

CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Saint Peter's Healthcare System, Inc.
Years Ended December 31, 2019 and 2018
With Report of Independent Auditors

Ernst & Young LLP



Saint Peter’s Healthcare System, Inc.

Consolidated Financial Statements
and Supplementary Information

Years Ended December 31, 2019 and 2018

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Report of Independent Auditors

The Board of Governors
Saint Peter's Healthcare System, Inc.

We have audited the accompanying consolidated financial statements of Saint Peter's Healthcare System, Inc. (the System), which comprise the consolidated balance sheets as of December 31, 2019 and 2018, and the related consolidated statements of operations and 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 Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Risk Assurance Company of Saint Peter's University Hospital (RAC), a wholly-owned subsidiary, which statements reflect total assets of \$26,303,000 and \$24,031,000 as of December 31, 2019 and 2018, respectively. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for RAC, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

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

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

Opinion

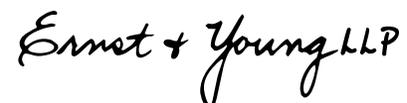
In our opinion, based on our audits and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Saint Peter's Healthcare System, Inc. at December 31, 2019 and 2018, and the consolidated results of its operations and changes in net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Adoption of ASU No. 2016-02, *Leases*

As discussed in Note 1 to the consolidated financial statements, the System changed its method of accounting for leases as a result of the adoption of the amendments to the Financial Accounting Standards Board Accounting Standards Codification resulting from Accounting Standards Update No. 2016-02, *Leases*, effective January 1, 2019. Our opinion is not modified with respect to this matter.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating balance sheet and consolidating statement of operations and changes in net assets as of and for the year ended December 31, 2019 are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, based on our audits and the report of other auditors, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.



April 24, 2020

Saint Peter's Healthcare System, Inc.

Consolidated Balance Sheets
(In Thousands)

	December 31	
	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 22,383	\$ 22,854
Patient accounts receivable, net	51,190	48,987
Assets whose use is limited, current portion	122,824	105,180
Supplies	5,450	5,013
Estimated third-party payor settlements, current portion	507	299
Other current assets	14,581	12,051
Total current assets	216,935	194,384
Assets whose use is limited, less current portion	39,975	37,697
Property, plant, equipment, and construction, net	188,630	197,641
Estimated third-party payor settlements, less current portion	516	246
Operating lease assets	13,034	–
Investments in joint ventures and other assets	6,472	6,511
	\$ 465,562	\$ 436,479
Liabilities and net assets		
Current liabilities:		
Current portion of long-term debt	\$ 8,635	\$ 11,413
Accounts payable	25,940	26,475
Accrued expenses and other liabilities	38,914	36,121
Accrued interest	3,933	4,066
Current portion of operating lease liability	3,331	–
Estimated third-party payor settlements, current portion	2,308	2,795
Total current liabilities	83,061	80,870
Long-term debt, less current portion	139,946	146,965
Operating lease liability, less current portion	9,703	–
Estimated third-party payor settlements, less current portion	2,731	1,599
Accrued pension liability	142,803	129,274
Other liabilities	27,753	24,225
Total liabilities	405,997	382,933
Commitments and contingencies		
Net assets:		
Net assets without donor restrictions	54,616	47,498
Net assets with donor restrictions	4,949	6,048
Total net assets	59,565	53,546
	\$ 465,562	\$ 436,479

See accompanying notes.

Saint Peter's Healthcare System, Inc.

Consolidated Statements of Operations and Changes in Net Assets
(In Thousands)

	Year Ended December 31	
	2019	2018
Revenue, gains, and other support:		
Net patient service revenue	\$ 466,802	\$ 458,334
Other operating revenue	33,126	30,266
Net assets released from restriction	2,299	1,502
Total revenue, gains, and other support	502,227	490,102
Expenses:		
Salaries and wages	236,143	229,950
Resident and physician fees	11,064	11,594
Employee benefits	53,174	53,728
Supplies and other	149,871	141,615
Governmental taxes, fees, and assessments	3,298	3,893
Interest	9,073	9,528
Depreciation and amortization	25,517	24,726
Total expenses	488,140	475,034
Income from operations	14,087	15,068
Severance costs	-	(6)
Equity in net earnings of joint ventures and other income	485	906
Gain on sale of property, plant, and equipment	68	677
Net change in unrealized gains and losses on equity investments	6,325	-
Non-operating net periodic pension cost	(3,994)	(1,396)
Excess of revenue over expenses	16,971	15,249
Net change in unrealized gains and losses on other-than-trading investments	2,199	(3,582)
Change in pension liability to be recognized in future periods	(14,263)	4,086
Donated equipment and other	2,145	3,998
Increase in net assets without donor restrictions before discontinued operations	7,052	19,751
Gain (loss) from discontinued skilled nursing facility	66	(13)
Increase in net assets without donor restrictions	7,118	19,738

Continued on next page.

Saint Peter's Healthcare System, Inc.

Consolidated Statements of Operations and Changes in Net Assets (continued)
(In Thousands)

	Year Ended December 31	
	2019	2018
Increase in net assets without donor restrictions	\$ 7,118	\$ 19,738
Net assets with donor restrictions:		
Restricted gifts and contributions and related items, net	1,200	(22)
Net assets released from restriction	(2,299)	(1,502)
Decrease in net assets with donor restrictions	(1,099)	(1,524)
Increase in net assets	6,019	18,214
Net assets at beginning of year	53,546	35,332
Net assets at end of year	\$ 59,565	\$ 53,546

See accompanying notes.

Saint Peter's Healthcare System, Inc.

Consolidated Statements of Cash Flows
(In Thousands)

	Year Ended December 31	
	2019	2018
Operating activities		
Increase in net assets	\$ 6,019	\$ 18,214
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	25,517	24,726
Net change in unrealized gains and losses on investments	(8,524)	3,582
Equity in net earnings of joint ventures	(485)	(906)
Donated equipment	(2,145)	(3,998)
Gain on discontinued skilled nursing facility	(66)	-
Gain on sale of equipment	(68)	(677)
Changes in operating assets and liabilities:		
Patient accounts receivable, net	(2,203)	5,772
Supplies and other assets	(3,117)	2,229
Accounts payable, accrued expenses, and other liabilities	5,653	(3,783)
Estimated third-party payor settlements, net	167	14
Accrued pension liability	13,529	(6,175)
Net cash provided by operating activities	34,277	38,998
Investing activities		
Cash received from joint ventures	739	894
Net purchases of assets whose use is limited	(11,572)	(9,496)
Purchases of property, plant, equipment, and construction, net	(14,082)	(15,212)
Net cash used in investing activities	(24,915)	(23,814)
Financing activities		
Repayments of line of credit	-	(7,675)
Proceeds from issuance of long-term debt	3,163	7,952
Payments on long-term debt and finance lease obligations	(13,170)	(10,902)
Net cash used in by financing activities	(10,007)	(10,625)
Net (decrease) increase in cash and cash equivalents and restricted cash and restricted cash equivalents	(645)	4,559
Cash and cash equivalents and restricted cash and restricted cash equivalents, beginning of year	29,982	25,423
Cash and cash equivalents and restricted cash and restricted cash equivalents, end of year	\$ 29,337	\$ 29,982
Reconciliation of cash and cash equivalents and restricted cash and restricted cash equivalents at end of year to the balance sheets		
Cash and cash equivalents	\$ 22,383	\$ 22,854
Restricted cash and cash equivalents – designated by donors	100	162
Restricted cash and cash equivalents – under bond indenture	6,854	6,966
Total cash and cash equivalents and restricted cash and restricted cash equivalents	\$ 29,337	\$ 29,982
Supplemental disclosure of non-cash investing and financing activities and cash flow information		
Assets acquired under finance lease obligations	\$ 1,006	\$ 2,110
Cash paid for interest, net of amounts capitalized	\$ 9,206	\$ 9,744

See accompanying notes.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (Dollars in Thousands)

December 31, 2019

1. Organization and Summary of Significant Accounting Policies

Organization

Saint Peter's Healthcare System, Inc. (the System) is a nonprofit corporation. The Roman Catholic Diocese of Metuchen (the Diocese) is the sponsor of the System and, as provided in the System's bylaws, certain powers are reserved to the Bishop of the Diocese. The System's accompanying consolidated financial statements include the following entities: Saint Peter's University Hospital (the Hospital), an acute care 478 licensed bed teaching hospital located in New Brunswick, New Jersey; Saint Peter's Health & Management Services Corporation (Management Services); Saint Peter's Foundation (the Foundation); Margaret McLaughlin McCarrick Care Center (the Care Center); Saint Peter's Properties Corporation (Properties); Risk Assurance Company of Saint Peter's University Hospital (RAC); Saint Peter's Solar Energy Solutions, Inc. (Solar Energy Solutions); Saint Peter's Healthcare System Physician Associates, P.C. (Physician Associates PC); Saint Peter's Advanced Care, P.C. (Advanced Care); Saint Peter's Specialty Physicians, P.C. (Specialty Physicians); and Park Avenue Collections Corporation (Park Avenue) (Park Avenue had no operations during 2019 or 2018). Effective April 1, 2019, the sole membership of The National Gianna Center for Women's Health and Fertility, Inc. (National Gianna) was transferred from the System to an unrelated entity for no consideration. Additionally, amounts due from National Gianna to the System were forgiven as of December 31, 2018. Gianna Physician Practice of New York, P.C. (Gianna NY PC) ended operations as of May 31, 2019. Prior to those dates, National Gianna and Gianna NY PC were included in the System's consolidated financial statements.

In December 2019, the System and RWJ Barnabas Health (RWJBH) entered into a non-binding letter of intent to explore options for a potential affiliation. The System's Board of Governors is currently evaluating the potential affiliation, the outcome of which is uncertain.

All intercompany balances and transactions have been eliminated in consolidation. Although these entities have been consolidated for financial statement reporting purposes, there may be limitations on the use of an entity's funds by another member of the group resulting from the charitable nature of some of the entities or other factors.

Other unconsolidated entities, for which the System records its interest or investment, include CARES Surgicenter, LLC (CARES); New Brunswick Cardiac Cath Lab, LLC (Cardiac Cath); New Brunswick CK Leasing, LLC (Cyber Knife joint venture); New Brunswick Affiliated Hospitals (NBAH); and Holy Redeemer Healthcare System (Holy Redeemer).

