



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

**For the Year Ended
December 31, 2018**

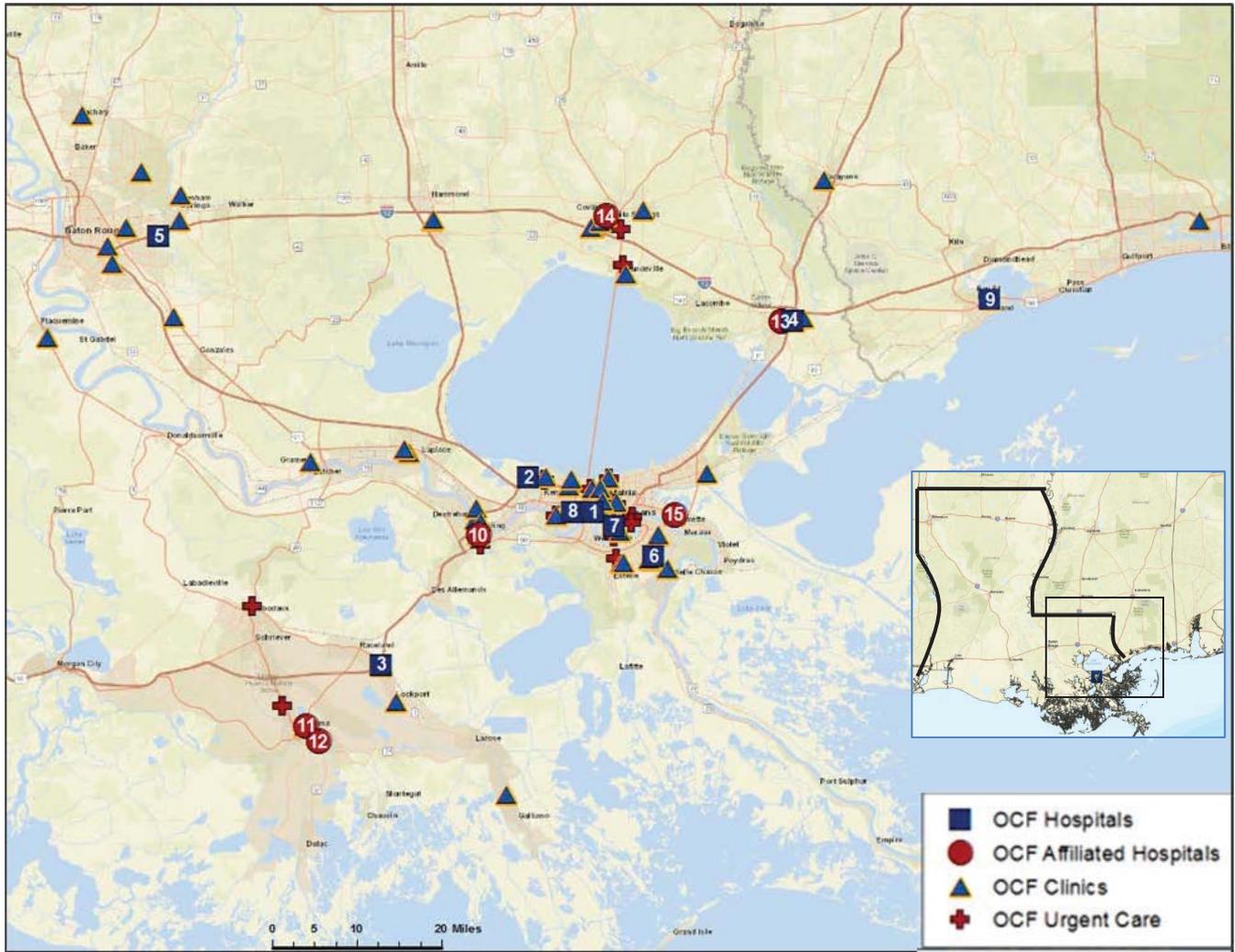
System Overview

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, 87 health centers, 15 Urgent Care Clinics and four Occupational Health Clinics. When combined with affiliated hospitals, Ochsner owns, provides management assistance and support, or is affiliated with 31 hospitals. It also employs approximately 1,500 active staff physicians that have 1,300 board certifications in 78 specialties, trains 288 medical residents and fellows annually, has 465 Doctor of Medicine students enrolled in the University of Queensland, Ochsner Clinical School, and is currently conducting over 1,200 clinical research studies. In 2018, more than 811,000 people from all 50 states and more than 70 countries visited Ochsner.

Ochsner is recognized nationally for quality. Awards and recognitions in 2018 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 three medical specialties, according to *U.S. News and World Report’s* 2018-19 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, Ochsner Baptist and Ochsner Medical Center – West Bank Campus have received the 2018 Distinguished Hospital Award for Clinical Excellence™ from Healthgrades.
- 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 named to the IBM Watson Health’s 100 Top Hospitals® award list, formerly known as the Truven Health Analytics® 100 Top Hospitals, as one of the top U.S. Major Teaching Hospitals.
- Ochsner Medical Center - Baton Rouge was named as one of the top Medium Community Hospitals for the 2018 100 Top Hospitals® Award by IBM Watson Health, formerly known as the Truven Health Analytics.
- *Becker’s Hospital Review* recognized Ochsner Medical Center as one of the “100 Great Hospitals in America” for 2018. This is the seventh consecutive year that Ochsner Medical has been recognized with this award and is the only Louisiana hospital named to this list.
- *Becker’s Hospital Review* recognized Ochsner Medical Center-Baton Rouge as one of the “100 Great Community Hospitals in America” for 2018.
- Ochsner Hospital for Children was ranked among the top 50 children’s hospitals in the country for pediatric gastroenterology and gastrointestinal surgery specialties in the new 2018-19 *U.S. News and World Reports* Best Children’s Hospitals rankings.
- Eleven Ochsner Facilities or affiliated hospitals received an “A” Grade for Patient Safety from the 2018 Leapfrog Group.

The following map indicates the locations of Ochsner’s acute care hospitals and health centers. See “Health Care Operations of the Credit Group – Facilities” herein for more information regarding Ochsner’s health care facilities.



Ochsner Clinic Foundation Hospitals

Ochsner Medical Center (1)	Ochsner Medical Center Kenner (2)	Ochsner St. Anne General Hospital (3)
Ochsner Medical Center Northshore (4)	Ochsner Medical Center Baton Rouge (5)	Ochsner Medical Center West Bank (6)
Ochsner Baptist Medical Center (7)	Ochsner Elmwood Hospital (8)	Ochsner Hancock Medical Center (9)

Ochsner Clinic Foundation Affiliate Hospitals

St. Charles Parish Hospital (10)	Terbonne General Medical Center (11)	Leonard J. Chabert Medical Center (12)
Slidell Memorial Hospital (13)	St. Tammany Parish Hospital (14)	St. Bernard Parish Hospital (15)

* Ochsner-LSU Health’s two hospitals in Shreveport and Monroe, Lafayette General Health’s seven hospitals, CHRISTUS Health Louisiana’s seven hospitals (incl. CHRISTUS Ochsner St Patrick Hospital and CHRISTUS Ochsner Lake Area Hospital) are excluded from map as each is located outside of the Service Area as hereinafter defined.

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 97.2% of the total assets of OCF Consolidated as of December 31, 2018 and 97.5% of the total revenue of OCF Consolidated for the year ended December 31, 2018.

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 687-bed acute care hospital located in New Orleans, Louisiana, which serves as the flagship of Ochsner, and includes an 11-story clinic building, a 134-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 satellite hospital of OMC, located in Elmwood, Louisiana, which primarily provides outpatient services;
- Ochsner Medical Center – West Bank Campus, a 165-bed acute care satellite hospital of OMC in Gretna, 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;
- 87 health centers throughout southeast Louisiana and Mississippi;
- 15 Urgent Care Clinics and four Occupational Health Clinics throughout Greater New Orleans; and,
- Several fitness centers that operate as Ochsner Fitness Center.

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

- Ochsner St. Anne General Hospital, a 35-bed acute care hospital in Raceland, Louisiana, and
- Ochsner 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 five 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.
- Ochsner LSU Health System of North Louisiana (“OLHS-NL”), which includes a 452 bed hospital in Shreveport, Louisiana, a 244 bed hospital in Monroe, Louisiana and healthcare operations in Shreveport, Louisiana and Monroe, 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 and CHRISTUS Health Louisiana.

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 and 2018 are as follows:

- Louisiana State University. Effective October 1, 2018, OCF entered into management agreement with a newly formed nonprofit entity Ochsner LSU Health System of North Louisiana (“OLHS-NL”) to provide management services, billing and collection services and administrative support for certain hospital and healthcare operations in Shreveport and Monroe. OCF and the Board of Supervisors of Louisiana State University and Agricultural and Mechanical College (“LSU”) formed OLHS-NL to assume overall responsibility for the operations and clinical activities of the former University Health hospitals and clinics in Shreveport and Monroe and coordinate the activities between LSU Medical School, the parties’ physicians, and the healthcare operations in Shreveport and Monroe. OLHS-NL is a standalone nonprofit organization and is not a subsidiary of either LSU or OCF. OLHS-NL’s Bylaws require that LSU and OCF each appoint an equal number of directors to the OLHS-NL Board to oversee, coordinate, and manage OLHS-NL’s activities. In conjunction with the management agreement of OLHS-NL, Ochsner acquired the EHR licenses and related liabilities, and hired the Information Services (IS) employees of OLHS-NL in exchange for a note payable of approximately \$6.2 million to the Biomedical Research Foundation on October 1, 2018. With this acquisition, Ochsner fully manages the IS function of OLHS-NL.
- CHRISTUS Health. 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”) in exchange for cash of \$35 million and a promissory note of \$27.8 million. 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 agreement was finalized September 1, 2018 once regulatory approval was received. CHRISTUS Health manages the hospitals, CHRISTUS St. Patrick, and CHRISTUS Lake Area Medical Center. Ochsner manages all physician and clinic operations.
- 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.

- **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.
- **Select Medical Corporation.** On June 15, 2015, Ochsner entered into a joint venture, OSR Louisiana, LLC, with Pennsylvania-based Select Medical Corporation to open a new \$35 million, 60-bed acute inpatient rehabilitation hospital. The facility began operations during the second quarter of 2018.

