay-as-you-go basis. The obligations under the postretirement plan are approximately \$1.6 million and \$2.0 million at December 31, 2017 and 2016, respectively.

#### **11. Endowment Funds and Temporarily and Permanently Restricted Net Assets**

Ochsner has 799 temporarily restricted funds and 70 permanently restricted funds established for a variety of purposes. These funds are classified and reported based on the existence or absence of donor-imposed restrictions. Restricted net assets include funds dedicated to Medical Education, Nursing Education, Pastoral Care, Biomedical Research, Cancer Research, Cardiology Research, Transplant Research, and Alzheimer's Research.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 11. Endowment Funds and Temporarily and Permanently Restricted Net Assets (continued)

ASC 958-205, *Not-for-Profit Entities – Presentation of Financial Statements*, provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA), which the state of Louisiana enacted on July 1, 2010.

UPMIFA requires Ochsner to classify the portion of each donor-restricted endowment fund that is not classified as permanently restricted net assets as temporarily restricted net assets (time restricted) until appropriated for expenditure. Temporarily restricted net assets available for appropriations at December 31, 2017 and 2016, total approximately \$7.8 million and \$6.8 million, respectively. Management retroactively adopted UPMIFA as of January 1, 2009.

UPMIFA also requires that Ochsner preserve the historic dollar value of the donor-restricted endowed funds. Therefore, permanently restricted net assets contain the aggregate fair market value of (1) an endowment fund at the time it became an endowment fund, (2) each subsequent donation to the fund at the time it is made, and (3) each accumulation made pursuant to a direction in the applicable gift instrument at the time the accumulation is added to the fund.

#### Restricted Net Assets as of December 31, 2017, by Purpose

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
	<i>(In Thousands)</i>		
Research	\$ 17,465	\$ 18,439	\$ 35,904
Education	6,150	3,643	9,793
Other	76,591	4,601	81,192
<b>Total</b>	<b>\$ 100,206</b>	<b>\$ 26,683</b>	<b>\$ 126,889</b>

#### Restricted Net Assets as of December 31, 2016, by Purpose

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
	<i>(In Thousands)</i>		
Research	\$ 13,402	\$ 17,671	\$ 31,073
Education	5,685	3,488	9,173
Other	69,132	4,674	73,806
<b>Total</b>	<b>\$ 88,219</b>	<b>\$ 25,833</b>	<b>\$ 114,052</b>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**11. Endowment Funds and Temporarily and Permanently Restricted Net Assets  
(continued)**

<b>Endowment Net Asset Composition by Type of Fund as of December 31, 2017</b>				
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
	<i>(In Thousands)</i>			
Donor-restricted funds	\$ –	\$ 14,563	\$ 26,683	\$ 41,246
Board-designated funds	1,559	–	–	1,559
<b>Total</b>	<b>\$ 1,559</b>	<b>\$ 14,563</b>	<b>\$ 26,683</b>	<b>\$ 42,805</b>

<b>Endowment Net Asset Composition by Type of Fund as of December 31, 2016</b>				
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
	<i>(In Thousands)</i>			
Donor-restricted funds	\$ –	\$ 10,399	\$ 25,833	\$ 36,232
Board-designated funds	1,391	–	–	1,391
<b>Total</b>	<b>\$ 1,391</b>	<b>\$ 10,399</b>	<b>\$ 25,833</b>	<b>\$ 37,623</b>

<b>Changes in Endowment Net Assets for the Year Ended December 31, 2017</b>				
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
	<i>(In Thousands)</i>			
Beginning balance	\$ 1,391	\$ 10,399	\$ 25,833	\$ 37,623
Investment gain	194	5,030	16	5,240
Contributions	–	–	835	835
Appropriations for expenditures	(26)	(866)	(1)	(893)
<b>Ending balance</b>	<b>\$ 1,559</b>	<b>\$ 14,563</b>	<b>\$ 26,683</b>	<b>\$ 42,805</b>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**11. Endowment Funds and Temporarily and Permanently Restricted Net Assets  
(continued)**

<b>Changes in Endowment Net Assets for the Year Ended December 31, 2016</b>				
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
	<i>(In Thousands)</i>			
Beginning balance	\$ 1,341	\$ 8,668	\$ 23,763	\$ 33,772
Investment gain	87	2,300	8	2,395
Contributions	–	5	2,042	2,047
Appropriations for expenditures	(37)	(554)	–	(591)
Transfers	–	(20)	20	–
Ending balance	<u>\$ 1,391</u>	<u>\$ 10,399</u>	<u>\$ 25,833</u>	<u>\$ 37,623</u>

**Funds With Deficiencies**

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 current law requires Ochsner to retain as a fund of perpetual duration. In accordance with U.S. GAAP, deficiencies of this nature are reported in unrestricted net assets. There were no such deficiencies as of December 31, 2017 or 2016.