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

The System accounts for its investments in CARES and Cardiac Cath on the equity method of accounting (see Note 5) because the System does not control the operations of the investees. The System accounts for its investments in Cyber Knife, Holy Redeemer and NBAH on the cost basis of accounting. The investment in NBAH is fully reserved.

Significant Accounting Policies

A summary of the significant accounting policies follows:

Use of Estimates: The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes, such as estimates for collections on accounts receivable for services to patients, estimated settlements with third-party payors, medical malpractice insurance liabilities and pension benefit liabilities, and disclosures of contingent assets and liabilities at the date of the financial statements. Estimates also affect the amounts of revenue and expenses reported during the period. There is at least a reasonable possibility that certain estimates will change by material amounts in the near term. Actual results could differ from those estimates and assumptions.

Cash and Cash Equivalents: The System considers all highly liquid investments with a maturity of three months or less at date of purchase, other than amounts held in assets whose use is limited investment portfolios, to be cash equivalents. The carrying amount of cash and cash equivalents reported on the consolidated balance sheets approximates fair value. The System does not hold any money market funds with significant liquidity restrictions that would be required to be excluded from cash equivalents.

Receivables for Patient Care: Patient accounts receivable for which the System receives payment under cost reimbursement, prospective payment formulae, or negotiated rates, which cover the majority of patient services, are stated at the estimated net amounts receivable from payors, which are generally less than the established billing rates of the System (see Note 3).

Assets Whose Use is Limited: Assets whose use is limited represent assets whose use is restricted for specific purposes through internal designation, by donors or under terms of bond indenture agreements or trust agreements, as well as investments held by RAC (see Note 4). Assets whose use is limited investments consist of marketable securities and alternative investments.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

Marketable securities are recorded at fair value as determined by reference to quoted market prices. Alternative investments consist of interests in funds of funds investments structured as limited partnerships and commingled funds. Alternative investment interests are reported based upon net asset values derived from the application of the equity method of accounting. Board designated assets are available for current use subject to approval by the System's Board.

Assets whose use is limited investments are classified as other than trading securities. Unrealized gains and losses on fixed income securities within assets whose use is limited, except for those unrealized losses which are deemed to be other than temporary impairments, are excluded from the excess of revenue over expenses on the accompanying consolidated statements of operations and changes in net assets. Other unrealized gains and losses, investment income and realized gains and losses on assets without donor restrictions are recorded as other operating revenue. Investment income derived from investments related to assets with donor restrictions is also recorded as other operating revenue unless the income or gain or loss is restricted by donor or law. Investment return is reported net of investment expenses.

Supplies: Supplies are carried at the lower of cost or net realizable value determined using the first-in, first-out method, or market method. Supplies are used in the provision of patient care and are not held for sale.

Deferred Financing Costs: Deferred financing costs were incurred to obtain financing for various construction and renovation projects. Amortization of these costs is provided on the effective interest method extending over the remaining term of the applicable indebtedness.

Property, Plant, Equipment, and Construction: Property, plant, equipment, and construction that were purchased by the System are carried at cost. Assets acquired under finance leases are recorded at the present value of the lease payments at the inception of the lease. Donated assets are recorded at fair market value at the date of donation. Annual provisions for depreciation and amortization of property, plant, and equipment are computed using the straight-line method over the lesser of the estimated useful lives of the assets or the term of the related lease for equipment held under finance lease obligations.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed of: The System reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Classification of Net Assets: The System separately accounts for and reports net assets without donor restrictions and net assets with donor restrictions. Net assets without donor restrictions are not externally restricted for identified purposes by donors or grantors. Resources arising from the results of operations or assets set aside by the System's Board are not considered to be donor restricted.

Net assets with donor restrictions are those whose use by the System has been limited by donors to a specific time frame or purpose, or have been restricted by donors as permanent endowments to be maintained in perpetuity. When donor restrictions expire, that is, when a time restriction ends or a purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported as net assets released from restriction.

The System follows the requirements of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as it relates to its permanent endowment contributions and net assets, as enacted by the State of New Jersey in 2009. The System annually expends the income distributed from the related assets according to donor stipulations.

The System recognizes governmental grants where commensurate value is not exchanged as contributions when conditions and restrictions are satisfied and reports such amounts within other revenue (see Note 15).

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

Excess of Revenue Over Expenses: The consolidated statements of operations and changes in net assets include excess of revenue over expenses as the performance indicator. Changes in net assets without donor restrictions which are excluded from the excess of revenue over expenses include the net change in unrealized gains and losses on other-than-trading investments (only applicable to fixed income securities in 2019), unless the unrealized losses are deemed to be other than temporary, donated equipment and other, the change in pension liability to be recognized in future periods, and gain or loss from discontinued operations. Transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported within income from operations.

Discontinued Operations: During November 2015, the Board of Governors, with no disapproval from the Vatican, approved the sale of the Care Center to an unrelated entity. The sale was approved by the New Jersey Attorney General in December 2015 and finalized on February 1, 2016. Proceeds from the sale were received in 2016, with minor wind down activity in 2019 and 2018. This transaction met the criteria to be reported as a discontinued operation initially in 2016. The System reported a gain (loss) from the operations of the discontinued skilled nursing facility of \$66 and (\$13) for the years ended December 31, 2019 and 2018, respectively.

Income Taxes: The System parent entity, the Hospital, the Care Center, Management Services, and the Foundation are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. Properties is a not-for-profit corporation as described in Section 501(c)(2) of the Code and is also exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. These entities are also exempt from state and local taxes. RAC is not subject to taxes on income or gains under the Cayman Islands tax concessions law except for a tax on dividends on domestic equities. Additionally, Physician Associates PC received its tax exemption determination in 2018.

Solar Energy Solutions, Advanced Care, Specialty Physicians, and Park Avenue are for-profit entities and, as such, are subject to federal, state, and local income taxes. The provision for income taxes associated with these entities is not material to the System's consolidated results of operations and is included in supplies and other expenses on the consolidated statements of operations and changes in net assets.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

As of and for the years ended December 31, 2019 and 2018, the System has made reasonable estimates of the provision for income taxes and deferred tax balances based on accounting guidance included in Accounting Standards Codification 740, *Income Taxes*. The System will continue to refine its calculations in future periods as additional regulations and guidance are issued by the Internal Revenue Service (IRS).

The Taxpayer Certainty and Disaster Tax Relief Act of 2019, signed into law on December 20, 2019 retroactively repealed Section 512(a)(7) of the Code which subjected amounts paid or incurred by an exempt organization to provide certain transportation fringe benefits to its employees to taxation as unrelated business taxable income. Prior year income tax payments, as well as current year payments for income taxes associated with Section 512(a)(7) for which refunds have been requested are recorded as receivables at December 31, 2019. These amounts are not significant to the accompanying consolidated financial statements.

Related-Party Transactions: The entities comprising the System provide various inter-entity services to their affiliated entities and the System parent company. The services consist of certain financial planning, information systems and telecommunications, general accounting, and other services. Charges for such services are based on the approximate cost to provide the services and are allocated between the entities based on an agreed-upon method which reflects the approximate level of usage by each entity. Such inter-entity charges and all intercompany balances between the entities comprising the System eliminate in consolidation.

Recent Accounting Pronouncements: In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. (ASU) 2016-01, *Financial Instruments – Overall*. ASU 2016-01 requires business-oriented health care not-for-profit entities to measure equity investments that do not result in consolidation and are not accounted for under the equity method at fair value and recognize any changes in fair value in the performance indicator unless the investments qualify for a new practicality exception. The practicality exception is available for equity investments without a readily determinable fair value, for which measurement would be based on cost less impairment and adjusted for observable price changes. The guidance is effective for annual periods beginning after December 15, 2018. Subsequent to the adoption of ASU 2016-01 effective January 1, 2019, the System no longer recognizes unrealized holding gains and losses on equity securities classified as other-than-trading outside of the performance indicator. This ASU does not impact the accounting for investments in debt securities.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

ASU 2016-01 also contains a provision that eliminates the requirement for the System to disclose the fair value of financial instruments measured at amortized cost. The adoption of ASU 2016-01 did not impact the System's net assets.

In February 2016, the FASB issued ASU 2016-02, *Leases*, which requires the rights and obligations arising from lease contracts, including existing and new arrangements, to be recognized as assets and liabilities on the balance sheets, including both finance leases (formally referred to as capital leases) and operating leases. ASU 2016-02 requires expanded disclosure related to lease agreements (See Note 9) and to help the financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. The recognition, measurement and presentation of expenses and cash flows arising from a lease primarily depend on its classification as a finance or operating lease.

The System adopted ASU 2016-02 effective January 1, 2019, following the modified retrospective method of application. As such, the 2018 consolidated financial statement amounts and disclosures have not been adjusted to reflect the provisions of the new standard. There was no cumulative-effect impact to the 2018 consolidated net assets as a result of the adoption. The System has made the transition-specific election to apply the package of practical expedients which allows for the carryforward of historical assessments of (1) whether contracts are or contain leases, (2) lease classification and (3) initial direct costs. Additionally, for operating leases entered into prior to January 1, 2019, the System has elected to utilize the operating leases' initial lease term to determine the discount rate used to initially measure the liability. Certain other accounting policy elections and quantitative and qualitative information pertaining to the System's adoption of ASU 2016-02 are described in Note 9.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The main objective of ASU 2016-13 and related ASU updates is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. The amendments affect loans, debt securities, trade receivables, net investments in leases, off balance sheet credit exposures, reinsurance receivables, and any other financial assets not excluded from the scope that have the contractual right to receive cash. The amendments in this update are effective for the System for fiscal years beginning after December 15, 2022. The System is in the process of evaluating the impact of ASU 2018-15 on its consolidated financial statements.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows – Restricted Cash*, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The System adopted ASU 2016-18 in 2019 using a retrospective transition method.