Governance

Following the expiration of their current terms on December 31, 2018, OCF announced the departures of Thomas Davis (Duncan), George Loss, MD and Leonardo Seane, MD from the Board of Directors. On February 25, 2019, OCF announced the following three members elected to the Board of Directors:

John A. Evans, Rehab Partners, Inc (Retired), has over four decades of healthcare experience. He is currently retired as a Physical Therapist; but, remains an active partner in several healthcare and non-healthcare business ventures. Mr. Evans serves on many Boards including, the American Bank and Statewide Bank; the West St. Tammany Chamber of Commerce; and was a founding member of the Board of St. Tammany Parish Hospital, where he continues to serve as Chairman.

Cuong “CJ” Bui, MD, serves as Chairman of the Department of Neurosurgery. He completed his neurosurgical training at SUNY- Upstate Medical Center in Syracuse and his fellowship training in pediatric neurosurgery from University of Alabama Children’s Hospital in Birmingham.

William “David” Sumrall, III MD, serves as Associate Medical Director, Surgical Services and System Chair, Anesthesiology & Interventional Pain Medicine. He is board certified in Anesthesiology.

Executive Leadership

Leonardo Seoane, MD, Senior Vice President and Chief Academic Officer. On November 1, 2018 Dr. Leonardo Seoane was appointed the permanent Chief Academic Officer for Ochsner Health System after serving as the interim Chief Academic Officer since May 24, 2018. Dr. Seoane has been associated with Ochsner since 1998 completing his Pulmonary, Critical Care, and Lung Transplant Fellowship at the combined LSU/Ochsner program. He joined Ochsner in 2002 and has served in various leadership roles at Ochsner including Medical Director of Lung Transplant, Associate Program Director of Internal Medicine Residency Program, Chair of Sepsis Performance Improvement Committee, Assistant Dean of Ochsner Clinical School for Curriculum, and Dean of the UQ-Ochsner Clinical School. He is a nationally recognized expert in the management of sepsis and in medical education. He has been recognized repeatedly for his teaching and leadership winning the Hurst B. Hatch Award for Teaching 7 times, the Ochsner Health System Award for Teaching, and the Ochsner Health System Physician Academic Contributor of the Year. Dr. Seoane graduated magna cum laude from Loyola University in New Orleans, with a Bachelor of Science in Biological Sciences. He earned his Doctor of Medicine degree at Louisiana State University School of Medicine in New Orleans, graduating with Alpha Omega Alpha honors, an elite designation recognizing excellence in scholarship and the highest ideals in the profession of medicine. After medical school, he completed an internship at the University of Alabama Birmingham Medical Center and residency in Internal Medicine at Louisiana State University Health Sciences Center (LSUHSC) in New Orleans.

Jennifer Bollinger, Senior Vice President of Consumer Strategy. Beginning January 2, 2019, Jennifer was appointed Senior Vice President of Consumer Strategy focused on developing actionable insights based on patient behavior and expectations. She and her team consistently support core teams across the organization to develop new capabilities that enhance access, care navigation, service excellence and to build new digital connectivity along the patient journey. After joining the organization in 2012, Jennifer served as the Vice President of Corporate Communications & Public Relations until 2018. In that role, she oversaw the teams responsible for the system's comprehensive internal and external messaging. Prior to joining Ochsner, Jennifer led strategy at several marketing and communications agencies for more than 20 years including Zehnder Communications, The Netcom Group, Keating Magee Advertising, Berger & Reed Advertising and Fitzgerald Advertising. She is a member of the Executive Summit of the American Hospital Association and has been named to the Power Generation and as a Woman of the Year by City Business Magazine and selected as one of Gambit Magazine's 40 Under 40 in New Orleans. A native of Washington D.C., Jennifer made New Orleans home after graduating from the A.B. Freeman School of Business at Tulane University.

Management Discussion and Analysis of Financial Results

Executive Summary:

OCF had Income from Operations of \$106.8 million (3.1% of Total Unrestricted Revenues) for 2018 compared to \$70.1 million (2.3% of Total Unrestricted Revenues) for 2017, a \$36.7 million increase. Operating EBIDA was \$306.8 million (9% of Total Unrestricted Revenues) for 2018 compared to \$248.0 million (8.3% of Total Unrestricted Revenues) for 2017, a \$58.8 million increase.

Ochsner adopted Accounting Standards Update 2014-09, *Revenue from Contracts with Customers (Topic 606)* on January 1, 2018, which changed the presentation of net operating revenues. The adoption of ASU 2014-09 did not materially impact Ochsner's consolidated financial position, results of operations, or cash flows. For more information, please see Note A of the Consolidated Statement of Operations.

Statement of Operations:

OCF achieved Total Unrestricted Revenues of approximately \$3.4 billion for 2018, an increase of \$413.2 million or 13.7% over 2017 primarily due to organic growth as well as an increase in patients referred from affiliates and outlying facilities. The 13.7% year over year growth of Total Unrestricted Revenues exceeded the 12.8% year over year growth of Total Expenses. Patient Service Revenue increased \$293.9 million or 12.8%. Premium Revenue increased \$19.6 million. When comparing 2018 to 2017, discharges decreased less than 1.0%, patient days increased less than 1.0%, inpatient surgical procedures decreased less than 1.0%, outpatient surgical procedures increased 6.9%, emergency room visits increased 11%, clinic relative value units increased 9.8%, clinic visits increased 11.5%, and unique clinic patient visits increased 11.8%. Revenue received from any of our managed or affiliated hospitals is not included within Patient Service Revenue.

Other Operating Revenue for 2018 was \$504.3 million, a \$100.9 million increase over 2017. Other Operating Revenue for 2018 includes a \$65.2 million increase in pharmacy revenue and a \$10.4 million increase related to third-party physician contracts. This increase is partially offset by a \$3.3 million decrease in electronic health records incentive payments. Other Operating Revenue for 2018 includes \$14.5 million related to a business economic loss claim due to the BP Deepwater Horizon oil spill. Other Operating Revenue for 2017 includes \$8.9 million of insurance proceeds. Other Operating Revenue also includes \$57 million in 2018 and \$41.1 million in 2017 of revenue related to management agreements and joint operating agreements.

Salaries and Wages for 2018 were \$1.5 billion, a \$146.3 million increase over 2017. The majority of the increase is related to additional staffing and additional providers needed to meet increased patient demand. Total providers increased by 12% or 180 full-time equivalents ("FTEs"). That includes an 8.5% increase in physicians, or 85 FTEs, and a 19% increase in the number of other providers, or 95 FTEs. Ochsner employs approximately 1,500 active staff physicians and over 700 Other Providers.

Medical Services to Outside Providers expense for 2018 increased by \$6.5 million from 2017. 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 \$83.2 million when comparing 2018 to 2017. Medical Supplies and Services as a percentage of Total Unrestricted Revenues was 19.1% for 2018 and 18.9% for 2017. Approximately \$18.9 million of the increase is due to increased drug expenses primarily due to an increased volume of chemotherapy and infusion drugs. Approximately \$27.5 million of the increase is related to drug expense in the retail pharmacy, as the retail pharmacy business continues to expand.

Other operating expenses which includes building and equipment, insurance, professional services and general and administrative expenses for 2018 increased by \$110.5 million over 2017. In 2018, OCF made a \$56 million payment to OLHS-NL to promote common charitable goals through the support of educational opportunities for medical and clinical professionals in the provision of healthcare services for low-income and needy patients. \$4.2 million of the increase is related to software expense associated with clinical system implementations and upgrades, as well as

software expense associated with Ochsner's partners. \$6.4 million of the increase is related to fees paid to a third-party vendor for the construction, installation, and management of energy facilities used to process and distribute chilled water and steam at OMC and Ochsner Medical Complex – The Grove (Baton Rouge).

OCF had net non-operating losses of \$34 million for 2018 and net non-operating gains of \$74.9 million for 2017. 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. Ochsner adopted Accounting Standards Update 2016-01, *Financial Instruments – Overall (Subtopic 825-10)* on January 1, 2018, which resulted in the changes of the fair value of investments in equity securities to be recognized in excess of revenues over expenses. For more information, please see Note B of the Consolidated Statement of Operations.

Ratings

In conjunction with the 2017 Official Statement dated May 11, 2017, Fitch Ratings has provided a rating for the Bonds of A- with a stable outlook and Moody's Investors Service, Inc. provided a rating for the Bonds of A3 with a stable outlook. On September 6, 2018 Moody's Investors Service, Inc. affirmed its rating for the Bonds of A3 with a stable outlook. On April 30, 2019 S&P Global Ratings assigned a rating for the Bonds of A with a stable outlook.

Liquidity and Cash Position

At December 31, 2018, OCF had unrestricted Cash and Investments of \$885.2 million which equates to 102 days cash on hand. Cash and Investments decreased by \$70.9 million from \$956.1 million or 124 days cash on hand at December 31, 2017. The 22 day reduction in days cash on hand includes an 8 day reduction due to the decrease in cash and a 14 day reduction due to the increase in expense per day. Operating EBIDA for 2018 was \$306.8 million. Cash decreased due to \$269.1 million of capital expenditures offset by a release of \$95.1 million of construction proceeds related to the Series 2017 bonds and \$85.1 million in Debt Service. Other uses of Cash include a \$22.0 million increase in Patients Accounts Receivable, a \$14.5 million increase in Other Receivables related to the business economic loss claim due to the BP Deepwater Horizon oil spill, a \$35 million investment related to the CHRISTUS membership interest purchase agreement, \$34.0 million reduction related to the Pooled Investment Portfolio and \$13.1 million of other changes to working capital. Gains related to the Pooled Investment Portfolio in the first quarter of 2019 exceeded 2018's losses. As of December 31, 2018, OCF had \$82 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, 2018</u>	<u>Dec. 31, 2017</u>	<u>Dec. 31, 2018</u>	<u>Dec. 31, 2017</u>
Monthly Liquidity	\$ 700,787	\$801,840	81	104
Liquidity greater than 30 days and less than one year	169,480	139,096	19	18
Locked Up (liquidity one year or more)	14,909	15,181	2	2
Total	\$ 885,176	\$956,117	102	124

Debt and Debt Service Coverage

As of December 31, 2018, OCF had \$1.3 billion in total long-term debt outstanding, compared to \$1.1 billion at December 31, 2017. The long-term debt to capitalization ratio for OCF was 61.6% in 2018 versus 62.5% in 2017.