**Return Objectives and Risk Parameters**

Ochsner has investment and spending practices for endowment assets that intend to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that Ochsner must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. The policy allows the endowment assets to be invested in a manner that is intended to produce results that exceed the price and yield results of the allocation index while assuming a moderate level of investment risk. Ochsner expects its endowment funds to provide a rate of return that preserves the gift and generates earnings to achieve the endowment purpose.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **11. Endowment Funds and Temporarily and Permanently Restricted Net Assets (continued)**

##### **Strategies Employed for Achieving Objectives**

To satisfy its long-term rate-of-return objectives, Ochsner relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and interest and dividend income. Ochsner uses a diversified asset allocation to achieve its long-term return objectives within prudent risk constraints to preserve capital.

##### **Spending Policy and How the Investment Objectives Relate to Spending Policy**

It is Ochsner's objective to establish a payout rate from endowment accounts that provides a stable, predictable level of spending for the endowed purposes that will increase with the rate of inflation, and to continue to invest in accordance with policy goals of providing for a rate of growth in the endowment earnings that meets or exceeds the rate of inflation. The annual spending appropriation will be subject to a minimum rate of 4% and a maximum rate of 7% of each endowment fund's current market value. Temporarily restricted net assets, along with other donor-restricted funds, include the spending appropriation and investment income of the endowments and are pending appropriation for expenditure consistent with the specific purpose of the fund.

#### **12. Business Combinations, Strategic Partnerships, and Affiliation Agreements**

##### **Business Combinations**

During 2017 and 2016, Ochsner completed several physician practice acquisitions, none of which were material to the results of operations. In 2016, Ochsner also purchased 100% of the equity interest of Sculpting Center of New Orleans, LLC.

On January 9, 2017, Ochsner completed the acquisition of Millennium Healthcare Management, Inc. (MHM). MHM is a leading provider of urgent care and occupational medicine in Louisiana and consists of 12 urgent care and 4 occupational health clinics. Under the terms of the acquisition, Ochsner paid approximately \$30.8 million in cash. Results of operations of MHM have been included in its consolidated financial statements from the date of acquisition.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **12. Business Combinations, Strategic Partnerships, and Affiliation Agreements (continued)**

##### **Strategic Partnerships and Affiliation Agreements**

In recent years, Ochsner has entered into several strategic partnership and affiliation agreements. While the direct financial impact of these agreements is not material, they are a component of Ochsner's efforts to increase local access to care, improve quality, reduce the cost of health care, and share best practices and resources in order to improve the health of Louisiana communities. Ochsner now has strategic partnerships and clinical affiliations with Lafayette General Health, CHRISTUS Health Louisiana, IASIS Glenwood Regional Medical Center, and Southwest Mississippi Regional Medical Center.

Ochsner also has Joint Operating Agreements (JOA) with St. Tammany Parish Hospital (STPH), Terrebonne General Medical Center (TGMC), and Slidell Memorial Hospital (SMH). These JOAs are intended to coordinate resources with the goal of lowering costs, improving quality, and creating a seamless clinical environment for patients in each of their respective local regions. STPH, TGMC, and SMH all remain public hospitals governed by their respective Boards. Ochsner is financially integrated with these hospitals and recognizes other operating revenue or other operating expense related to the JOAs in its consolidated statements of operations.

Ochsner also provides management assistance and support for Chabert, SCPH and, beginning November 2017, SBPH. Under these management agreements, Ochsner receives management fees and any excess of revenues over expenses generated by each of the facilities annually, as well as reimbursement of purchased services incurred on behalf of the facilities. Ochsner also has a management agreement with Hancock. Under its management agreement with Hancock, Ochsner receives management fees as well as reimbursement of expenses incurred for providing management assistance and support services; see further discussion in subsequent event caption below.

In October 2016, Ochsner entered into a professional services agreement with Adeptus Health, Inc. (Adeptus) to enhance access to emergency medical care in Louisiana. Ochsner opened a freestanding emergency department in Marrero, Louisiana, and Adeptus managed the operations. On March 30, 2017, Ochsner and Adeptus terminated this agreement and the previously established joint venture.