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958); Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. ASU 2018-08 clarifies existing guidance in order to address diversity in practice in classifying grants (including governmental grants) and contracts received by not-for-profit entities, and requires entities to evaluate whether the resource provider receives commensurate value. In addition, the standard clarifies the guidance on how entities determine when a contribution is conditional, including whether the agreement includes a barrier (or barriers) that must be overcome for the recipient to be entitled to the transferred assets and a right of return of the transferred assets (or a right of release of the promisor's obligation to transfer the assets). The standard was applied on a modified prospective basis to agreements that were not completed as of the effective date and to agreements entered into after the effective date. The System adopted ASU 2018-08 effective January 1, 2019. The adoption of ASU 2018-08 did not have a material impact on the System's consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15, *Intangibles – Goodwill and Other -Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract*. The standard aligns the requirement for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by this standard. The standard requires the customer in a hosting arrangement that is a service contract to follow the guidance in Accounting Standards Codifications Subtopic 350-40 to determine which implementation costs to capitalize as an asset related to the service contract and which costs to expense by determining which project stage an implementation activity relates to and the nature of the costs. The standard also

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

1. Organization and Summary of Significant Accounting Policies (continued)

requires the customer to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement, among other provisions. The amendments in ASU 2018-15 are effective for annual reporting periods beginning after December 15, 2020, and interim periods thereafter. Early adoption is permitted. The amendments should be applied either retrospectively or prospectively to all implementation costs incurred after the date of adoption. The System is in the process of evaluating the impact of ASU 2018-15 on its consolidated financial statements.

The FASB has amended certain guidance related to various disclosures in ASU 2018-13, *Technical Corrections and Improvements to Financial Instruments-Overall (Subtopic 825-10)-Recognition and Measurement of Financial Assets and Financial Liabilities*, and ASU 2018-14, *Compensation-Retirement Benefits-Defined Benefit Plans-General (Subtopic 715-20)-Disclosure Framework-Changes to the Disclosure Requirements for Defined Benefit Plans*. ASU 2018-13 includes several disclosure changes involving transfers between the fair value levels and other updates related to fair value Level 3 investments. ASU 2018-13 also requires entities that use the practical expedient to measure the fair value of certain investments at their net asset values to disclose (1) the timing of liquidation of an investee's assets and (2) the date when redemption restrictions will lapse, but only if the investee has communicated this information to the entity or announced it publicly. The guidance in ASU 2018-14 requires all sponsors of defined benefit plans to provide certain new disclosures: the weighted-average interest crediting rate for cash balance plans and other plans with promised interest crediting rates and an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period. Among other changes, ASU 2018-14 eliminates the required disclosure for all sponsors of defined benefit plans to disclose the amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year. The updates noted above have effective dates as follows with early adoption permitted: ASU 2018-13: fiscal years beginning after December 15, 2019 and ASU 2018-14: fiscal years ending after December 15, 2021. The System has not completed the process of evaluating the impact of these ASUs on its consolidated financial statements.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

2. Charity Care and Community Benefits

In accordance with its mission and philosophy, the System commits substantial resources to sponsor a broad range of services to both the indigent as well as the broader community.

The System provides care to patients who meet certain criteria defined by the New Jersey Department of Health (DOH) without charge or at amounts less than established rates. Because the System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The System's records identify and monitor the level of charity care it provides and include the amount of charges forgone for services and supplies furnished. DOH allows retroactive application for charity care up to two years from the date of service.

For patients who were determined by the System to have the ability to pay but did not, the expected uncollected amounts are classified as an implicit price concession which reduces net patient service revenue (\$15,819 and \$17,494 in 2019 and 2018, respectively). Distinguishing between charity care and implicit price concessions is difficult, in part because services are often rendered prior to the System's full evaluation of the patient's ability to pay.

Community benefits provided to the indigent include the cost of providing services to persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. This type of community benefit includes the costs of: traditional charity care; unpaid costs of care provided to beneficiaries of Medicaid and other indigent public programs; services such as free clinics and meal programs for which a patient is not billed or for which a nominal fee has been assessed; and cash and in-kind donations of equipment, supplies, or staff time volunteered on behalf of the community.

Community benefits provided to the broader community include the costs of providing services to other populations who may not qualify as indigent but may need special services and support. This type of community benefit includes the costs of: services such as health promotion and education, health clinics, and screenings, all of which are not billed or can be operated only on a deficit basis; unpaid portions of training health professionals such as medical residents, nursing students, and students in allied health professions; and the unpaid portions of testing medical equipment and controlled studies of therapeutic protocols.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

2. Charity Care and Community Benefits (continued)

A summary of the estimated cost of community benefits provided to both the indigent and the broader community follows:

	Year Ended December 31	
	2019	2018
Community benefits provided to the indigent:		
Charity care provided	\$ 23,426	\$ 20,896
Unpaid cost of public programs, Medicaid, and other indigent care programs	8,359	9,773
Community benefits provided to the broader community:		
Non-billed services for the community	5,484	3,864
Education and research provided for the community	5,297	4,754
Estimated cost of community benefits	\$ 42,566	\$ 39,287

The costs of charity care and other community benefit activities are derived from both estimated and actual data. The estimated cost of charity care includes the direct and indirect cost of providing such services and is estimated utilizing the Hospital's ratio of cost to standard charges, which is then multiplied by the uncompensated charges associated with providing care to charity patients.

The estimated cost of community benefits was 9.1% and 8.6% of total Hospital operating expenses in 2019 and 2018, respectively, before consideration of charity care subsidies.

The System receives payments from the New Jersey Health Care Subsidy Funds for charity care, and such amounts totaled approximately \$4,333 and \$3,423 for the years ended December 31, 2019 and 2018, respectively.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

3. Net Patient Service Revenue

Accounts Receivable and Net Patient Service Revenue

Net patient service revenue is reported at the amount that reflects the consideration to which the System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others and includes provisions for variable consideration (reductions to revenue) for retroactive revenue adjustments, including adjustments due to the settlement of ongoing and future audits, reviews, and investigations.

The System uses a portfolio approach to account for categories of patient contracts as a collective group rather than recognizing revenue on an individual contract basis. The portfolios consist of major payor classes for inpatient revenue and major payor classes and types of services provided for outpatient revenue. Based on historical collection trends and other analyses, the System believes that revenue recognized by utilizing the portfolio approach approximates the revenue that would have been recognized if an individual contract approach were used.

The System's initial estimate of the transaction price for services provided to patients is determined by reducing the total standard charges related to the patient services provided by various elements of variable consideration, including contractual adjustments, discounts, implicit price concessions, and other reductions to the System's standard charges. The System determines the transaction price associated with services provided to patients who have third-party payor coverage on the basis of contractual or formula-driven rates for the services rendered (see description of third-party payor payment programs below). The estimates for contractual allowances and discounts are based on contractual agreements, the System's discount policies and historical experience. For uninsured and under-insured patients who do not qualify for charity care, the System determines the transaction price associated with services on the basis of charges reduced by implicit price concessions. Implicit price concessions included in the estimate of the transaction price are based on the System's historical collection experience for applicable patient portfolios. Under the System's policy for self-pay patients, a patient who has no insurance and is ineligible for any government assistance program has his or her bill reduced to the amount which would be billed to a commercially insured patient.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

3. Net Patient Service Revenue (continued)

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

Substantially all of its performance obligations relate to contracts with a duration of less than one year. The unsatisfied or partially unsatisfied performance obligations primarily relate to inpatient acute care services at the end of the reporting period for patients who remain admitted at that time (in-house patients). The performance obligations for in-house patients are generally completed when the patients are discharged, which for the majority of the System's in-house patients occurs within days or weeks after the end of the reporting period.

Subsequent changes to the estimate of the transaction price (determined on a portfolio basis when applicable) are generally recorded as adjustments to patient service revenue in the period of the change. For the years ended December 31, 2019 and 2018, changes in the System's estimates of implicit price concessions, discounts, contractual adjustments or other reductions to expected payments for performance obligations satisfied in prior periods were not significant. Portfolio collection estimates are updated quarterly based on collection trends. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay (determined on a portfolio basis when applicable) are recorded as bad debt expense. Bad debt expense for the years ended December 31, 2019 and 2018 was not significant.

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

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

3. Net Patient Service Revenue (continued)

Net patient service revenue by major payor source for the years ended December 31, 2019 and 2018, based on primary insurance designation, is as follows:

	2019	2018
Medicare	\$ 106,759	\$ 105,454
Medicaid	81,906	75,637
Commercial carriers and managed care organizations	275,074	274,275
Self-pay	3,063	2,968
	\$ 466,802	\$ 458,334

Deductibles, copayments and coinsurance under third-party payment programs which are the patient's responsibility are not included within the self-pay category above.

Net patient service revenue for the years ended December 31, 2019 and 2018 by line of business is as follows:

	2019	2018
Hospital	\$ 428,126	\$ 418,628
Physician services	38,676	39,706
	\$ 466,802	\$ 458,334

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

3. Net Patient Service Revenue (continued)

At December 31, 2019 and 2018 accounts receivable is comprised of the following components:

	<u>2019</u>	<u>2018</u>
Patient receivables	\$ 46,007	\$ 43,375
Contract assets	5,183	5,612
	<u>\$ 51,190</u>	<u>\$ 48,987</u>

Contract assets are related to in-house patients who were provided services during the reporting period but were not discharged as of the reporting date and for which the System may not have the right to bill.

Third-Party Payment Programs

The System has agreements with third-party payors that provide for payment for services rendered at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare: Hospitals are paid for most Medicare inpatient and outpatient services under the national prospective payment system and other methodologies of the Medicare program for certain other services. Federal regulations provide for certain adjustments to current and prior years' payment rates, based on industry-wide and hospital-specific data. Medicare cost reports of the System have been audited and settled for years through 2015 at December 31, 2019.

Medicaid: Inpatient acute care services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge. Outpatient services rendered to Medicaid program beneficiaries are reimbursed under cost-based and fee schedule methodologies. The System is reimbursed for outpatient services at a tentative rate with final settlement determined after submission of annual cost reports and audits thereof by the Medicaid fiscal intermediary. Medicaid cost reports of the System for years through 2016 have been audited and settled.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

3. Net Patient Service Revenue (continued)

Other Third-Party Payors: The System also has entered into payment agreements with certain commercial insurance carriers and managed care organizations. The basis for payment to the System under these agreements includes prospectively determined rates per discharge or days of hospitalization and discounts from established charges.

Medicare and Medicaid cost reports, which serve as the basis for final settlement with these programs, have been audited by the applicable fiscal intermediary and settled through years noted above, although revisions to final settlements or other retroactive changes could be made. Other years and various issues remain open for audit and settlements. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount when open years are settled, audits are completed and additional information is obtained.