Debt Service Coverage Calculation:	<u>2018</u>	<u>2017</u>
Income Available for Debt Service	\$301,870	\$295,154
Annual Debt Service	\$72,097	\$69,141
Annual Debt Service Coverage Ratio	4.2x	4.3x

<u>Series</u>	<u>Par Amt O/S</u>	<u>Final Maturity</u>	<u>Interest Mode</u>
OCHSNER CLINIC FOUNDATION			
Series 2015 Taxable New Money	252,820,000	5/15/2045	Fixed
Series 2015 Tax Exempt Refunding	108,680,000	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⁾	5,595,867	3/31/2033	Fixed
December 2013 Note Payable ⁽¹⁾	47,211,656	12/31/2028	Fixed
July 2014 Note Payable ⁽¹⁾	68,819,829	8/15/2034	Fixed
December 2013 Promissory Note	10,547,916	12/30/2020	Variable ⁽³⁾
October 2014 Promissory Note	16,133,333	10/31/2021	Fixed
September 2015 Promissory Note	21,000,000	9/30/2022	Variable ⁽³⁾
September 2018 Promissory Note	27,423,636	9/1/2023	Fixed
October 2018 Promissory Note	5,767,560	9/30/2021	Fixed ⁽³⁾
2006 Working Capital Note ⁽²⁾	8,912,012	5/1/2026	Variable
Software and Equipment Loans ⁽²⁾	147,955	N/A	N/A
Capital Lease Obligations ⁽²⁾	131,304,453	N/A	N/A
SUBTOTAL	1,279,979,217		

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
For the Years Ended December 31, 2018 and 2017
(\$ In Thousands)

	<u>2018</u>	<u>2017^{A, B}</u>	<u>Difference</u>
Unrestricted revenues:			
Patient service revenue	2,595,675	2,301,804	293,871
Premium revenue	318,453	298,824	19,629
Other operating revenue	504,342	403,463	100,879
Net assets released from restriction used for operations	5,155	6,319	(1,164)
Total unrestricted revenues	<u>3,423,625</u>	<u>3,010,410</u>	<u>413,215</u>
Expenses:			
Salaries and wages	1,505,643	1,359,294	146,349
Benefits	145,877	138,008	7,869
Medical services to outside providers	140,491	133,952	6,539
Medical supplies and services	653,371	570,155	83,216
Other operating expenses	671,492	560,994	110,498
Depreciation and amortization	147,528	128,098	19,430
Interest	52,411	49,762	2,649
Total expenses	<u>3,316,813</u>	<u>2,940,263</u>	<u>376,550</u>
Income from operations	<u>106,812</u>	<u>70,147</u>	<u>36,665</u>
Non-operating gains (losses):			
Investment and other realized gains - net	34,557	47,147	(12,590)
Loss on early extinguishment of debt	-	(9,256)	9,256
Unrealized (losses) gains on investments - net	<u>(68,569)</u>	<u>36,968</u>	<u>(105,537)</u>
Total non-operating (losses) gains	<u>(34,012)</u>	<u>74,859</u>	<u>(108,871)</u>
Excess of revenues over expenses	<u>\$ 72,800</u>	<u>\$ 145,006</u>	<u>\$ (72,206)</u>

Note A: In May 2014, the Financial Accounting Standards Board (“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. 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 Ochsner starting January 1, 2018. Ochsner used a full retrospective method of application to adopt ASU 2014-09 on January 1, 2018. Adoption of ASU 2014-09 resulted 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. While the adoption of ASU 2014-09 changed the presentation of net operating revenues in Ochsner’s consolidated statements of operations, it did 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 accordance with the full retrospective method, all 2017 amounts have been restated to adopt this pronouncement.

Note B: 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. The provisions of ASU 2016-01 were effective for Ochsner starting January 1, 2018, including interim periods within that reporting period. The adoption of ASU 2016-01 resulted 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. All 2017 amounts have been restated to comply with this new pronouncement.

Ochsner Clinic Foundation and Subsidiaries
Consolidated Balance Sheets
As of December 31, 2018 and 2017
(\$ In Thousands)

	<u>2018</u>	<u>2017</u> ¹
Assets		
Current assets:		
Cash and cash equivalents	137,604	186,401
Assets limited as to use, required for current liabilities	7,630	7,370
Patient accounts receivable, net	271,331	249,299
Other receivables	149,190	104,827
Inventories	69,757	68,608
Prepaid expenses and other current assets	40,814	34,395
Estimated third-party payor settlements	27,448	22,224
Total current assets	<u>703,774</u>	<u>673,124</u>
Assets limited as to use:		
By Board for capital improvements, charity, research, and other	747,572	769,717
Under bond indenture agreements	-	95,106
Under self-insurance trust fund	10,024	9,301
Donor-restricted long-term investments	82,010	97,425
Total assets limited as to use	<u>839,606</u>	<u>971,549</u>
Less assets limited as to use, required for current liabilities	<u>(7,630)</u>	<u>(7,370)</u>
Non-current assets limited as to use	831,976	964,179
Investments in unconsolidated affiliates, real estate, and other	83,409	19,644
Property, net	1,171,795	927,979
Goodwill	72,411	71,195
Intangible assets	11,477	12,354
Other assets	50,167	47,332
Total assets	<u>\$2,925,009</u>	<u>\$2,715,807</u>

Ochsner Clinic Foundation and Subsidiaries
Consolidated Balance Sheets
As of December 31, 2018 and 2017
(\$ In Thousands)

	2018	2017¹
Liabilities and net assets		
Current liabilities:		
Accounts payable	205,582	190,683
Accrued salaries, wages, and benefits	190,359	163,218
Deferred revenue	39,476	35,552
Estimated third-party payor settlements	5,079	4,275
Bonds payable, current portion	4,060	2,095
Notes payable, current	52,430	52,430
Long-term debt, current portion	15,606	13,299
Other current liabilities	43,230	33,266
Total current liabilities	555,822	494,818
Pension and postretirement obligations	141,993	147,596
Bonds payable	980,831	986,730
Long-term debt	193,672	175,722
Other long-term liabilities	118,094	38,770
Total liabilities	1,990,412	1,843,636
Net assets:		
Without donor restrictions	820,414	745,282
With donor restrictions	114,183	126,889
Total net assets	934,597	872,171
Total liabilities and net assets	\$2,925,009	\$2,715,807

Note 1: In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new standard intends to simplify the presentation of financial information for not-for-profits, specifically with respect to liquidity, financial performance, and cash flows, and to provide more relevant information to donors, grantors, creditors, and other users. This includes areas such as net asset classification, investment return, expenses, and liquidity and availability of resources. Ochsner adopted ASU 2016-14 in its consolidated financial statements effective December 31, 2018, applying retrospectively to all periods presented. The impact of adoption changes the classification of net assets on the consolidated balance sheets and consolidated statements of changes in net assets from three classes of net assets to two classes of net assets. The impact of adopting ASU 2016-14 had no impact to total unrestricted revenues, excess of revenues over expenses, or total net assets. All 2017 amounts have been restated to comply with this new pronouncement.

Ochsner Clinic Foundation
Condensed Consolidated Statements of Cash Flows
For the Years Ended December 31, 2018 and 2017
(In Thousands)

	<u>2018</u>	<u>2017</u>
<u>Cash Flows from Operating Activities:</u>		
Increase in net assets	\$ 62,426	\$ 161,153
Adjustments to reconcile decrease in net assets to net cash provided by operating activities:		
Pension related changes other than net periodic pension costs	13,180	(2,674)
Depreciation and amortization	147,528	128,098
Non-cash portion of loss on early extinguishment of debt	-	8,793
Amortization of deferred financing costs and debt discounts	(441)	(591)
(Income) loss from equity-method investment, net of cash received	(1,040)	721
Net realized and unrealized (gains) losses on investments	37,910	(88,705)
Other reconciling items, net	(1,137)	(1,045)
Changes in operating assets and liabilities, net of acquisitions:		
Patient accounts receivable	(18,686)	3,299
Other current and noncurrent assets	(58,300)	(27,962)
Accounts payable	(12,420)	38,924
Accrued expenses and other liabilities	16,312	27,332
Net cash provided by operating activities	<u>185,332</u>	<u>247,343</u>
<u>Cash Flows from Investing Activities:</u>		
Purchases of assets whose use is limited and other investments	(152,872)	(389,924)
Sales and maturities of assets whose use is limited and other investments	246,905	339,601
Capital expenditures	(269,054)	(228,542)
Purchase of interest in equity-method investments	(35,349)	-
Acquisitions of businesses, net of \$2,396 cash acquired in 2018	848	(30,816)
Other	936	313
Net cash used in investing activities	<u>(208,586)</u>	<u>(309,368)</u>
<u>Cash Flows from Financing Activities:</u>		
Repayment of bonds payable and long-term debt	(15,885)	(323,471)
Proceeds from bonds payable and long-term borrowings	-	458,024
Payments of debt financing costs	-	(4,288)
Payments on capital lease obligations	(10,245)	(4,258)
Proceeds from contributions restricted for long-term investments	587	850
Net cash (used in) provided by financing activities	<u>(25,543)</u>	<u>126,857</u>
Net (Decrease) Increase in Cash and Cash Equivalents	(48,797)	64,832
Cash and Cash Equivalents, Beginning of Year	186,401	121,569
Cash and Cash Equivalents, End of Year	<u>\$ 137,604</u>	<u>\$ 186,401</u>