In December 2017, Ochsner, the state of Louisiana (State), the Board of Supervisors of Louisiana State University and Agricultural and Mechanical College (LSU), and the Biomedical Research Foundation (BRF) signed Letters of Intent (LOI) to create a new, long-term, Public Private Partnership agreement in Shreveport and Monroe. Under the proposed agreement, LSU and

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **12. Business Combinations, Strategic Partnerships, and Affiliation Agreements (continued)**

Ochsner will jointly form a new University Health System (UHS) structure to coordinate activities between the school and the health care delivery system. This agreement is expected to be effective in 2018.

##### *Subsequent Events*

On January 2, 2018, Ochsner completed the acquisition of New Orleans Urgent Care (NOUC), which consists of two urgent care clinics for approximately \$1.2 million in cash. Results of operations of NOUC will be included in Ochsner's consolidated financial statements from the date of acquisition.

On January 19, 2018, Ochsner completed an asset purchase agreement with NOLA Weightloss, LLC for approximately \$167,000. Ochsner acquired the seller's interest in and rights to operate a Medi-Weightloss franchise business, as well as other considerations.

In March 2018, Ochsner signed a membership interest purchase agreement with CHRISTUS Health (CHRISTUS) to acquire a 40% minority ownership interest in CHRISTUS Health Southwestern Louisiana (SWLA). SWLA owns and operates health care facilities and operations related to physician practices in Louisiana, including CHRISTUS St. Patrick Hospital, CHRISTUS Lake Area Medical Center, and various clinical facilities. CHRISTUS St. Patrick Hospital is a 50-bed hospital and CHRISTUS Lake Area Medical Center is an 88-bed, full-service acute care hospital in Lake Charles, Louisiana. This purchase is expected to close during the second half of 2018 once regulatory approval is received.

On April 1, 2018, Ochsner completed an agreement to lease Hancock Medical Center, a 102-bed acute care hospital, six related medical office buildings, and equipment. This new agreement terminated the existing management agreement. The net present value of lease payments to be paid over the life of the 25-year capital lease is approximately \$12.5 million, and Ochsner will own the property at the end of the lease term. As part of this transaction, Ochsner will acquire the current assets, liabilities, and provider number of Hancock. Results of operations of Hancock will be included in Ochsner's consolidated financial statements from the transaction date.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 13. Equity Method Investments and Joint Ventures

##### Investment in Equity Investees

Ochsner's investment in unconsolidated affiliates at December 31 and its income from equity investees for the years then ended are as follows (in thousands):

	<b>Ownership Interest</b>	<b>Investment in Equity Investees</b>	<b>Equity in Income of Equity Investees</b>
<b>2017</b>			
Southeast Louisiana Homecare LLC	25%	\$ 2,999	\$ (122)
Louisiana Extended Care Hospital of Kenner, LLC	25%	356	17
OSR Louisiana, LLC	49%	–	(156)
Ochsner-Acadia, LLC	25%	6,586	458
OMC West JV, LLC	49%	5,860	–
		<u>\$ 15,801</u>	<u>\$ 197</u>
<b>2016</b>			
Southeast Louisiana Homecare LLC	25%	\$ 3,176	\$ 359
Louisiana Extended Care Hospital of Kenner, LLC	25%	82	123
OSR Louisiana, LLC	49%	–	(252)
Ochsner-Acadia, LLC	25%	6,994	–
		<u>\$ 10,252</u>	<u>\$ 230</u>

On June 15, 2015, Ochsner entered into a joint venture, OSR Louisiana, LLC, with Pennsylvania-based Select Medical Corporation to jointly open a new, 60-bed, acute inpatient rehabilitation hospital. Construction began in early 2016 and the joint venture commenced patient service operations at the new facility in April 2018. This joint venture did not have material operations during the year ended December 31, 2017.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **13. Equity Method Investments and Joint Ventures**

On May 17, 2016, Ochsner formed a joint venture, Ochsner-Acadia, LLC, with Acadia Healthcare (Acadia) to open and operate an 82-bed behavioral health facility in Laplace, Louisiana. Ochsner contributed the facility and recorded a gain of \$6,994 for a 25% interest in the joint venture and Acadia will contribute the facility build-out, equipment, and working capital. Construction began in 2016 and the facility opened in November 2017. The results of the joint venture's operations were not material to its consolidated financial statements for the year ended December 31, 2017.