Settlements with third-party payors for cost report filings and retroactive adjustments due to ongoing and future audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor and the System's historical settlement activity (for example, cost report final settlements or repayments related to recovery audits), including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Such estimates are determined through either a probability-weighted estimate or an estimate of the most likely amount, depending on the circumstances related to a given estimated settlement item. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available), or as years are settled or are no longer subject to such audits, reviews, and investigations. For the years ended December 31, 2019 and 2018, there was no impact of the System's revisions to prior year settlement estimates impacting net patient service revenue.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) *(Dollars in Thousands)*

3. Net Patient Service Revenue (continued)

There are various proposals at the federal and state levels that could, among other things, significantly reduce payment rates or modify payment methods. The ultimate outcome of these proposals and other market changes, including the potential effects of or revisions to health care reform that has been or will be enacted by the federal and state governments, cannot be determined presently. Future changes in the Medicare and Medicaid programs and any reduction of funding could have an adverse impact on the System. Additionally, certain payors' payment rates for various years have been appealed by the System for cost report year 2006 through 2019. If the appeals are successful, additional income applicable to those years could be realized.

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge the System's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon the System. Other than the matter described below, the System is not aware of any allegations of non-compliance that could have a material adverse effect on the accompanying consolidated financial statements and believes that it is in compliance in all material respects with applicable laws and regulations. In addition, certain contracts the System has with commercial payors also provide for retroactive audit and review of claims.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

3. Net Patient Service Revenue (continued)

In December 2018, the System, jointly with the New Brunswick Cardiac Cath Lab, LLC (Cardiac Cath), submitted a preliminary letter to the Office of Counsel to the Inspector General, United States Department of Health and Human Services (the OIG) through the OIG's Self-Disclosure Protocol (the Protocol), notifying the OIG of certain physician compensation matters that potentially violate the Federal Civil Monetary Penalties Law (CMPL), the Anti-kickback statute, and/or the Stark Law and requesting acceptance into the Protocol. In January 2019, the System and Cardiac Cath received notification that they had been accepted into the Protocol. On March 28, 2019, the System and Cardiac Cath filed a detailed review of their investigation in accordance with the Protocol. The OIG Protocol was established to encourage providers to voluntarily identify, disclose and resolve certain matters involving Federal health care programs under the OIG's civil monetary penalties authorities. The OIG's Protocol indicates that a provider's good faith participation in the Protocol can potentially mitigate the provider's exposure under the OIG's civil monetary penalties authorities.

At December 31, 2019, and as of the issuance of the accompanying consolidated financial statements, the amount of potential obligations to (or other actions that may be taken by) the OIG and/or others in connection with the referenced self-disclosure is unknown. Corrective actions relating to the matters discussed in the March 2019 letter have been taken and a preliminary allowance estimate has been established.

State and Other Funding

The New Jersey Health Care Subsidy Funds were established for various purposes, including the distribution of charity care payments to hospitals statewide. Effective January 1, 2014, the State of New Jersey replaced the Hospital Relief Subsidy Fund with the Delivery System Reform Incentive Payment Pool (the Pool). The Pool is available to certain hospitals that are able to establish performance improvement activities in one of eight specified clinical improvement areas. Amounts received from the Pool are subject to the satisfaction of certain performance criteria, with adjustments to the Pool allocations processed prospectively. The following state and other funding amounts have been included in the System's net patient service revenue:

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

3. Net Patient Service Revenue (continued)

	Year Ended December 31	
	2019	2018
State:		
Delivery System Reform Incentive Payments	\$ 4,644	\$ 3,192
Charity Care (<i>Note 2</i>)	4,333	3,423
Graduate Medical Education	6,475	5,873
Federal:		
Graduate Medical Education	4,262	4,121
	\$ 19,714	\$ 16,609

The System expects to receive approximately \$2,170 in Charity Care subsidies for distributions scheduled through June 30, 2020. Charity Care subsidies subsequent to June 30, 2020 are presently unknown.

In addition to direct Graduate Medical Education funding received from the federal and state Medicare and Medicaid programs, the System also receives a portion of its Medicare rate for indirect medical education costs.

4. Liquidity and Assets Whose Use is Limited

Liquidity and Availability

The System has a working capital surplus of \$133,874 and \$113,514 as of December 31, 2019 and 2018, respectively. The System's average days of cash on hand as of December 31, 2019 and 2018 was 109.1 and 98.3, respectively (based on normal expenditures).

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

4. Liquidity and Assets Whose Use is Limited (continued)

Financial assets available for general expenditure within one year of December 31, 2019 and 2018 consist of the following:

	2019	2018
Cash and cash equivalents	\$ 22,383	\$ 22,854
Patient accounts receivable, net	51,190	48,987
Physician services receivable, net	2,867	1,621
Assets whose use is limited which are available for general expenditures:		
Board designated	111,514	93,014
Donor restricted – health care programs	2,480	1,458
	\$ 190,434	\$ 167,934

The System has certain board designated and donor-restricted assets which are available for general expenditure within one year in the normal course of operations. Accordingly, these assets have been included in the table above. The System has other assets for donor-restricted purposes, held under bond indenture and for the professional and general liability captive insurance program which are not readily available for general expenditures.

As part of the System's liquidity management plan, cash in excess of daily requirements are invested in short term money market funds. The money market funds at December 31, 2019 and 2018 totaled \$13,300 and \$15,000, respectively.

Additionally, the System maintains a \$10,000 line of credit, as described in Note 7. As of December 31, 2019 and 2018, there was no balance outstanding on the line of credit.

As of December 31, 2019 and 2018, the System was in compliance with all financial debt covenants.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

4. Liquidity and Assets Whose Use is Limited (continued)

Assets Whose Use Is Limited

Assets whose use is limited, primarily at fair value, are maintained for the following purposes:

	December 31	
	2019	2018
Assets held as designated by Board of Trustees of the Hospital	\$ 111,514	\$ 93,014
Assets held as designated by donors	4,566	5,394
Assets held under bond indenture	22,202	22,192
Assets held by RAC (Note 10)	24,517	22,277
Total assets whose use is limited	162,799	142,877
Less current portion	122,824	105,180
Non-current portion	\$ 39,975	\$ 37,697

Refer to Note 12 for the composition by asset type for investments reported at fair value. The System's holdings of alternative investments and commingled funds within assets whose use is limited totaled approximately \$8,418 and \$5,953 at December 31, 2019 and 2018, respectively. These investments are measured based on the equity method of accounting as described in Note 1.

Assets held by a trustee under bond indenture agreements are maintained for the following purposes:

	December 31	
	2019	2018
Debt service interest fund	\$ 3,944	\$ 4,106
Debt service principal fund	2,799	2,665
Debt service reserve fund	15,459	15,421
	\$ 22,202	\$ 22,192

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

4. Liquidity and Assets Whose Use is Limited (continued)

Investment income, included in other operating revenue, consists of the following:

	Year Ended December 31	
	2019	2018
Interest and dividend income	\$ 3,236	\$ 2,877
Realized gains and losses	1,550	(217)
Total investment income reported in other operating revenue (Note 15)	\$ 4,786	\$ 2,660

For fixed income securities in 2019 and fixed income and equity securities in 2018 (prior to the effective date of ASU 2016-01), the System's gross unrealized losses and fair value of individual securities, aggregated by investment category, which have been in a continuous unrealized loss position less than 12 months and greater than 12 months at December 31, 2019 and 2018 are as follows:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2019						
U.S. government obligations (1 securities)	\$ 996	\$ -	\$ -	\$ -	\$ 996	\$ -
Corporate bonds/fixed income (14 securities)	1,028	(8)	1,372	(9)	2,400	(17)
Mortgage and asset-backed securities (39 securities)	8,248	(70)	3,316	(69)	11,564	(139)
Total	\$ 10,272	\$ (78)	\$ 4,688	\$ (78)	\$ 14,960	\$ (156)
December 31, 2018						
U.S. government obligations (12 securities)	\$ 321	\$ (2)	\$ 2,824	\$ (20)	\$ 3,145	\$ (22)
Corporate bonds/fixed income (64 securities)	7,549	(109)	9,621	(136)	17,170	(245)
Mortgage and asset-backed securities (102 securities)	10,046	(170)	29,215	(427)	39,261	(597)
Mutual funds – equities (17 securities)	13,637	(538)	-	-	13,637	(538)
Total	\$ 31,553	\$ (819)	\$ 41,660	\$ (583)	\$ 73,213	\$ (1,402)

At December 31, 2019 and 2018, management determined that the unrealized losses above were temporary based on the extent and length of time the securities' fair value was below cost.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

5. Other Assets

Included within investment in joint ventures and other assets on the accompanying consolidated balance sheets are the System's joint venture investments, including CARES and Cardiac Cath which are equity method investments (aggregate balance of approximately \$1,800 at December 31, 2019 and \$1,700 at December 31, 2018). CARES leases and operates an ambulatory surgery center located in a building owned by the Hospital. Cardiac Cath leases a portion of the CARES building to operate a low-risk outpatient cardiac catheterization laboratory. In 2019 and 2018, the System collected distributions from these joint ventures of approximately \$376 and \$578, respectively, and recorded gains of \$485 and \$590, respectively.

The following is a condensed summary of financial information of CARES and Cardiac Cath:

	CARES		Cardiac Cath	
	December 31		December 31	
	2019	2018	2019	2018
Total assets	\$ 3,636	\$ 3,185	\$ 1,774	\$ 2,570
Total liabilities	504	501	634	965
Total equity	3,132	2,684	1,140	1,605

In 2019 and 2018, the System collected distributions from the Cyber Knife joint venture of approximately \$363 and \$316, respectively.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

6. Property, Plant, Equipment, and Construction

Property, plant, equipment, and construction consist of the following:

	December 31	
	2019	2018
Land	\$ 8,152	\$ 8,152
Buildings, building service equipment, and improvements	341,544	332,343
Fixed equipment	9,071	9,071
Major movable equipment	247,107	241,339
	605,874	590,905
Less accumulated depreciation and amortization	418,199	396,890
	187,675	194,015
Construction-in-progress	955	3,626
	\$ 188,630	\$ 197,641

Depreciation expense was \$25,306 and \$24,509 in 2019 and 2018, respectively. Useful lives of depreciable assets range from 3 to 40 years.

During 2019 and 2018, the System wrote off approximately \$3,900 and \$9,800 of fully depreciated assets, respectively.