OCHSNER CLINIC FOUNDATION UTILIZATION STATISTICS

	2016	2017	2018
Licensed Beds (1)	1,284	1,388	1,556
Average Number of Beds in Use (2)	1,372	1,365	1,527
Discharges Including Newborn	67,454	70,052	69,861
Discharges Excluding Newborn	61,341	63,597	63,329
Patient Days Including Newborn	326,145	342,561	343,507
Patient Days Excluding Newborn	312,349	327,929	328,927
Average Daily Census (3)	853	898	903
Percent Occupancy (3)	62.20%	65.79%	59.16%
Average Length of Stay	4.8	4.9	4.9
Adjusted Patient Days (3)	659,409	699,547	739,904
Clinic Visits (4)	1,823,527	2,012,588	2,243,621
Clinic RVUs	6,050,375	6,584,475	7,226,658
Unique Clinic Patients (5)	446,515	513,328	573,754
Employed Physician FTEs	924	995	1,080
Transfers through Regional Referral Center	10,201	10,691	11,173

	Ochsner Medical Center	OMC West Bank	Ochsner St. Anne	OMC Baton Rouge	OMC North Shore	OMC Kenner	Ochsner Baptist Med. Ctr.	OMC Hancock	TOTAL
Licensed Beds (1)	687	165	35	150	168	110	139	102	1,556
Average Number of Beds in Use (2)	687	181	35	159	168	110	140	47	1,527
Discharges Including Newborn	27,616	8,089	2,076	8,353	4,774	7,569	10,557	827	69,861
Discharges Excluding Newborn	27,616	7,062	1,718	7,083	4,774	6,596	7,775	705	63,329
Patient Days Including Newborn	174,427	34,714	7,345	28,645	20,986	28,036	46,701	2,653	343,507
Patient Days Excluding Newborn	174,427	32,292	6,671	26,008	20,986	25,719	40,401	2,423	328,927
Average Daily Census (3)	478	88	18	71	57	70	111	9	903
Percent Occupancy (3)	69.56%	48.88%	52.22%	44.81%	34.22%	64.06%	79.06%	18.75%	59.16%
Average Length of Stay	6.3	4.3	3.5	3.4	4.4	3.7	4.4	3.2	4.9
Adjusted Patient Days (3)	335,327	75,975	33,937	85,354	42,157	67,795	88,394	10,965	739,904

(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. 2016 was 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, 2018 AND 2017**

Payor Groupings	12/31/2017	12/31/2018
Managed Medicare	24%	25%
Commercial	34%	33%
Medicaid	17%	18%
Medicare	21%	20%
Guarantor / Patients	2%	2%
Other	2%	2%
TOTAL	100%	100%

CONSOLIDATED FINANCIAL STATEMENTS

Ochsner Clinic Foundation and Subsidiaries
Years Ended December 31, 2018 and 2017
With Report of Independent Auditors

Ernst & Young LLP



Ochsner Clinic Foundation and Subsidiaries

Consolidated Financial Statements

Years Ended December 31, 2018 and 2017

Contents

Report of Independent Auditors..... 1

Consolidated Financial Statements

Consolidated Balance Sheets 3

Consolidated Statements of Operations 5

Consolidated Statements of Changes in Net Assets 6

Consolidated Statements of Cash Flows..... 7

Notes to Consolidated Financial Statements..... 8



Ernst & Young LLP
3900 One Shell Square
701 Poydras Street
New Orleans, LA 70139

Tel: +1 504 581 4200
Fax: +1 504 596 4233
ey.com

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 subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, 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 financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor’s Responsibility

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

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

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



Adoption of ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* and ASU No. 2016-14, *Presentation of Financial Statements of Not-For-Profit Entities*

As discussed in Note 1 to the consolidated financial statements, Ochsner Clinic Foundation changed its method of revenue recognition and financial statement presentation as a result of the adoption of Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*, and ASU 2016-14, *Presentation of Financial Statements of Not-For-Profit Entities*, respectively. Our opinion is not modified with respect to this matter.

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 subsidiaries at December 31, 2018 and 2017, 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 29, 2019

Ochsner Clinic Foundation and Subsidiaries

Consolidated Balance Sheets
(In Thousands)

	December 31,	
	2018	2017
Assets		
Current assets:		
Cash and cash equivalents	\$ 137,604	\$ 186,401
Assets limited as to use required for current liabilities	7,630	7,370
Patient accounts receivable	271,331	249,299
Accounts receivable other	149,190	104,827
Inventories	69,757	68,608
Prepaid expenses and other current assets	40,814	34,395
Estimated third-party payor settlements	27,448	22,224
Total current assets	<u>703,774</u>	<u>673,124</u>
Assets limited as to use:		
By Board for capital improvements, charity, research, and other	747,572	769,717
Under bond indenture agreements	–	95,106
Under self-insurance trust fund	10,024	9,301
Donor-restricted long-term investments	82,010	97,425
Total assets limited as to use	<u>839,606</u>	<u>971,549</u>
Less assets limited as to use required for current liabilities	<u>(7,630)</u>	<u>(7,370)</u>
Non-current assets limited as to use	831,976	964,179
Investments in unconsolidated affiliates, real estate, and other	83,409	19,644
Property – net	1,171,795	927,979
Goodwill	72,411	71,195
Intangible assets	11,477	12,354
Other assets	50,167	47,332
Total assets	<u><u>\$ 2,925,009</u></u>	<u><u>\$ 2,715,807</u></u>

Ochsner Clinic Foundation and Subsidiaries

Consolidated Balance Sheets
(In Thousands)

	December 31,	
	2018	2017
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 205,582	\$ 190,683
Accrued salaries, wages, and benefits	190,359	163,218
Deferred revenue	39,476	35,552
Estimated third-party payor settlements	5,079	4,275
Bonds payable – current portion	4,060	2,095
Notes payable – current	52,430	52,430
Long-term debt – current portion	15,606	13,299
Other current liabilities	43,230	33,266
Total current liabilities	<u>555,822</u>	<u>494,818</u>
Pension and postretirement obligations	141,993	147,596
Bonds payable	980,831	986,730
Long-term debt	193,672	175,722
Other long-term liabilities	118,094	38,770
Total liabilities	<u>1,990,412</u>	<u>1,843,636</u>
Commitments and contingencies (Notes 6 and 18)		
Net assets:		
Without donor restrictions	820,414	745,282
With donor restrictions	114,183	126,889
Total net assets	<u>934,597</u>	<u>872,171</u>
Total liabilities and net assets	<u>\$ 2,925,009</u>	<u>\$ 2,715,807</u>

See notes to financial statements.

Ochsner Clinic Foundation and Subsidiaries

Consolidated Statements of Operations
(In Thousands)

	Year Ended December 31,	
	2018	2017
Unrestricted revenues:		
Patient service revenue	\$ 2,595,675	\$ 2,301,804
Premium revenue	318,453	298,824
Other operating revenue	504,342	403,463
Net assets released from restrictions used for operations	5,155	6,319
Total unrestricted revenues	<u>3,423,625</u>	<u>3,010,410</u>
Expenses:		
Salaries and wages	1,505,643	1,359,294
Benefits	145,877	138,008
Medical services to outside providers	140,491	133,952
Medical supplies and services	653,371	570,155
Other operating expenses	671,492	560,994
Depreciation and amortization	147,528	128,098
Interest	52,411	49,762
Total expenses	<u>3,316,813</u>	<u>2,940,263</u>
Operating income	106,812	70,147
Non-operating gains (losses):		
Investment and other realized gains – net	34,557	47,147
Loss on early extinguishment of debt	–	(9,256)
Unrealized (losses) gains on investments – net	(68,569)	36,968
Total non-operating (losses) gains	<u>(34,012)</u>	<u>74,859</u>
Excess of revenues over expenses	<u>\$ 72,800</u>	<u>\$ 145,006</u>

See notes to financial statements.

Ochsner Clinic Foundation and Subsidiaries

Consolidated Statements of Changes in Net Assets
(In Thousands)

	Year Ended December 31,	
	2018	2017
Changes in net assets without donor restrictions		
Excess of revenues over expenses	\$ 72,800	\$ 145,006
Net assets released from restrictions used for capital acquisitions	15,511	636
Pension-related changes other than net periodic pension costs	(13,180)	2,674
Increase in net assets without donor restrictions	<u>75,131</u>	<u>148,316</u>
Changes in net assets with donor restrictions		
Contributions	10,797	13,852
Investment (loss) income	(2,836)	5,940
Net assets released from restrictions used for:		
Operations	(5,155)	(6,319)
Capital acquisitions	(15,511)	(636)
(Decrease) increase in net assets with donor restrictions	<u>(12,705)</u>	<u>12,837</u>
Increase in net assets	62,426	161,153
Net assets – beginning of year	872,171	711,018
Net assets – end of year	<u>\$ 934,597</u>	<u>\$ 872,171</u>

See notes to financial statements.

Ochsner Clinic Foundation and Subsidiaries

Consolidated Statements of Cash Flows (In Thousands)

	Year Ended December 31,	
	2018	2017
Operating activities		
Increase in net assets	\$ 62,426	\$ 161,153
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Pension-related changes other than net periodic pension costs	13,180	(2,674)
Depreciation and amortization	147,528	128,098
Non-cash portion of loss on early extinguishment of debt	–	8,793
Amortization of deferred financing costs and debt premiums and discounts	(441)	(591)
(Income) loss from equity-method investments, net of cash received	(1,040)	721
Net realized and unrealized losses (gains) on investments	37,910	(88,705)
Other, net	(1,137)	(1,045)
Changes in operating assets and liabilities, net of acquisitions:		
Patient accounts receivable	(18,686)	3,299
Other current and non-current assets	(58,300)	(27,962)
Accounts payable	(12,420)	38,924
Accrued expenses and other liabilities	16,312	27,332
Net cash provided by operating activities	185,332	247,343
Investing activities		
Purchases of assets whose use is limited and other investments	(152,872)	(389,924)
Sales and maturities of assets whose use is limited and other investments	246,905	339,601
Capital expenditures	(269,054)	(228,542)
Purchase of interest in equity-method investments	(35,349)	–
Acquisition of businesses, net of cash acquired of \$2,396 and \$5 in 2018 and 2017, respectively	848	(30,816)
Other	936	313
Net cash used in investing activities	(208,586)	(309,368)
Financing activities		
Repayment of bonds payable and long-term debt	(15,885)	(323,471)
Proceeds from long-term borrowings	–	458,024
Payments of debt financing costs	–	(4,288)
Payments on capital lease obligations	(10,245)	(4,258)
Proceeds from contributions restricted for long-term investments	587	850
Net cash (used in) provided by financing activities	(25,543)	126,857
Net (decrease) increase in cash and cash equivalents	(48,797)	64,832
Cash and cash equivalents – beginning of year	186,401	121,569
Cash and cash equivalents – end of year	\$ 137,604	\$ 186,401

See notes to financial statements.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements

December 31, 2018

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 134-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; operates a hospital in Bay St. Louis, Mississippi, that operates as Ochsner Hancock Medical Center; 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 hospitals and clinics located in Shreveport, Louisiana, and Monroe, Louisiana, known as Ochsner LSU Health System of North Louisiana (OLHS-NL).