On December 20, 2017, Ochsner entered into a joint venture with a commercial real estate company to form OMC West JV, LLC (OMC West). The focus of the new partnership is to own and provide property management for a medical building located at 2614 Jefferson Highway in Jefferson, Louisiana. The five-story, 129,875 square-foot medical building will house three separate health care components, including long-term acute care, inpatient rehabilitation, and a skilled nursing facility. Ochsner is the lessor of the building and will make future minimum lease payments to OMC West for this lease totaling approximately \$43.5 million over 10 years. Ochsner also subleases space to its equity-method investments OSR Louisiana, LLC, and Louisiana Extended Care Hospital of Kenner, LLC, and will receive approximately \$39.8 million over 10 years. These lease amounts are included in Ochsner's lessee and lessor commitments disclosed in Note 17 to the consolidated financial statements. The results of Ochsner's equity-method investment in OMC West were not material in 2017.

#### **14. Electronic Health Records Services Agreements**

In order to develop a better clinical integration and provide cost savings for its JOA partners and equity-method investments, Ochsner has entered into electronic health records services and hosting agreements to implement and support a common EHR system. During 2015, Ochsner implemented its EHR system at STPH and continues to host and maintain it. During 2017, Ochsner implemented its EHR system at TGMC, the clinics of SMH, and its equity-method investment with Acadia and continues to host and maintain them.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 15. Functional Expenses

Ochsner provides general health care services primarily to residents within its geographic location. Expenses related to providing these services for the years ended December 31 are as follows (in thousands):

	2017	2016
Health care services	\$ 2,050,580	\$ 1,858,093
General and administrative	820,973	790,743
Medical education	30,019	38,716
Research	15,201	13,999
Fitness center	11,634	12,310
Hotel	3,618	3,546
Total	\$ 2,932,025	\$ 2,717,407

#### 16. Supplemental Disclosures of Cash Flow Information

	Year Ended December 31,	
	2017	2016
Cash paid for interest (net of amounts capitalized)	\$ 49,871	\$ 52,567
Supplemental non-cash investing and financing activities:		
Property purchases included in accounts payable	\$ 14,186	\$ 14,625
Property purchases financed by capital leases and long-term debt	\$ 2,852	\$ 6,474

#### 17. Commitments and Contingencies

##### Professional and General Liability Insurance

Professional and general liability claims have been asserted against Ochsner by various claimants. The claims are in various stages of processing, and some may ultimately be brought to trial. Incidents occurring through December 31, 2017, may result in the assertion of additional claims.

Ochsner participates in a risk management program to provide for professional and general liability coverage.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **17. Commitments and Contingencies (continued)**

Under this program, Ochsner carries professional and general liability insurance coverage for up to \$65.0 million each of annual aggregate claims subject to certain deductible provisions. Ochsner is self-insured with respect to the first \$3.0 million of each claim for professional liability with an annual aggregate exposure of \$6.0 million. General liability claims are subject to a retention of \$1.0 million per claim and \$2.0 million annual aggregate. Ochsner also carries additional coverage on certain community hospitals that carry similar coverage with lower self-retention and aggregate levels.

Professional liability claims are limited by Louisiana statute to \$500,000 per occurrence, the first \$100,000 of which is payable by the health care provider and the remainder of which is payable by the Patient's Compensation Fund (the Fund) for participants in the Fund. The Fund was established by the Medical Malpractice Act (the Act), which was enacted in 1975 by the state of Louisiana. The Act established the Fund and limited recovery in medical malpractice cases to \$500,000. The limitation on recovery has been challenged and, to date, successfully defended in the courts. Expenditures recorded by Ochsner for participation in the Fund for the years ended December 31, 2017 and 2016, were approximately \$18.8 million and \$17.9 million, respectively, and are included in other operating expenses in the accompanying consolidated statements of operations.

Ochsner has an established trust fund held by a financial institution. Disbursements are made from the trust fund for self-insured professional and general liability claims, claims administration costs, and legal fees. The amounts to be contributed to the trust funds are determined annually by an independent actuary. The trust fund assets for Ochsner in the aggregate totaled approximately \$9.3 million and \$9.1 million at December 31, 2017 and 2016, respectively. The trust fund assets are included in assets limited as to use under self-insurance trust fund in the accompanying consolidated balance sheets. The estimated liability recorded by Ochsner in the aggregate for claims, based on the actuarial report, is approximately \$14.1 million with no estimated reinsurance recoveries at December 31, 2017, and \$13.8 million with no estimated reinsurance recoveries at December 31, 2016. The estimated liability is included in other current liabilities and other long-term liabilities in the accompanying consolidated balance sheets. The estimated liability for Ochsner was discounted at approximately 2.5% at both December 31, 2017 and 2016. If the risk management program is terminated, the trust fund balances, if any, revert to Ochsner after satisfaction of outstanding claims. Any proceeds from such a reversion would be used to reduce future costs for liability coverage.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **17. Commitments and Contingencies (continued)**

##### **Estimated Workers' Compensation and Employee Health Claims**

Ochsner is self-insured for workers' compensation and employee health claims. The estimated liability for workers' compensation and employee health claims totaled approximately \$17.6 million and \$18.8 million at December 31, 2017 and 2016, respectively, which is included in accrued salaries, wages, and benefits; other current liabilities; and other long-term liabilities in the accompanying consolidated balance sheets.