During 2019 and 2018, the System received grants related to certain energy upgrade projects. Grant revenue of \$510 and \$3,017 related to an energy resilient project in 2019 and 2018 respectively, was recognized in the accompanying statements of operations and changes in net assets.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

7. Long-Term Debt and Line of Credit

Long-term debt and line of credit consist of the following:

	December 31	
	2019	2018
New Jersey Health Care Facilities Financing Authority (NJHCFFA) Series 2011 Revenue and Refunding Bonds, which bear interest at rates between 5.00% and 6.25% due in varying maturities through July 1, 2035 (a)	\$ 74,525	\$ 78,785
NJHCFFA Series 2007 Revenue Bonds, which bear interest at rates between 5% and 6.25% due in varying maturities through July 1, 2037 (a)	59,245	60,265
Other loans (b)	12,080	15,253
Mortgages payable with interest between 4.75% and 5.25% payable in monthly installments of principal and interest through December 1, 2031	1,763	3,406
Finance lease obligations, with interest rates ranging from 1.53% to 4.50% and payments through 2023	2,947	2,858
	150,560	160,567
Less unamortized original issue discount	528	568
Less unamortized deferred financing costs	1,451	1,621
Less current portion	8,635	11,413
	\$ 139,946	\$ 146,965

(a) In August 2011, the Hospital and the Care Center, collectively the Saint Peter's University Hospital Obligated Group (the Obligated Group), closed on the Series 2011 Revenue and Refunding Bonds (the Series 2011 Bonds) in the amount of \$100,640 issued by the NJHCFFA on behalf of the Obligated Group. The proceeds of the Series 2011 Bonds were used for (i) the current refunding of all of the outstanding Series F Revenue Bonds, Series 2000A Revenue Bonds, and Series 2000B Bonds; (ii) the payment or reimbursement of the costs of certain capital expenditures relating to the renovation of portions of the Hospital's facilities and the acquisition and installation of various equipment to be used by the Hospital at its facilities (approximately \$5,500); (iii) the funding of the Debt Service Reserve Fund relating to the Series 2011 Bonds; and (iv) the payment of the costs of issuance of the Series 2011 Bonds.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

7. Long-Term Debt and Line of Credit (continued)

In December 2007, the Obligated Group closed on the Series 2007 Revenue Bonds (the Series 2007 Bonds) with the NJHCFFA in the amount of \$65,175, the proceeds of which were used to (i) refund a portion of the outstanding principal amount of the St. Peter's Medical Center Issue, Series F; (ii) pay or reimburse the costs of the construction and renovation of certain portions of the Hospital's facilities and the acquisition of various capital equipment; (iii) pay capitalized interest on a portion of the Series 2007 Bonds; (iv) fund the Debt Service Reserve Fund related to the Series 2007 Bonds; and (v) pay or reimburse the costs of issuance of the Series 2007 Bonds.

The Series 2011 and Series 2007 Bonds were issued in the name of the Obligated Group. Each of the Series 2011 and Series 2007 Bonds is collateralized by a pledge of the revenue of the Obligated Group and the assets held under bond indenture pursuant to the Master Trust Indenture (the Indenture). Under the terms of the Indenture, the Obligated Group is required to maintain a Debt Service Reserve Fund in an amount equal to one year's principal and interest for the Series 2011 and Series 2007. At December 31, 2019 and 2018, the Obligated Group was in compliance with this requirement.

Under the terms of the Indenture and other agreements with the NJHCFFA, the Obligated Group is required to maintain certain financial ratios and be in compliance with other restrictive covenants as described in the respective agreements. At December 31, 2019 and 2018, the Obligated Group was in compliance with such financial covenants.

Subsequent to February 1, 2016, the Obligated Group consists of the Hospital only and the mortgage and the Care Center were released from the Obligated Group. Residual assets held by the Care Center which existed at that date were transferred to the Hospital in 2017 upon final disposition and, accordingly, are included in the Obligated Group.

- (b) At December 31, 2019 and 2018, the System has a loan to a utility company totaling \$3,272 and \$3,693, respectively, related to amounts borrowed for the installation of solar panels by Solar Energy Solutions. The loan is being repaid by tax credits that are purchased by the utility company. The tax credits are created when solar energy is produced.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

7. Long-Term Debt and Line of Credit (continued)

The System participated in an energy resilient project through the New Jersey Economic Development Authority (EDA) using grant funding received from the U.S. Department of Housing and Urban Development, combined with a loan from the EDA of \$2,531 paid over 20 years at a 2% interest rate. The loan was initially approved by the EDA in 2017; the loan repayment amount has been revised based on application of grant funding. The project is also funded by a \$1,057 loan payable over 10 years to a utility company at zero interest. The System had drawn down approximately \$108 and \$949 of the loan as of December 31, 2019 and 2018, respectively.

During 2015, the System entered into an agreement for an equipment loan from a financial institution for approximately \$4,900 maturing in December 2020 with an interest rate of approximately 4.01%. There was no outstanding balance on this loan at December 31, 2019 (approximately \$1,780 at December 31, 2018).

The System has other loans with financial institutions maturing in 2024 with interest rates ranging from approximately 3.50% to 4.50% to finance the construction of interventional radiology and catheterization suites and the replacement of the System's power plant totaling \$5,273 and \$6,300 at December 31, 2019 and 2018, respectively.

The System maintains a \$10,000 line of credit with a bank. At December 31, 2019 and 2018, no balance was outstanding on the line. The line is due on demand and expires in September 2023. Interest on the line is a variable rate based on LIBOR plus 2%.

During 2019, the System early retired debt of approximately \$3,200 and by doing so saved interest of approximately \$171.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

7. Long-Term Debt and Line of Credit (continued)

Scheduled principal payments on long-term debt and finance lease obligations, net of interest, for the next five years and thereafter are as follows:

	Series 2011 and 2007 Bonds	Other Loans	Finance Lease Obligations	Total
2020	\$ 5,550	\$ 2,124	\$ 961	\$ 8,635
2021	5,830	2,018	941	8,789
2022	6,245	1,708	610	8,563
2023	6,570	1,597	246	8,413
2024	6,925	1,553	174	8,652
Thereafter	102,650	4,843	15	107,508
	<u>\$ 133,770</u>	<u>\$ 13,843</u>	<u>\$ 2,947</u>	<u>\$ 150,560</u>

8. Retirement Plans

The System sponsors a non-contributory defined benefit retirement plan (the Plan) covering all eligible employees of affiliated organizations of the System. Plan benefits are based on years of service and employee compensation as defined in the plan document of affiliated organizations of the System.

The Plan was amended such that effective July 1, 2010, any employee hired after June 30, 2010, is not eligible to participate in the Plan. Additionally, active participation in the Plan is frozen for any employee who terminated employment before July 1, 2010, and is rehired after such date, and active participation in the Plan is frozen for any employee who terminated employment on or after July 1, 2010, unless he/she is rehired before the first anniversary of their termination. The System maintains a defined contribution plan for employees hired as of and subsequent to July 1, 2010. All existing eligible employees as of June 30, 2010 will remain as participants in the defined benefit plan and participate in the defined contribution plan. In February 2012, the System announced to participants of the Plan a plan freeze effective December 31, 2012.

The defined contribution plan established in 2010 provides for annual contributions for eligible employees of between 1% and 3% of pay based on the employee's years of service. Eligible employees begin to accrue benefits six months from their date of hire. The System funds the defined contribution expense on a current basis. Such expense was approximately \$2,217 and

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

8. Retirement Plans (continued)

\$8,476 in 2019 and 2018, respectively. Additionally, a defined contribution plan was established in 2014 for Physician Associates PC eligible employees with contribution expense of approximately \$93 and \$247 in 2019 and 2018, respectively.

In 2019, the System froze the existing defined contribution plans and instituted a new 401(k) retirement plan effective April 2019. The System contributes 2% of the employee's pay for all plan participants with an employee match contribution up to 3%. The System funds the 401(k) plan on a current basis. Such expense totaled \$7,045 in 2019.

The System recognizes on its consolidated balance sheets an asset for a defined benefit postretirement plan's overfunded status or a liability for a plan's underfunded status, measures the defined benefit postretirement plan's assets and obligations that determine its funded status as of the end of the System's fiscal year, and recognizes changes in the funded status of a defined benefit postretirement plan in changes in net assets without donor restrictions in the year in which the changes occur. Amounts that are recognized as a component of changes in net assets without donor restrictions will be subsequently recognized as net periodic pension cost in future periods.

The underfunded status of the Plan as recognized on the System's consolidated balance sheets is as follows:

	December 31	
	2019	2018
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 314,107	\$ 339,101
Interest cost	13,621	12,648
Benefits paid	(10,881)	(9,280)
Actuarial loss (gain)	37,511	(28,362)
Benefit obligation at end of year	354,358	314,107
Change in plan assets:		
Fair value of plan assets at beginning of year	184,833	203,652
Actual return on plan assets	33,067	(13,266)
Employer contributions	5,000	4,000
Benefits paid	(10,881)	(9,280)
Administrative expenses and other	(464)	(273)
Fair value of plan assets at end of year	211,555	184,833
Accrued pension liability	\$ (142,803)	\$ (129,274)

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

8. Retirement Plans (continued)

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets are as follows:

	December 31	
	2019	2018
Projected benefit obligation	\$ 354,358	\$ 314,107
Accumulated benefit obligation	354,358	314,107
Fair value of plan assets	211,555	184,833

The actuarial loss (gain) of \$37,511 and (\$28,362) in 2019 and 2018, respectively, primarily relates to a decrease in 2019 and an increase in 2018 in the discount rate assumption.

The unrecognized actuarial loss included in other changes in net assets without donor restrictions at December 31, 2019 and 2018 is \$138,277 and \$124,014, respectively, of which \$3,550 is expected to be recognized in net periodic pension cost during the year ending December 31, 2020. The change in the pension liability to be recognized in future periods as reported on the accompanying consolidated statements of operations and changes in net assets totaled (\$14,263) in 2019 and represents the change in these amounts from December 31, 2019 to 2018.