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 8, 9, and 10.

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 net realizable 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):

	2018	2017
In one year or less	\$ 9,517	\$ 7,772
Between one and five years	17,655	22,103
Greater than five years	5,670	7,519
	<u>32,842</u>	<u>37,394</u>
Less discount (ranging from 0.72%–4.25% at December 31, 2018 and 2017) and allowance for uncollectible pledges	<u>(2,170)</u>	<u>(3,270)</u>
Pledges receivable – net	<u>\$ 30,672</u>	<u>\$ 34,124</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 and unrealized 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.

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) on investments on the consolidated statements of operations.

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 years ended December 31, 2018 and 2017.

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, 2018 or 2017.

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 \$6.5 million and \$4.6 million for the years ended December 31, 2018 and 2017, 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.

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 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 and concluded the fair value exceeded the carrying value, and no further action was required for 2018 or 2017.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Deferred Revenue

Deferred revenue 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 15).

In June 2017 and March 2018, 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 and Ochsner Medical Complex – The Grove (located in Baton Rouge, Louisiana), respectively. 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 agreements, Ochsner received payments totaling approximately \$32.8 million from the third-party vendor. Ochsner recorded these payments as deferred revenue within the consolidated balance sheets. The associated revenue is being amortized and recognized over the lives of the agreements and is included in other operating revenue in the accompanying consolidated statements of operations. Deferred revenue associated with these agreements totaled \$30.8 million and \$20.3 million as of December 31, 2018 and 2017, respectively.

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 \$11.7 million and \$12.3 million net of accumulated amortization at December 31, 2018 and 2017, 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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

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.

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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Net Assets

Resources are classified for reporting purposes as net assets without donor restrictions and net assets with donor restrictions, according to the absence or existence of donor-imposed restrictions.

Net Assets Without Donor Restrictions

Net assets without donor restrictions are those whose use by OCF has not been limited by donors and are available for general operating use. Board-designated net assets are net assets without donor restrictions that have been set aside by the Board for specific purposes.

Net Assets With Donor Restrictions

Net assets with donor restrictions are those assets, including contributions and accumulated investment returns, whose use by OCF has been limited by donors to a specific time, period, or purpose. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources are maintained in perpetuity to provide a permanent source of income. Donor-restricted gifts are recorded as an addition to net assets with donor restrictions in the period received. Earnings on donor-restricted gifts are recorded as investment income in net assets with donor restrictions and subsequently used in accordance with the donor's designation.

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 net assets without donor restriction, which are excluded from excess of revenues over expenses, consistent with industry practice, include 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)

Patient Service Revenue

Patient service revenue is reported at the amount that reflects the consideration Ochsner expects to be entitled for providing patient care. These amounts are due from patients, third-party payors (including managed care payors and government programs), and others, and include variable consideration for retroactive revenue adjustments due to settlement of reviews and audits. Generally, Ochsner bills the patients and third-party payors after the services are performed or shortly after discharge. Revenue is recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services provided by Ochsner. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected or actual charges. Ochsner believes that this method provides a reasonable depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients receiving inpatient acute care services. Ochsner measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. These services are considered to be a single performance obligation. Revenue for performance obligations satisfied at a point in time is recognized when services are provided. Management believes this method provides a faithful depiction of the transfer of services over the term of performance obligations based on the inputs needed to satisfy the obligations.

Because its performance obligations relate to contracts with a duration of less than one year, Ochsner has elected to apply the optional exemption provided in Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 606-10-60-14(a) and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

As provided for under the guidance, Ochsner does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Ochsner is utilizing the portfolio approach practical expedient in ASC 606 for contracts related to patient service revenue. Ochsner accounts for the contracts within each portfolio as a collective group, rather than individual contracts, based on the payment pattern expected in each portfolio category and the similar nature and characteristics of the patients within each portfolio. The portfolios consist of major payor classes for inpatient revenue and outpatient revenue. Based on historical collection trends and other analyses, Ochsner has concluded that revenue for a given portfolio would not be materially different from accounting for revenue on a contract-by-contract basis.

Ochsner has agreements with third-party payors that generally provide for payments at amounts different from Ochsner's established rates. For uninsured patients who do not qualify for charity care, Ochsner recognizes revenue based on established rates, subject to certain discounts and implicit price concessions in accordance with policy. Ochsner determines the transaction price based on standard charges for services provided, reduced by explicit price concessions provided to third-party payors, discounts provided to uninsured patients in accordance with policy, and implicit price concessions provided to uninsured patients. Explicit price concessions are based on contractual agreements, discount policies, and historical experience. Implicit price concessions represent differences between amounts billed and the estimated consideration Ochsner expects to receive from patients, which are determined based on historical collection experience, current market conditions, and other factors.

Generally, patients who are covered by third-party payors are responsible for patient responsibility balances, including deductible and coinsurance, which vary in amount. Ochsner estimates the transaction price for patients with deductibles and coinsurance based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any explicit price concessions, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change. Adjustments arising from a change in the transaction price were not significant in 2018 or 2017.

Provisions for third-party payor settlements and adjustments are estimated in the period the related services are provided and adjusted in future periods as additional information becomes available and final settlements are determined.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is a possibility that recorded estimates will change by a material amount.

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, 2018 and 2017, the estimated costs incurred by Ochsner to provide care to patients who met certain criteria under its charity care policy were approximately \$27.9 million and \$29.2 million, respectively.

Community Benefit

Ochsner and four other health care providers have formed nonprofit organizations with the purpose of creating 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, 2018 and 2017, were approximately \$84.0 million and \$28.4 million, respectively. In 2018, OCF made a \$56 million payment to OLHS-NL to promote common charitable goals through the support of educational opportunities for medical and clinical professionals in the provision of health care services for low-income and needy patients. These expenditures are included in other operating expenses in the consolidated statements of operations.

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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

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 \$1.0 million and \$4.3 million in other operating revenue in the accompanying consolidated statements of operations for 2018 and 2017, 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, 2018 and 2017. Ochsner accounts for EHR incentive payments under the grant accounting model as grants related to income.

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 within net assets with donor restrictions 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, net assets with donor restrictions are reclassified as net assets without donor restrictions 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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Bonds Payable

The fair values of Ochsner's revenue bonds are based on currently traded values of similar financial instruments as disclosed in Note 9.

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, 2018 and 2017, due to the variable nature of the interest rate or based on a comparison of its fixed rates to current market rates.

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 2015 through 2018 in Ochsner's main tax jurisdictions. The Tax Cuts and Jobs Act (the Tax Act) was enacted on December 22, 2017. The Tax 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 were previously tax deferred, and creates new taxes on certain foreign sourced earnings. For tax-exempt entities, the Tax 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. The Tax Act did not have a material impact on Ochsner's consolidated financial statements.

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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

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.

Recently Adopted Pronouncements

In May 2014, the FASB issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. ASU 2014-09 supersedes most current revenue recognition guidance, including industry-specific guidance, and requires expanded disclosures about revenue recognition to enable financial statement users to understand the nature, timing, amount, and uncertainty of revenue and cash flows arising from contracts with customers. Ochsner used a full retrospective method of application to adopt ASU 2014-09 on January 1, 2018. Ochsner performed an analysis of revenue streams and transactions under ASU 2014-09. In particular, for patient service revenue, Ochsner performed an analysis into the application of the portfolio approach as a practical expedient to group patient contracts with similar characteristics, such that revenue for a given portfolio would not be materially different than if it were evaluated on a contract-by-contract basis. Upon adoption, the majority of what was previously classified as provision for uncollectible accounts and presented as a reduction to patient service revenue on the consolidated statements of operations is treated as a price concession that reduces the transaction price, which is reported as patient service revenue. ASU 2014-09 also requires enhanced disclosures related to the disaggregation of revenue and signification judgments made in measurement and recognition. The impact of adopting ASU 2014-09 was not material to Ochsner's total unrestricted revenues, excess of revenues over expenses, or total net assets.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – 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

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

recognized in excess of revenues over expenses. The provisions of ASU 2016-01 were effective for Ochsner starting January 1, 2018. The adoption of ASU 2016-01 resulted in a reclassification of \$4.7 million of unrealized holding gains and losses on equity securities from other changes in unrestricted net assets to excess of revenues over expenses for the year ended December 31, 2017.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new standard intends to simplify the presentation of financial information for not-for-profits, specifically with respect to liquidity, financial performance, and cash flows, and to provide more relevant information to donors, grantors, creditors, and other users. This includes areas such as net asset classification, investment return, expenses, and liquidity and availability of resources. Ochsner adopted ASU 2016-14 in its consolidated financial statements effective December 31, 2018, applying retrospectively to all periods presented. The impact of adoption changes the classification of net assets on the consolidated balance sheets and consolidated statements of changes in net assets from three classes of net assets to two classes of net assets. Ochsner also added disclosure for the liquidity and availability of financial assets at the balance sheet date to meet cash needs for general expenditures within one year and disaggregated functional expense classifications by their nature expense classification. The impact of adopting ASU 2016-14 had no impact to Ochsner's total unrestricted revenues, excess of revenues over expenses, or total net assets.

Pending Accounting Pronouncements

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, on their 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 will be applied using a modified retrospective approach. The primary effect of the new standard will be to record right-of-use assets and obligations for current operating leases, which is estimated to increase assets and liabilities by approximately \$230.0 million on the consolidated balance sheet.