##### **Property Insurance**

Ochsner carries property insurance coverage through third-party insurers. The policy limit is \$750.0 million and is subject to a deductible of \$250,000 per occurrence for property damage and 24 hours for the time element. The Named Wind sublimit is \$160.0 million. The Named Wind deductible is 3% for property damage and 72 hours for the time element, subject to a minimum of \$500,000 and a maximum of \$50.0 million. Ochsner also carried coverage on certain community hospitals with self-retention and aggregate levels.

##### **Lease Commitments**

Ochsner leases certain software and equipment under capital leases. The capital lease obligations are included in other current liabilities and other non-current liabilities in the accompanying consolidated balance sheets.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

**17. Commitments and Contingencies (continued)**

Additionally, Ochsner leases assets under various rental agreements. Ochsner leases have varying terms, which may include renewal or purchase options and escalation clauses that are factored into determining minimum lease payments. The following schedule summarizes its future annual minimum rental commitments on outstanding leases as of December 31, 2017 (in thousands):

	<u>Lease Obligations</u>	
	<u>Capital</u>	<u>Operating</u>
2018	\$ 6,825	\$ 48,592
2019	2,931	40,743
2020	1,834	35,645
2021	476	31,757
2022	153	29,371
Thereafter	–	195,924
Total minimum lease payments	12,219	<u>\$ 382,032</u>
Less amounts representing interest	<u>(538)</u>	
	11,681	
Less current maturities	<u>(6,560)</u>	
Capital lease obligations – non-current	<u>\$ 5,121</u>	

Rent expense, which includes operating leases and cancelable short-term rental agreements, was approximately \$64.0 million and \$53.5 million for the years ended December 31, 2017 and 2016, respectively.

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### 17. Commitments and Contingencies (continued)

##### Operating Leases – Lessor

Ochsner leases office space to other businesses. Lease terms generally range from one to four years, with options of renewal for additional periods. All such property leases provide for minimum annual rentals, and all rental revenue has been recorded on a straight-line basis. Following is a schedule by years of future minimum rental payments under non-cancelable operating leases as of December 31, 2017 (in thousands):

Years ending December 31:	
2018	\$ 6,785
2019	6,653
2020	5,469
2021	5,304
2022	5,298
Thereafter	30,079
Total minimum lease payments to be received	<u>\$ 59,588</u>

##### Contingencies

The health care industry as a whole is subject to numerous complex laws and regulations of federal, state, and local governments. Compliance with these laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. Such compliance with laws and regulations in the health care industry has come under increased government scrutiny. Ochsner and its subsidiaries are parties to various legal proceedings and potential claims arising in the ordinary course of their business. Management of Ochsner believes the reserves it has established for these issues are adequate and does not believe, based on current facts and circumstances and after review with counsel, that these matters will have a material adverse effect on its consolidated statements of financial position or results of operations.

The Tax Relief and Health Care Act of 2006 authorized a permanent program involving the use of third-party recovery audit contractors (RACs) to identify Medicare and Medicaid overpayments and underpayments made to providers. RACs are compensated based on the amount of both overpayments and underpayments they identify by reviewing claims submitted to Medicare for correct coding and medical necessity. Payment recoveries resulting from RAC reviews are

## Ochsner Clinic Foundation and Subsidiaries

### Notes to Consolidated Financial Statements (continued)

#### **17. Commitments and Contingencies (continued)**

appealable through administrative and judicial processes. Payment recoveries and denials resulting from RAC reviews can be appealed through administrative and judicial processes, and management intends to pursue the reversal of adverse determinations where appropriate. In addition to overpayments that are not reversed on appeal, Ochsner will incur additional costs to respond to requests for records and to pursue the reversal of payment denials. Ochsner expects the RACs will continue to seek CMS approval to review additional issues.

Management of Ochsner believes that the reserves it has established for RAC reviews, which are included in other long-term liabilities in the accompanying consolidated balance sheets, are adequate but cannot predict with certainty the impact of the Medicare and Medicaid RAC program on its future consolidated results of operations or cash flows.

#### **18. Subsequent Events**

Ochsner has evaluated subsequent events through April 23, 2018, the date the accompanying consolidated financial statements were available for issuance.

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