The following table provides the components of net periodic pension cost:

	Year Ended December 31	
	2019	2018
Interest cost	\$ 13,621	\$ 12,648
Expected return on plan assets	(13,177)	(14,537)
Recognized actuarial loss and administrative expenses	3,822	3,800
Net periodic pension cost	<u>\$ 4,266</u>	<u>\$ 1,911</u>

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

8. Retirement Plans (continued)

The following assumptions were used in determining the benefit obligations and net periodic pension costs:

	December 31	
	2019	2018
Weighted average assumptions used to determine benefit obligations at December 31:		
Discount rate	3.50%	4.41%
Weighted average assumptions used to determine net periodic benefit cost for the year ended December 31:		
Discount rate	4.41%	3.78%
Expected long-term rate of return on plan assets	7.25%	7.25%

To develop the expected long-term rate of return on assets assumption, the System considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio. This resulted in the selection of the 7.25% expected long-term rate of return on assets assumption at December 31, 2019 and 2018.

The Plan's investment policy is designed to achieve return on assets to match or exceed the actuarial required rate of return. The asset allocation guidelines and permissible ranges by asset category are listed below.

	Target	Permissible Range
Equities	48%	33% – 55%
Fixed income	21%	18% – 23%
Global asset allocation	6%	4% – 10%
Equity alternatives	10%	6% – 14%
Fixed-income alternatives	15%	10% – 20%

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

8. Retirement Plans (continued)

The Plan's asset allocations by asset category are as follows:

	December 31	
	2019	2018
Equities	49%	43%
Fixed income	21	20
Global asset allocation	6	10
Equity alternatives	10	10
Fixed-income alternatives	14	17
	100%	100%

Assets invested in the Plan are carried at fair value. Marketable debt and equity securities with readily determinable values are carried at fair value as determined based on independent published sources. Alternative investments (non-traditional, not readily marketable holdings) include hedge funds. Alternative investment interests generally are structured such that the Plan holds a limited partnership interest or an interest in an investment management company. The Plan's ownership structure does not provide for control over the related investees and the Plan's financial risk is limited to the carrying amount reported for each investee. Fair value for alternative investments is determined by the Plan for each investment using net asset value as a practical expedient, as permitted by generally accepted accounting principles, rather than using another valuation method to independently estimate fair value.

Refer to Note 12 for the composition at fair value of the defined benefit pension plan assets at December 31, 2019 and 2018.

The System received a favorable ruling from the IRS dated August 14, 2013, to operate the Plan as a church plan, which exempts the System from the requirements of the Employee Retirement Income Security Act of 1974 (ERISA) and its funding requirements. In 2013, the System was sued by certain plan participants claiming the Plan did not qualify as a church plan. Management defended the lawsuit and in June 2017, the U.S. Supreme Court, in a unanimous decision, determined that the Plan could be a church plan. Other issues related to this matter are still in litigation.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

8. Retirement Plans (continued)

The accrued pension liability reported in the accompanying consolidated financial statements of \$142,803 and \$129,274 at December 31, 2019 and 2018, respectively, is actuarially determined in accordance with the accounting requirements for reporting in the financial statements of the plan sponsor, which differs from the determination of the accumulated plan benefits as reported in the Plan's financial statements.

During 2019 and 2018, the System contributed \$5,000 and \$4,000 to the Plan, respectively. The System plans to contribute \$6,000 to the Plan in 2020.

The following benefit payments under the Plan are expected to be paid:

2020	\$	12,394
2021		13,360
2022		14,305
2023		15,183
2024		16,099
2025–2029		90,969

9. Leases and Other Commitments and Contingencies

Leases

As described in Note 1, the System adopted ASU 2016-02 effective January 1, 2019. The System leases certain property and equipment under finance and operating leases. Leases are classified as either finance or operating leases based on the underlying terms of the agreement and certain criteria, such as the term of the lease relative to the useful life of the asset and the total lease payments to be made as compared to the fair value of the asset, amongst other criteria. Finance leases result in an accounting treatment similar to an acquisition of the asset.

For leases with initial terms greater than a year (or initially greater than one year remaining under the lease at the date of adoption of ASU 2016-02), the System records the related right-of-use assets and liabilities at the present value of the lease payments to be paid over the life of the related lease. The System's leases may include variable lease payments and renewal options. Variable lease payments are excluded from the amounts used to determine the right-of-use assets and liabilities unless the variable lease payments depend on an index or rate or are in substance fixed payments.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

9. Leases and Other Commitments and Contingencies (continued)

Lease payments related to periods subject to renewal options are also excluded from the amounts used to determine the right-of-use assets and liabilities unless the System is reasonably certain to exercise the option to extend the lease. The present value of lease payments is calculated by utilizing the discount rate stated in the lease, when readily determinable. For leases for which this rate is not readily available, the System has elected to use a risk-free discount rate determined using a period comparable with that of the lease term. The System has made an accounting policy election to separate lease components from non-lease components in contracts when determining its lease payments for its asset classes except for medical equipment, as permitted by ASU 2016-02. As such, the System does not account for the applicable non-lease components together with the related lease components when determining the right-of-use assets and liabilities.

The System has made an accounting policy election not to record leases with an initial term of less than a year as right-of-use assets and liabilities.

Operating leases with a present value of approximately \$15,380 were recorded as right-of-use liabilities and assets as of January 1, 2019 upon the adoption of ASU 2016-02.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

9. Leases and Other Commitments and Contingencies (continued)

The following schedule summarizes information related to the lease assets and liabilities as of and for the year ended December 31, 2019:

Lease cost:	
Finance lease cost:	
Amortization of right-of-use asset	\$ 850
Interest on lease liabilities	94
Operating lease cost	4,311
Short-term lease cost	2,167
Sublease income	20
Total lease cost	<u>\$ 7,442</u>
Right-of-use assets and liabilities:	
Right-of-use assets – finance leases	\$ 2,908
Lease liability – finance leases	2,947
Right-of-use assets – operating leases	13,034
Lease liability – operating leases	13,034
Other information:	
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from finance leases	\$ 94
Operating cash flows from operating leases	3,979
Financing cash flows from finance leases	917
Right-of-use assets obtained in exchange for new finance lease liabilities	1,006
Right-of-use assets obtained in exchange for new operating lease liabilities	1,342
Weighted-average remaining lease term – finance leases	3.41
Weighted-average remaining lease term – operating leases	6.26
Weighted-average discount rate – finance leases	2.71%
Weighted-average discount rate – operating leases	2.14%

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

9. Leases and Other Commitments and Contingencies (continued)

For finance leases, right-of-use assets are recorded in property, buildings and equipment and lease liabilities are recorded in long-term debt in the accompanying consolidated balance sheets. For operating leases, right-of-use assets are recorded in operating lease assets and lease liabilities are recorded in operating lease liability, current and non-current, in the accompanying consolidated balance sheets.

The following table reconciles the undiscounted lease payments to the lease liabilities recorded on the accompanying consolidated balance sheet at December 31, 2019:

	<u>Finance leases</u>	<u>Operating leases</u>
2020	\$ 1,026	\$ 3,580
2021	977	2,404
2022	625	1,540
2023	251	1,359
2024	176	1,383
Thereafter	15	3,749
Total lease payments	<u>3,070</u>	<u>14,015</u>
Less imputed interest	123	981
Total lease obligation	<u>2,947</u>	<u>13,034</u>
Less current portion	961	3,331
Long-term portion	<u>\$ 1,986</u>	<u>\$ 9,703</u>

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

9. Leases and Other Commitments and Contingencies (continued)

Other Commitments and Contingencies

Various lawsuits and claims arising in the normal course of operations are pending or are on appeal against the System. While the outcome of these lawsuits cannot be determined at this time, management believes that any loss which may arise from the System's actions will not have a material adverse effect on the System's consolidated financial position or results of operations.

In relation to workers' compensation exposure, the System maintains a standby letter of credit in the amount of \$775 and is part of the \$10,000 line of credit in place to secure its self-insured workers' compensation program. There were no draws on the letter of credit in 2019 or 2018.

10. Medical Malpractice and General Liability Claims

As part of a structured and comprehensive risk management program, the System funds its risk of professional and general liability loss through RAC, a wholly-owned captive insurance company domiciled in the Cayman Islands.

RAC began accepting risk on January 1, 2004, and provides professional and general liability insurance protection for all entities within the System, including the Hospital, the Care Center, employed physicians and surgeons, the paramedical staff, and all affiliated corporations and divisions. Professional liability insurance is written as claims-made coverage while general liability is written on an occurrence basis. Prior to 2004, the Hospital purchased first-dollar primary and excess liability coverage in the commercial insurance market.

Currently, RAC issues policies with a maximum retention of \$3,000 for each medical incident or occurrence. RAC further retains, under a first excess or buffer policy, another \$2,000 for each medical incident with a \$2,000 aggregate retention. In addition, RAC issues an excess liability policy which provides separate limits towers of \$45,000 each. The first tower applies to professional liability claims; the second, to claims for all other liabilities. These excess limits are 100% reinsured by companies rated A or A+ by A.M. Best Company. The System has made, and will continue to make, adjustments to the structure, limits, and retentions of the captive program, as circumstances warrant.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

10. Medical Malpractice and General Liability Claims (continued)

Reserves for loss and loss adjustment expense are set based on management's best estimate of liability and damages. At December 31, 2019 and 2018, undiscounted reserve amounts were \$14,731 and \$9,861, respectively, and are included within other liabilities on the accompanying consolidated balance sheets. These reserves are estimates of the ultimate value of loss and loss adjustment expenses for all claims made during respective policy years and are subject to changes in amounts of settlements, verdicts, frequency of claims, or other economic or legal factors. These undiscounted reserves are not offset by estimates of reinsurance claims. While management believes the reserves for losses and loss adjustment expenses are adequate, it also recognizes the variability inherent in the data used in estimating these liabilities and that the ultimate value of losses and loss adjustment expense may vary significantly from the estimated amounts included in the accompanying consolidated financial statements. These estimates are continually reviewed and are adjusted, as necessary. Estimated receivables for reinsurance recoveries recorded by RAC total \$1,786 and \$1,754 at December 31, 2019 and 2018, respectively, and are included within other current assets on the accompanying consolidated balance sheets.

In relation to claims insured through RAC, the Hospital recorded an estimated insurance recovery receivable and medical malpractice claim liability at December 31, 2019 and 2018 equal to RAC's liability estimates. Such amounts are recorded within other assets and other liabilities within the Hospital's balance sheets and eliminate in consolidation.