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 2016-15, *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, 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.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*, to provide guidance on the presentation of restricted cash or restricted cash equivalents in the statement of cash flows. The amendments require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The provisions of ASU 2016-18 are effective for Ochsner for the fiscal year starting January 1, 2019, and for interim periods starting January 1, 2020, and early adoption is permitted. Management is currently evaluating the impact of this pronouncement on Ochsner's consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, *Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*. The amendments in this update eliminate Step 2 from the goodwill impairment test in an effort to simplify the subsequent measurement of goodwill. Step 2 requires determining the fair value at the impairment testing date of assets and liabilities (including unrecognized assets and liabilities) following the procedure that would be required in determining the fair value of assets acquired and liabilities assumed in a business combination. The provisions of ASU 2017-04 are effective for Ochsner starting January 1, 2021, 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)

1. Summary of Significant Accounting Policies (continued)

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 for the fiscal year ending December 31, 2019, and for interim periods starting January 1, 2020, and early adoption is permitted. Ochsner adopted this pronouncement retrospectively effective January 1, 2019. As a result of this adoption, approximately \$4.9 million of net periodic pension benefit will be reclassified out of income from operations for 2018.

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The amendments in ASU 2018-08 clarify and improve the scope and the accounting guidance for contributions received and contributions made. The amendments in ASU 2018-08 provide guidance for evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) within the scope of Topic 958, *Not-for-Profit Entities*, or as exchange (reciprocal) transactions subject to other guidance, and for determining whether a contribution is conditional. The provisions of ASU 2018-08 are effective for Ochsner starting January 1, 2019, including interim periods within that reporting period. Management is currently evaluating the impact of this pronouncement on Ochsner's consolidated financial statements.

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

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.

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)

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. There were no transfers between Level 1 and Level 2 in the years ended December 31, 2018 and 2017.

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):

	Fair Value Measurements at Reporting Date Using			
	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)^(a)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Estimated Fair Value
December 31, 2018				
Money market funds	\$ 12,063	\$ –	\$ –	\$ 12,063
Fixed income investments	275,156	–	–	275,156
Marketable equity securities	92,310	–	–	92,310
Diversifiers	109,835	–	–	109,835
Natural resources and other	38,550	–	–	38,550
Total	<u>\$ 527,914</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 527,914</u>
December 31, 2017				
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
Total	<u>\$ 640,916</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 640,916</u>

^(a) 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 \$306.9 million and \$325.8 million at December 31, 2018 and 2017, respectively, are not included in these tables since they are accounted for using the equity method of accounting and not measured at fair value. As of December 31, 2018 and 2017, real estate investments of approximately \$7.6 million 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 \$13.8 million and \$17.2 million and realized net gains on sales of securities of approximately \$20.8 million and \$29.9 million for 2018 and 2017, respectively. Unrealized (losses) gains on alternative investments were approximately \$(29.1) million and \$32.3 million during 2018 and 2017, respectively, and unrealized (losses) gains on investments other than alternative investments were approximately \$(39.5) million and \$4.7 million during 2018 and 2017, respectively.

3. Patient Service Revenue

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

Medicare and Medicaid

Inpatient acute care services 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.

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 either on a cost basis subject to certain limits or on a prospectively determined amount per procedure.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

3. Patient Service Revenue (continued)

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation as well as significant regulatory action, and, in the normal course of business, Ochsner is subject to contractual review and audits, including audits initiated by the Medicare Recovery Audit Contract program. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term. Ochsner believes it is in compliance with applicable laws and regulations governing the Medicare and Medicaid programs and that adequate provisions have been made for any adjustments that may result from final settlements.

Settlements with third-party payors for retroactive adjustments due to review and audits are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care in the period the related services are provided. 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, correspondence from the payor and Ochsner's historical settlement activity, including an assessment to ensure that it is probable that a significant revenue reversal in the amount of the cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known or as years are settled or are no longer subject to such reviews and audits. Adjustments arising from a change in estimated settlements increased patient service revenue by \$1.4 million and \$1.9 million in 2018 and 2017, 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, 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. 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 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 2018 and 2017, Ochsner recognized approximately \$244.0 million and \$172.4 million, respectively, in patient service revenue related to the Program and recorded accounts receivable of approximately \$2.2 million as of December 31, 2018 and 2017. 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 \$318.5 million and \$298.8 million in 2018 and 2017, 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 \$140.5 million and \$134.0 million in 2018 and 2017, 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 \$218.0 million and \$208.5 million in 2018 and 2017, respectively, and is included in patient service revenue in the accompanying consolidated statements of operations.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

3. 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.

The table below shows the sources of patient service revenue for the years ended December 31 (in thousands).

	2018	2017
Commercial	\$ 1,259,855	\$ 1,131,976
Medicaid	522,434	408,593
Medicare	461,722	447,844
Managed Medicare	337,980	293,740
Guarantor/patients/other	13,684	19,651
Patient service revenue	\$ 2,595,675	\$ 2,301,804

4. Patient Accounts Receivable

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

	2018	2017
Commercial	\$ 164,171	\$ 142,355
Medicaid	28,946	24,004
Medicare	39,849	42,175
Managed Medicare	32,322	34,784
Guarantor/patients/other	6,043	5,981
Total patient accounts receivable – net	\$ 271,331	\$ 249,299

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

5. Liquidity and Availability

Financial assets available for general expenditure within one year of December 31, 2018, include the following (in thousands):

Cash and cash equivalents	\$	137,604
Patients accounts receivable		271,331
Accounts receivable other		149,190
Assets limited to use by Board for capital improvements, charity, research, and other		<u>747,572</u>
	\$	<u>1,305,697</u>

Ochsner has assets limited as to use held by trustees under self-insurance trust agreements and investments restricted by donors. These investments are not reflected in the amounts above.

As part of Ochsner's liquidity management plan, cash in excess of daily requirements for general expenditures is invested in long-term investments. Ochsner's long-term investment portfolio contains money market funds and other liquid investments that can be drawn upon, if necessary, to meet liquidity needs.

Ochsner also maintains a \$53.0 million credit line as discussed in Note 8.

6. Property – Net

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

	<u>2018</u>	<u>2017</u>
Land and improvements	\$ 112,486	\$ 107,014
Buildings and leasehold improvements	934,174	832,485
Equipment, furniture, and fixtures	1,310,928	1,142,190
Construction-in-progress	217,600	124,664
Total property – at cost	<u>2,575,188</u>	<u>2,206,353</u>
Less accumulated depreciation	1,403,393	1,278,374
Property – net	<u>\$ 1,171,795</u>	<u>\$ 927,979</u>

Depreciation and amortization expense totaled approximately \$147.5 million and \$128.1 million for the years ended December 31, 2018 and 2017, respectively.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

6. Property – Net (continued)

At December 31, 2018 and 2017, Ochsner has purchase commitments totaling approximately \$49.5 million and \$105.7 million, respectively, toward additional capital expenditures.

Ochsner leases certain real estate, 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):

	<u>2018</u>	<u>2017</u>
Real estate	\$ 63,340	\$ –
Software and equipment	29,816	26,158
Accumulated amortization	(18,736)	(10,322)
Net carrying value of capital lease assets	<u>\$ 74,420</u>	<u>\$ 15,836</u>

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

7. 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 January 9, 2017, Ochsner completed the acquisition of Millennium Healthcare Management, Inc. (MHM). As part of this transaction, Ochsner recorded approximately \$28.0 million of goodwill and \$0.9 million of other intangible assets related to the acquisition.

On January 2, 2018, Ochsner completed the acquisition of New Orleans Urgent Care (NOUC). As part of this transaction, Ochsner recorded approximately \$1.1 million of goodwill related to the acquisition.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

7. Goodwill and Intangible Assets (continued)

On January 19, 2018, Ochsner completed an asset purchase agreement with NOLA Weightloss, LLC. As part of this transaction, Ochsner recorded approximately \$0.1 million of goodwill related to the acquisition.

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

	<u>2018</u>	<u>2017</u>
Goodwill	\$ 72,411	\$ 71,195
Trade name – intangible assets	\$ 11,433	\$ 11,433
Other – intangible assets	44	921
	<u>\$ 11,477</u>	<u>\$ 12,354</u>

8. 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 9, 2019. 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, 2018 and 2017. As of December 31, 2018 and 2017, Ochsner had borrowings outstanding under this 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 3.60% and 2.86% at December 31, 2018 and 2017, respectively. All amounts are classified as current at December 31, 2018 and 2017.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

9. 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.

	2018	2017
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	\$ 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	154,060
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%	108,680	110,775
Series 2015 taxable bonds issued June 2015, due in 2045, annual interest rate at 5.90%	252,820	252,820
Unamortized net bond premium	57,216	59,416
Total	994,331	998,626
Less deferred financing costs	9,440	9,801
Less current portion	4,060	2,095
Non-current portion of bonds payable	\$ 980,831	\$ 986,730

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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

9. Bonds Payable (continued)

In May 2017, the LPFA 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 were used to provide funding for various Ochsner capital projects.