The System has estimated its liability for losses due to claims from medical incidents that have occurred subsequent to 2004 but have not yet been reported to be approximately \$1,838 and \$1,877 at December 31, 2019 and 2018, respectively, with such estimated liability discounted at a rate of 4% based on expected timing of future payments. These amounts are included within other liabilities on the accompanying consolidated balance sheets.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued) (Dollars in Thousands)

11. Concentrations of Credit Risk

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

Concentration of gross accounts receivable from patients and third-party payors are as follows:

	December 31	
	2019	2018
Medicare and Medicaid	15%	17%
Blue Cross	23	22
Patients	1	1
Commercial	4	5
Managed care	54	51
Other third-party payors	3	4
	100%	100%

12. Fair Value Measurements

The System utilizes various methods of calculating the fair value of its financial assets. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements are applied based on the unit of account from the System's perspective. The unit of account determines what is being measured by reference to the level at which the asset or liability is aggregated (or disaggregated). The fair value hierarchy is comprised of three levels based on the source of inputs as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 – inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

12. Fair Value Measurements (continued)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. In determining fair value, the System uses valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers non-performance risk in its assessment of fair value.

The following table presents the financial instruments carried at fair value, excluding assets invested in the System's defined benefit plan, as of December 31, 2019 and 2018, by caption on the consolidated balance sheets based upon the fair value hierarchy defined above:

	Level 1	Level 2	Level 3	Total
December 31, 2019				
Cash and cash equivalents	\$ 22,383	\$ —	\$ —	\$ 22,383
Assets whose use is limited:				
Cash and cash equivalents	7,370	—	—	7,370
Fixed income:				
U.S. Treasury bills	4,836	—	—	4,836
Asset-backed securities	—	31,753	—	31,753
Corporate bonds	—	17,435	—	17,435
Mortgage-backed securities	16,692	15,347	—	32,039
Mutual funds:				
Fixed income	1,538	—	—	1,538
Domestic	21,298	—	—	21,298
International	13,045	—	—	13,045
Real estate	140	—	—	140
Commodities	411	—	—	411
Assets held by RAC:				
Cash and cash equivalents	3,131	—	—	3,131
Fixed income-asset fund	7,515	2,578	—	10,093
Domestic equities	11,292	—	—	11,292
Total assets whose use is limited	<u>87,268</u>	<u>67,113</u>	<u>—</u>	<u>154,381</u>
Total assets at fair value	<u>\$ 109,651</u>	<u>\$ 67,113</u>	<u>\$ —</u>	<u>\$ 176,764</u>

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

12. Fair Value Measurements (continued)

	Level 1	Level 2	Level 3	Total
December 31, 2018				
Cash and cash equivalents	\$ 22,854	\$ —	\$ —	\$ 22,854
Assets whose use is limited:				
Cash and cash equivalents	8,000	—	—	8,000
Fixed income:				
U.S. Treasury bills	6,885	—	—	6,885
Asset-backed securities	—	31,984	—	31,984
Corporate bonds	—	21,524	—	21,524
Mortgage-backed securities	7,784	15,226	—	23,010
Mutual funds:				
Fixed income	2,021	—	—	2,021
Domestic	13,814	—	—	13,814
International	6,678	—	—	6,678
Real estate	147	—	—	147
Commodities	582	—	—	582
Assets held by RAC:				
Cash and cash equivalents	1,791	—	—	1,791
Fixed income-asset fund	6,921	2,614	—	9,535
Domestic equities	2,016	8,937	—	10,953
Total assets whose use is limited	56,639	80,285	—	136,924
Total assets at fair value	\$ 79,493	\$ 80,285	\$ —	\$ 159,778

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

12. Fair Value Measurements (continued)

The following table presents the financial instruments of the defined benefit plan (see Note 8) as of December 31, 2019 and 2018, by the valuation hierarchy defined above:

	Level 1	Level 2	Level 3	Total
December 31, 2019				
Cash and cash equivalents	\$ 2,040	\$ –	\$ –	\$ 2,040
Equity funds:				
Domestic	47,939	–	–	47,939
International	28,925	–	–	28,925
Fixed-income mutual fund	86,811	–	–	86,811
	<u>\$ 165,715</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 165,715</u>
Investments measured at net asset value:				
Equity alternatives				35,644
Fixed income alternatives				10,196
Total				<u>\$ 211,555</u>
December 31, 2018				
Cash and cash equivalents	\$ 2,466	\$ –	\$ –	\$ 2,466
Equity funds:				
Domestic	35,494	–	–	35,494
International	20,947	–	–	20,947
Fixed-income mutual fund	77,253	–	–	77,253
	<u>\$ 136,160</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 136,160</u>
Investments measured at net asset value:				
Equity alternatives				48,673
Total				<u>\$ 184,833</u>

Fair value for Level 1 assets is based upon quoted market prices.

Level 2 assets consist of certain fixed-income securities for which the fair value at each year-end is estimated based on quoted prices and other valuation considerations (e.g., credit quality and prevailing interest rates).

Equity and fixed income alternative financial instruments maintained by the Plan represent the Plan's investment in funds of funds and are valued as described in Note 8. Financial information used to evaluate the alternative investments is provided by the investment manager or general partner and includes fair value valuations (quoted market prices and values determined through

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

12. Fair Value Measurements (continued)

other means) of underlying securities and other financial instruments held by the investee and estimates that require varying degrees of judgment. The alternative investments may indirectly expose the Plan to securities lending, short sales of securities, and trading in futures and forwards contracts, options, and other derivative products. Alternative investments often have liquidity restrictions under which capital may be divested only at specified times. At December 31, 2019 and 2018, there were no commitments or liquidity restrictions.

13. Net Assets with Donor Restrictions

Net assets with donor restrictions are available for the following purposes:

	December 31	
	2019	2018
Health care programs	\$ 2,480	\$ 1,458
Children's fund	1,087	2,608
Health education	1,256	1,759
Purchase of equipment	126	223
	<u>\$ 4,949</u>	<u>\$ 6,048</u>

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

14. Functional Expenses

Operating expenses by function and natural classification are as follows:

	2019		
	Health Care Program Expenses	General and Administrative Expenses	Total Expenses
Salaries and wages	\$ 193,163	\$ 42,980	\$ 236,143
Resident and physician fees	9,593	1,471	11,064
Employee benefits	43,496	9,678	53,174
Supplies and other	96,103	53,768	149,871
Governmental taxes, fees, and assessments	3,028	270	3,298
Interest	8,624	449	9,073
Depreciation and amortization	25,109	408	25,517
	\$ 379,116	\$ 109,024	\$ 488,140
	2018		
	Health Care Program Expenses	General and Administrative Expenses	Total Expenses
Salaries and wages	\$ 186,716	\$ 43,234	\$ 229,950
Resident and physician fees	10,076	1,518	11,594
Employee benefits	43,626	10,102	53,728
Supplies and other	87,036	54,579	141,615
Governmental taxes, fees, and assessments	2,872	1,021	3,893
Interest	9,035	493	9,528
Depreciation and amortization	24,318	408	24,726
	\$ 363,679	\$ 111,355	\$ 475,034

The accompanying consolidated financial statements report certain expense categories that are attributable to more than one health care service or support function. Costs not directly attributable to a function are allocated on a functional basis based on internal records and estimates.

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

15. Other Operating Revenue

Other operating revenue consists of the following:

	Year Ended December 31	
	2019	2018
Grant revenue	\$ 1,417	\$ 2,329
Rental income	2,068	1,892
Electronic health records	177	306
Investment income <i>(Note 4)</i>	4,786	2,660
Child Protection Center revenue	2,980	1,971
Retail pharmacy cost sharing	5,340	5,122
Nursing services	1,789	1,745
Food services	1,841	1,976
Physician billing services	4,368	4,631
Ambulance services	458	642
Solar energy credits	1,065	928
Adult day care	–	154
Outreach laboratory fees	372	368
Research studies	429	486
Purchasing rebates and settlements	1,444	437
Joint venture distribution	363	–
Parking	434	438
Pay for performance initiatives	1,453	921
Contributions	685	920
Other	1,657	2,340
	\$ 33,126	\$ 30,266

Saint Peter's Healthcare System, Inc.

Notes to Consolidated Financial Statements (continued)
(Dollars in Thousands)

16. Subsequent Events

Subsequent events have been evaluated through April 24, 2020 which is the date the accompanying consolidated financial statements were issued.

Due to the global viral outbreak caused by Coronavirus Disease 2019 (COVID-19) in 2020, there have been resulting effects which could negatively impact the System's financial condition, including significant stock market exchange volatility, including various temporary volatility trading halts which commenced initially on March 9, 2020 due to market declines, various temporary business closures and event cancellations, and other effects which could result in supply disruptions and/or decisions to defer elective procedures and other medical treatments at the System as the broader economic impact of COVID-19 develops. Management continues to closely monitor the impact of COVID-19 in many respects. The ultimate impact of these matters to the System and its financial condition is presently unknown. To enhance liquidity, in April 2020, the System entered into a \$10,000 revolving line of credit with a bank. Also in April 2020, the System drew \$9,200 on its previously existing line of credit (see Note 7). Additionally, the System is participating in the Centers for Medicare & Medicaid Services' Accelerated and Advance Payment Program under which it received approximately \$36,459 in April 2020 in expedited payments for future services. This advance payment amount will be recouped over time as Medicare services are provided after a 120-day delay period, with a final repayment of any remaining balance due in April 2021. The System also received grant distributions under the Coronavirus Aid, Relief, and Economic Security (CARES) Act totaling \$9,084 through April 24, 2020. The accompanying consolidated financial statements as of and for the year ended December 31, 2019 do not reflect the effects of these subsequent events.

Supplementary Information

Saint Peter's Healthcare System, Inc.