At December 31, 2018, 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:	
2019	\$ 4,060
2020	5,590
2021	7,210
2022	7,580
2023	7,955

The estimated fair value of the Series 2015 tax-exempt bonds, Series 2015 taxable bonds, Series 2016 tax-exempt bonds, and Series 2017 tax-exempt bonds as of December 31, 2018 and 2017, is approximately \$1.1 billion. This fair value is based on quoted market prices for similarly rated health care revenue bond issues, a Level 2 input.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

10. Long-Term Debt

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

	2018	2017
Working capital note, due May 2026 (subject to six additional 5-year extensions), including accrued interest at rates varying from 1.71% to 2.33% during 2018 with a rate of 2.16% as of December 31, 2018	\$ 8,912	\$ 8,732
Note payable 4.61% Senior Secured Note, entered into March 2013, due March 2033	5,596	5,868
Note payable 5.26% Senior Secured Note, entered into December 2013, due December 2028	47,212	50,709
Promissory note entered into December 2013, due December 2020 with interest synthetically fixed at 3.97%	10,548	12,623
Note payable 5.09% Senior Secured Note, entered into July 2014, due August 2034	68,820	71,622
Promissory note entered into October 2014, due October 2021 with interest at 3.75%	16,133	17,600
Promissory note entered into September 2015, due September 2022 with interest synthetically fixed at 4.13%	21,000	24,000
Promissory note entered into September 2018, due September 2023 with interest at 2.47%	27,424	–
Promissory note entered into October 2018, due September 2021 with interest at 5.50%	5,767	–
Software and equipment loans, due varying dates in 2016–2019	148	341
Total long-term debt	211,560	191,495
Less deferred financing costs	2,281	2,470
Less unamortized discount	1	4
Less current portion	15,606	13,299
Non-current portion of long-term debt	\$ 193,672	\$ 175,722

St. Anne

On May 1, 2006, Ochsner entered into lease and management services agreements with Lafourche Parish Hospital Service District No. 2 (Lafourche), which owned and operated 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

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

10. Long-Term Debt (continued)

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 2.16% and 1.76% at December 31, 2018 and 2017, respectively. All amounts are classified as non-current at December 31, 2018 and 2017, 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)

10. 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, 2018 and 2017, the fair value of the interest rate swap agreement was an asset of \$84,000 and \$8,000, respectively, and is included within other assets 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)

10. 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 \$367,000 and \$212,000 at December 31, 2018 and 2017, respectively, and is included within other assets in the consolidated balance sheets.

September 2018 Promissory Note

OCF entered into a promissory note with CHRISTUS Health for the principal amount of approximately \$27.8 million on September 1, 2018, in connection with Ochsner's equity method investment in CHRISTUS Health Southwestern Louisiana discussed in Note 14. The CHRISTUS Health promissory note bears stated interest of 2.47% on the outstanding principal balance. The security includes a pledge of all present and future accounts receivable of OCF and a mortgage of certain property. Interest-only payments are due quarterly with the first payment due on October 1, 2018, based upon a 5-year fixed interest payment amortization period. The balance of the outstanding principal is due on a 5-year maturity date of September 1, 2023, and actual/360-day interest period.

October 2018 Promissory Note

OCF entered into a promissory note with Biomedical Research Foundation of Northwest Louisiana (BRF) for an unsecured loan with the principal amount of approximately \$6.3 million on October 1, 2018, in connection with Ochsner's acquisition of EHR licenses for the management of OLHS-NL as discussed in Note 13. The BRF promissory note bears stated interest of 5.50% on

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

10. Long-Term Debt (continued)

the outstanding principal balance. Principal and interest payments are due monthly with the first payment due on October 31, 2018, based upon a three-year fixed interest payment amortization period. The balance of the outstanding principal is due on a 3-year maturity date of September 30, 2021, and actual/360-day interest period.

At December 31, 2018, scheduled repayments of long-term debt for the next five fiscal years are as follows (in thousands):

Years ending December 31:	
2019	\$ 15,606
2020	22,334
2021	25,530
2022	20,075
2023	35,925

11. 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 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, accrued 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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

11. Employee Benefit Plans (continued)

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

	December 31,	
	2018	2017
Change in benefit obligation:		
Benefit obligation – beginning of year	\$ 577,926	\$ 553,815
Interest cost	21,074	22,477
Actuarial (gain) loss	(35,009)	27,296
Benefits paid	(26,915)	(25,662)
Benefit obligation – end of year	<u>537,076</u>	<u>577,926</u>
Change in plan assets:		
Fair value of plan assets – beginning of year	446,352	404,409
Actual return on plan assets	(22,584)	52,514
Employer contributions	13,883	15,091
Benefits paid	(26,914)	(25,662)
Fair value of plan assets – end of year	<u>410,737</u>	<u>446,352</u>
Funded status	<u>\$ (126,339)</u>	<u>\$ (131,574)</u>
	December 31,	
	2018	2017
Amounts recognized in the consolidated balance sheets consist of:		
Pension and postretirement obligations – non-current portion	\$ (126,339)	\$ (131,574)
Unrestricted net assets	N/A	N/A
Amounts recognized in unrestricted net assets:		
Net actuarial loss	<u>265,183</u>	<u>251,647</u>
Total amounts recognized	265,183	251,647
Other changes in plan assets and benefit obligations recognized in unrestricted net assets:		
Net loss	21,546	5,518
Recognized loss	(8,010)	(7,716)
Total amounts recognized	<u>\$ 13,536</u>	<u>\$ (2,198)</u>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

11. Employee Benefit Plans (continued)

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

	<u>2018</u>	<u>2017</u>
Weighted average discount rate	4.33%	3.70%
Rate of compensation increase	N/A	N/A

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

	<u>2018</u>	<u>2017</u>
Interest cost	\$ 21,074	\$ 22,477
Expected return on plan assets	(33,972)	(30,735)
Amortization of net loss	8,010	7,716
Net periodic pension benefit	<u>\$ (4,888)</u>	<u>\$ (542)</u>

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

	<u>2018</u>	<u>2017</u>
Weighted-average discount rate	3.70%	4.15%
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)

11. Employee Benefit Plans (continued)

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

	Fair Value Measurements at Reporting Date Using			
	Quoted Prices in Active Markets for Observable Identical Assets and Liabilities (Level 1) ^(a)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Estimated Fair Value
2018				
Money market funds	\$ 7,953	\$ —	\$ —	\$ 7,953
Fixed income investments	15,263	—	—	15,263
Marketable equity securities	31,242	—	—	31,242
Absolute return	39,272	—	—	39,272
Natural resources	26,846	—	—	26,846
Total	<u>\$ 120,576</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 120,576</u>
2017				
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>

^(a) 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 \$290.2 million and \$300.8 million at December 31, 2018 and 2017, respectively, which are measured at fair value using net asset value as a practical expedient.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

11. Employee Benefit Plans (continued)

The Defined Benefit Plan asset allocation as of the measurement dates (December 31, 2018 and 2017) and the target asset allocation, presented as a percentage of total plan assets, were as follows:

	2018	2018 Target Allocation	2017
Debt securities	13%	15%	13%
Equity securities	38	40	42
Private equity/venture capital	3	2	3
Hedge funds	34	33	27
Natural resources/REITs	10	10	10
Other	2	–	5

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)

11. 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 \$11.6 million in 2019.

For 2018 and 2017, Ochsner's Defined Benefit Plan had accumulated benefit obligations of approximately \$537.1 million and \$577.9 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 \$8.7 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, 2018, are as follows (in thousands):

Years ending December 31:	
2019	\$ 29,296
2020	30,637
2021	31,988
2022	33,197
2023	34,349
2024–2028	180,126
	<u>\$ 339,593</u>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

11. 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, 2018 and 2017, OHS has accrued approximately \$32.4 million and \$30.2 million, respectively, for matching contributions to the Plan for the 2018 and 2017 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 \$14.3 million and \$13.9 million for the 457(f) plan at December 31, 2018 and 2017, 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 \$1.2 million and \$1.6 million at December 31, 2018 and 2017, respectively.

12. Endowment Funds and Net Assets With Donor Restrictions

Ochsner has 917 donor-restricted funds established for a variety of purposes. Endowment funds are classified and reported based on donor-imposed restrictions as net assets with donor restrictions. Net assets with donor restrictions include funds dedicated to Medical Education, Nursing Education, Pastoral Care, Biomedical Research, Cancer Research, Cardiology Research, Transplant Research, and Alzheimer's Research, and other purposes.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

12. Endowment Funds and Net Assets With Donor Restrictions (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 that Ochsner preserve the historic dollar value of the donor-restricted endowed funds. As a result of this interpretation, Ochsner classifies as net assets with donor restrictions 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. The remaining portion of the donor-restricted endowment fund that is not classified in the permanent endowment is available for appropriation for expenditure by Ochsner in a manner consistent with the standard for expenditure prescribed by UPMIFA. Net assets with donor restriction available for appropriations as of December 31, 2018 and 2017, total approximately \$8.7 million and \$7.8 million, respectively.

Restricted Net Assets as of December 31, by Purpose

	2018	2017
	<i>(In Thousands)</i>	
Research	\$ 34,704	\$ 35,904
Education	9,653	9,793
Other	69,826	81,192
Total	\$ 114,183	\$ 126,889

Endowment Net Asset Composition by Type of Fund as of December 31, 2018

	Without Donor Restriction	With Donor Restriction	Total
	<i>(In Thousands)</i>		
Donor-restricted funds	\$ –	\$ 38,377	\$ 38,377
Board-designated funds	1,434	–	1,434
Total	\$ 1,434	\$ 38,377	\$ 39,811

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

12. Endowment Funds and Net Assets With Donor Restrictions (continued)

Endowment Net Asset Composition by Type of Fund as of December 31, 2017

	Without Donor Restriction	With Donor Restriction	Total
	<i>(In Thousands)</i>		
Donor-restricted funds	\$ —	\$ 41,246	\$ 41,246
Board-designated funds	1,559	—	1,559
Total	\$ 1,559	\$ 41,246	\$ 42,805

Changes in Endowment Net Assets for the Year Ended December 31, 2018

	Without Donor Restriction	With Donor Restriction	Total
	<i>(In Thousands)</i>		
Beginning balance	\$ 1,559	\$ 41,246	\$ 42,805
Investment loss	(97)	(2,532)	(2,629)
Contributions	—	595	595
Appropriations for expenditures	(28)	(932)	(960)
Ending balance	\$ 1,434	\$ 38,377	\$ 39,811

Changes in Endowment Net Assets for the Year Ended December 31, 2017

	Without Donor Restriction	With Donor Restriction	Total
	<i>(In Thousands)</i>		
Beginning balance	\$ 1,391	\$ 36,232	\$ 37,623
Investment gain	194	5,046	5,240
Contributions	—	835	835
Appropriations for expenditures	(26)	(867)	(893)
Ending balance	\$ 1,559	\$ 41,246	\$ 42,805

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

12. Endowment Funds and Net Assets With Donor Restrictions (continued)

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, 2018 or 2017.

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.

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. Net assets with donor restrictions include the spending appropriation and investment income of the endowments and are pending appropriation for expenditure consistent with the specific purpose of the fund.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

13. Business Combinations, Strategic Partnerships, and Affiliation Agreements

Business Combinations

On January 9, 2017, Ochsner completed the acquisition of 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 Ochsner's consolidated financial statements from the date of acquisition.

On January 2, 2018, Ochsner completed the acquisition of NOUC, which consists of two urgent care clinics, for approximately \$1.2 million in cash. Results of operations of NOUC have been 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.

On April 1, 2018, Ochsner completed an agreement to lease Hancock Medical Center (Hancock), 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 acquired the current assets, liabilities, and provider number of Hancock, and received \$2.4 million in cash. Results of operations of Hancock have been included in Ochsner's consolidated financial statements from the transaction date.

During 2018 and 2017, Ochsner completed several physician practice acquisitions, none of which were material to the results of operations.

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, and CHRISTUS Health Louisiana.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

13. Business Combinations, Strategic Partnerships, and Affiliation Agreements (continued)

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, SBPH, and, beginning October 2018, OLHS-NL. Under the management agreements for Chabert, SCPH, and SBPH, 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. Prior to April 1, 2018, Ochsner had a management agreement with Hancock. Under its management agreement with Hancock, Ochsner received management fees as well as reimbursement of expenses incurred for providing management assistance and support services.

Effective October 1, 2018, OCF entered into management agreements with a newly formed nonprofit entity OLHS-NL to provide management services, billing and collection services, and administrative support for certain hospital and health care operations in Shreveport and Monroe. OCF and the Board of Supervisors of Louisiana State University and Agricultural and Mechanical College (LSU) formed OLHS-NL to assume overall responsibility for the operations and clinical activities of the former University Health hospitals and clinics in Shreveport and Monroe and coordinate the activities between LSU Medical School, the parties' physicians, and the health care operations in Shreveport and Monroe. OLHS-NL is a stand-alone nonprofit organization and is not a subsidiary of either LSU or OCF. OLHS-NL's Bylaws require that LSU and OCF each appoint an equal number of directors to the OLHS-NL Board to oversee, coordinate, and manage OLHS-NL's activities.

In conjunction with the management agreement of OLHS-NL, Ochsner acquired the EHR licenses and related liabilities, and hired the Information Services (IS) employees of OLHS-NL in exchange for a note payable of approximately \$6.2 million to the BRF on October 1, 2018. With this acquisition, Ochsner fully manages the IS function of OLHS-NL.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

13. Business Combinations, Strategic Partnerships, and Affiliation Agreements (continued)

Subsequent Event

On March 27, 2019, Ochsner announced its intent to partner with St. Mary Parish Hospital Service District 2 to lease and operate Teche Regional Medical Center, located in Morgan City, Louisiana. The agreement is expected to close during the fourth quarter of 2019 once approved by the Attorney General.

14. 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):

	Ownership Interest	Investment in Equity Investees	Equity in Income of Equity Investees
2018			
Southeast Louisiana Homecare LLC	25%	\$ 2,981	\$ 307
Louisiana Extended Care Hospital of Kenner, LLC	25%	–	(356)
OSR Louisiana, LLC	49%	–	(172)
Ochsner-Acadia, LLC	25%	5,878	(708)
OMC West JV, LLC	49%	5,380	47
NSR Louisiana LLC	30%	237	–
CHRISTUS Health Southwestern Louisiana	40%	65,850	3,426
		<u>\$ 80,326</u>	<u>\$ 2,544</u>
2017			
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>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

14. Equity Method Investments and Joint Ventures (continued)

Ochsner has two joint ventures with LHC Group, Inc. Ochsner owns a 25% interest in Southeast Louisiana Homecare, LLC, and Louisiana Extended Care Hospital of Kenner, LLC, while LHC Group, Inc. owns 75% interest in these entities. The results of these joint ventures were not material to Ochsner's consolidated financial statements in 2018 or 2017.

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. The results of this joint venture were not material to Ochsner's consolidated financial statements in 2018 or 2017.

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 for a 25% interest in the joint venture and Acadia contributed 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 in 2018 or 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 houses three separate health care components, including long-term acute care, inpatient rehabilitation, and a skilled nursing facility. Ochsner is the lessee of the building and makes minimum lease payments to OMC West for this lease totaling approximately \$43.5 million at inception over 10 years. Ochsner also subleases space to its equity-method investments OSR Louisiana, LLC, and Louisiana Extended Care Hospital of Kenner, LLC, and at inception, will receive approximately \$39.8 million over 10 years. These lease amounts are included in Ochsner's lessee and lessor commitments disclosed in Note 18 to the consolidated financial statements. The results of Ochsner's equity-method investment in OMC West were not material in 2018 or 2017.

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) in exchange for cash of \$35.0 million and a promissory note of \$27.8 million. SWLA owns and operates health care facilities and operations related to physician

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

14. Equity Method Investments and Joint Ventures (continued)

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 agreement was finalized September 1, 2018, once regulatory approval was received.

On August 22, 2018, Ochsner entered into a joint venture with Select Medical Corporation, St. Tammany Parish Hospital, and Slidell Memorial Hospital to own and operate an inpatient rehabilitation hospital on the Northshore, NSR Louisiana, LLC. Ochsner purchased a 30% interest in this new entity for \$237,000. The rehabilitation hospital is expected to open in Lacombe, Louisiana, in the fall of 2019.

15. 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 EHR 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. During 2018, Ochsner implemented its EHR system with its equity method investment in Louisiana Extended Care Hospital of Kenner, LLC and continues to host and maintain it.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

16. Functional Expenses

Ochsner provides general health care services primarily to residents within its geographic location.

Functional Expenses as of December 31, 2018							
Health Care Services	Medical Education	Research	Fitness Center	Hotel	General and Administrative	Total	
<i>(In Thousands)</i>							
Salaries, wages, and benefits	\$ 1,267,307	\$ 22,472	\$ 13,399	\$ 6,429	\$ 1,403	\$ 340,510	\$ 1,651,520
Medical services to outside providers	140,491	–	–	–	–	–	140,491
Medical supplies and services	653,164	61	128	15	3	–	653,371
Other operating expenses	212,790	6,730	2,594	4,779	1,575	443,024	671,492
Depreciation and amortization	47,708	820	579	747	472	97,202	147,528
Interest	2,166	–	–	–	233	50,012	52,411
	<u>\$ 2,323,626</u>	<u>\$ 30,083</u>	<u>\$ 16,700</u>	<u>\$ 11,970</u>	<u>\$ 3,686</u>	<u>\$ 930,748</u>	<u>\$ 3,316,813</u>

Functional Expenses as of December 31, 2017							
Health Care Services	Medical Education	Research	Fitness Center	Hotel	General and Administrative	Total	
<i>(In Thousands)</i>							
Salaries, wages, and benefits	\$ 1,106,530	\$ 21,192	\$ 11,990	\$ 6,263	\$ 1,305	\$ 350,022	\$ 1,497,302
Medical services to outside providers	133,952	–	–	–	–	–	133,952
Medical supplies and services	566,225	21	155	7	3	3,744	570,155
Other operating expenses	211,596	8,174	2,506	4,634	1,659	332,425	560,994
Depreciation and amortization	40,374	632	550	730	508	85,304	128,098
Interest	141	–	–	–	143	49,478	49,762
	<u>\$ 2,058,818</u>	<u>\$ 30,019</u>	<u>\$ 15,201</u>	<u>\$ 11,634</u>	<u>\$ 3,618</u>	<u>\$ 820,973</u>	<u>\$ 2,940,263</u>

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

17. Supplemental Disclosures of Cash Flow Information

	Year Ended December 31,	
	2018	2017
	<i>(In Thousands)</i>	
Cash paid for interest (net of amounts capitalized)	\$ 52,859	\$ 49,871
Supplemental non-cash investing and financing activities:		
Property purchases included in accounts payable	\$ 37,553	\$ 14,186
Property purchases financed by capital leases and long-term debt	\$ 72,361	\$ 2,852
Purchase of interest in equity-method investment financed by long-term note	\$ 27,424	\$ –
Acquisitions of businesses financed by capital leases and long-term debt	\$ 20,839	\$ –

18. 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, 2018, may result in the assertion of additional claims.

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

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 leased and managed hospitals that carry similar coverage with lower self-retention and aggregate levels.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

18. Commitments and Contingencies (continued)

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, 2018 and 2017, were approximately \$18.2 million and \$18.8 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 \$10.0 million and \$9.3 million at December 31, 2018 and 2017, 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 \$14.3 million with no estimated reinsurance recoveries at December 31, 2018, and \$14.1 million with no estimated reinsurance recoveries at December 31, 2017. 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, 2018 and 2017. 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.

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 \$21.1 million and \$17.6 million at December 31, 2018 and 2017, respectively, which is included in accrued salaries, wages, and benefits; other current liabilities; and other long-term liabilities in the accompanying consolidated balance sheets.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

18. Commitments and Contingencies (continued)

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.

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, 2018 (in thousands):

	Lease Obligations	
	Capital	Operating
2019	\$ 12,451	\$ 44,867
2020	10,874	36,967
2021	9,927	32,497
2022	7,685	29,264
2023	6,953	23,999
Thereafter	83,414	155,273
Total minimum lease payments	131,304	\$ 322,867
Less amounts representing interest	(31,326)	
	99,978	
Less current maturities	(9,648)	
Capital lease obligations – non-current	\$ 90,330	

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

18. Commitments and Contingencies (continued)

Rent expense, which includes operating leases and cancelable short-term rental agreements, was approximately \$64.0 million for the years ended December 31, 2018 and 2017.

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 year of future minimum rental payments under non-cancelable operating leases as of December 31, 2018 (in thousands):

Years ending December 31:	
2019	\$ 9,720
2020	7,844
2021	7,325
2022	6,932
2023	6,162
Thereafter	<u>37,574</u>
Total minimum lease payments to be received	<u>\$ 75,557</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.

Ochsner Clinic Foundation and Subsidiaries

Notes to Consolidated Financial Statements (continued)

18. Commitments and Contingencies (continued)

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 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.

19. Subsequent Events

Ochsner has evaluated subsequent events through April 29, 2019, the date the accompanying consolidated financial statements were available for issuance.

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

© 2019 Ernst & Young LLP.
All Rights Reserved.

ey.com