Consolidating Balance Sheet
(In Thousands)

December 31, 2019

	Saint Peter's University Hospital & Subsidiaries			Saint Peter's Health & Management Services						Saint Peter's Healthcare System, Inc.						Total Saint Peter's Health Care System			
	Obligated Group Saint Peter's University Hospital	Consolidating and Eliminating Entries	Total Saint Peter's University Hospital & Subs	Care Center	Properties	SP Solar Energy Solutions	SP Health & Mgmt Services	Gianna Phys Practice NY	Consolidating and Eliminating Entries	Total Saint Peter's Health & Management Services	Saint Peter's Healthcare System, Inc	Saint Peter's Foundation	National Gianna	SPHCS Physician Associates	Saint Peter's Advanced Care		Saint Peter's Specialty Physicians	Consolidating and Eliminating Entries	
Assets																			
Current assets:																			
Cash and cash equivalents	\$ 19,515	\$ -	\$ -	\$ 19,515	\$ 52	\$ 293	\$ 9	\$ -	\$ 1	\$ -	\$ 355	\$ 1,152	\$ 975	\$ -	\$ 384	\$ -	\$ 2	\$ -	\$ 22,383
Patient accounts receivable, net	51,190	-	-	51,190	-	-	-	-	-	-	-	-	-	-	-	-	-	-	51,190
Assets whose use is limited, current portion	118,258	-	-	118,258	-	-	-	-	-	-	-	-	4,566	-	-	-	-	-	122,824
Supplies	5,450	-	-	5,450	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5,450
Estimated third-party payer settlements, current portion	507	-	-	507	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Due from related parties, current portion	5,773	-	-	5,773	-	-	-	-	-	-	-	88,977	-	-	3,547	-	-	(98,297)	507
Other current assets	9,754	-	-	11,540	-	4	8	-	-	12	-	2,540	304	-	148	-	-	-	-
Total current assets	210,447	1,786	-	212,233	52	297	17	-	1	367	92,669	5,845	-	4,079	-	39	(98,297)	216,935	
Assets whose use is limited, less current portion	15,458	24,517	-	39,975	-	-	-	-	-	-	-	-	-	-	-	-	-	-	39,975
Property, plant, equipment and construction, net	176,485	-	-	176,485	-	3,210	7,099	-	-	10,309	-	1	-	1,835	-	-	-	-	188,630
Estimated third-party payer settlements, less current portion	516	-	-	516	-	-	-	-	-	-	-	-	-	-	-	-	-	-	516
Operating lease assets	7,170	-	-	7,170	-	-	-	-	-	-	552	-	-	5,312	-	-	-	-	13,034
Beneficial interest in Foundation	5,613	-	-	5,613	-	-	-	-	-	-	-	-	-	-	-	-	-	(5,613)	-
Due from related parties, noncurrent	2,023	-	-	2,023	-	-	-	-	-	-	-	-	-	-	-	-	-	(2,023)	-
Investments in joint ventures and other assets	25,093	-	(20,592)	4,501	-	-	-	2,343	-	2,343	-	-	-	-	-	-	(500)	-	
	\$ 442,805	\$ 26,303	\$ (20,592)	\$ 448,516	\$ 52	\$ 3,507	\$ 7,116	\$ 2,343	\$ 1	\$ 13,019	\$ 93,221	\$ 5,974	\$ -	\$ 11,226	\$ -	\$ 39	\$ (106,433)	\$ 465,562	
Liabilities and net assets																			
Current liabilities:																			
Current portion of long-term debt	\$ 8,202	\$ -	\$ -	\$ 8,202	\$ -	\$ 57	\$ 376	\$ -	\$ -	\$ 433	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 8,635
Accounts payable	21,808	1,193	-	23,001	-	-	-	-	-	-	2,457	-	-	482	-	-	-	-	25,940
Accrued expenses and other liabilities	33,740	-	-	33,740	-	8	-	-	39	47	3,745	315	-	981	34	52	-	-	38,914
Accrued interest	3,933	-	-	3,933	-	-	-	-	-	-	-	-	-	-	-	-	-	-	3,933
Current portion of operating lease liability	1,767	-	-	1,767	-	-	-	-	-	-	264	-	-	1,300	-	-	-	-	3,331
Estimated third-party payer settlements, current portion	2,308	-	-	2,308	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2,308
Due to related parties	12,780	-	-	12,780	-	3	2,557	-	3,297	5,857	80,592	46	-	70,642	2,323	3,020	(175,260)	-	
Total current liabilities	84,538	1,193	-	85,731	-	68	2,933	-	3,336	6,337	87,058	361	-	73,405	2,357	3,072	(175,260)	83,061	
Long-term debt, less current portion	135,344	-	-	135,344	-	1,706	2,896	-	-	4,602	-	-	-	-	-	-	-	-	139,946
Operating lease liability, less current portion	5,403	-	-	5,403	-	-	-	-	-	-	288	-	-	4,012	-	-	-	-	9,703
Estimated third-party payer settlements, less current portion	2,731	-	-	2,731	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2,731
Accrued pension liability	136,928	-	-	136,928	-	-	-	-	-	-	5,875	-	-	-	-	-	-	-	142,803
Other liabilities	27,714	14,731	(14,692)	27,753	-	-	-	-	-	-	-	-	-	-	-	-	-	-	27,753
Total liabilities	392,658	15,924	(14,692)	393,890	-	1,774	5,829	-	3,336	10,939	93,221	361	-	77,417	2,357	3,072	(175,260)	405,997	
Net assets:																			
Net assets without donor restrictions	43,789	10,379	(5,900)	48,268	52	1,733	1,287	2,343	(3,335)	2,080	-	1,409	-	(66,191)	(2,357)	(3,033)	74,440	54,616	
Net assets with donor restrictions	6,358	-	-	6,358	-	-	-	-	-	-	-	4,204	-	-	-	-	(5,613)	-	4,949
Total net assets	50,147	10,379	(5,900)	54,626	52	1,733	1,287	2,343	(3,335)	2,080	-	5,613	-	(66,191)	(2,357)	(3,033)	68,827	59,565	
	\$ 442,805	\$ 26,303	\$ (20,592)	\$ 448,516	\$ 52	\$ 3,507	\$ 7,116	\$ 2,343	\$ 1	\$ 13,019	\$ 93,221	\$ 5,974	\$ -	\$ 11,226	\$ -	\$ 39	\$ (106,433)	\$ 465,562	

Note: The consolidating schedules are presented for supplementary informational purposes. Due to the effects of intercompany transactions, which are eliminated in consolidation, the schedules are not intended to present the financial position or results of operations of the individual entities.

Saint Peter's Healthcare System, Inc.

Consolidating Statement of Operations and Changes in Net Assets
(In Thousands)

Year Ended December 31, 2019

	Saint Peter's University Hospital & Subsidiaries			Saint Peter's Health & Management Services						Saint Peter's Healthcare System, Inc.						Total Saint Peter's Health Care System			
	Obligated Group Saint Peter's University Hospital	RAC	Consolidating and Eliminating Entries	Total Saint Peter's University Hospital & Subs	Care Center	Properties	SP Solar Energy Solutions	SP Health & Mgmt Services	Gianna Phys Practice NY	Consolidating and Eliminating Entries	Total Saint Peter's Health & Management Services	Saint Peter's Healthcare System, Inc	Saint Peter's Foundation	National Gianna	Saint Peter's Physician Associates		Saint Peter's Advanced Care	Saint Peter's Specialty Physicians	Consolidating and Eliminating Entries
Revenue, gains and other support:																			
Net patient service revenue	\$ 457,097	\$ -	\$ -	\$ 457,097	\$ -	\$ -	\$ -	\$ -	\$ 77	\$ -	\$ 77	\$ -	\$ -	\$ -	\$ 9,539	\$ -	\$ 89	\$ -	\$ -
Other operating revenue	29,630	4,607	(3,901)	30,336	-	246	1,065	-	66	-	1,377	46,045	816	-	920	-	-	(46,368)	33,126
Net assets released from restriction	10	-	-	10	-	-	-	-	-	-	-	-	1,723	566	-	-	-	-	2,299
Total revenue, gains, and other support	486,737	4,607	(3,901)	487,443	-	246	1,065	-	143	-	1,454	46,045	2,539	566	10,459	-	89	(46,368)	502,227
Expenses:																			
Salaries and wages	225,076	-	-	225,076	-	7	54	-	219	-	280	22,376	46	5	10,719	-	17	(22,376)	236,143
Resident and physician fees	9,628	-	-	9,628	-	-	-	-	5	-	5	78	-	-	1,299	-	54	-	11,064
Employee benefits	50,769	-	-	50,769	-	2	12	-	47	-	61	5,039	10	1	2,333	-	-	(5,039)	53,174
Supplies and other	145,020	9,989	(3,901)	151,108	-	11	99	-	85	-	195	17,753	2,641	813	4,780	-	27	(27,446)	149,871
Governmental taxes, fees, and assessments	3,281	-	-	3,281	-	17	-	-	-	-	17	-	-	-	-	-	-	-	3,298
Interest	8,535	-	-	8,535	-	89	449	-	-	-	538	-	-	-	-	-	-	-	9,073
Depreciation and amortization	24,704	-	-	24,704	-	75	408	-	-	-	483	-	-	-	330	-	-	-	25,517
Total expenses	467,013	9,989	(3,901)	473,101	-	201	1,022	-	356	-	1,579	45,246	2,697	819	19,461	-	98	(54,861)	488,140
Income (loss) from operations	19,724	(5,382)	-	14,342	-	45	43	-	(213)	-	(125)	799	(158)	(253)	(9,002)	-	(9)	8,493	14,087
Equity in net earnings of joint ventures and other income	376	-	-	376	-	-	-	485	-	-	485	-	-	-	-	-	-	(376)	485
Gain on sale of property, plant, and equipment	61	-	-	61	-	-	-	-	-	-	-	-	-	-	7	-	-	-	68
Net change in unrealized gains and losses on equity investments	4,143	1,842	-	5,985	-	-	-	-	-	-	-	-	340	-	-	-	-	-	6,325
Non-operating net periodic pension cost	(3,951)	-	-	(3,951)	-	-	(2)	-	(1)	-	(3)	(799)	(1)	-	(39)	-	-	799	(3,994)
Forgiveness of debt	-	-	-	-	-	-	-	-	-	-	-	-	-	303	-	-	-	(303)	-
Equity transfer	(629)	-	-	(629)	-	-	-	253	-	-	253	-	-	-	-	-	-	376	-
Excess (deficiency) of revenue over expenses	19,724	(3,540)	-	16,184	-	45	41	738	(214)	-	610	-	181	50	(9,034)	-	(9)	8,989	16,971
Net change in unrealized gains and losses other-than-trading investments	2,023	115	-	2,138	-	-	-	-	-	-	-	-	61	-	-	-	-	-	2,199
Change in pension liability to be recognized in future periods	(14,263)	-	-	(14,263)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(14,263)
Donated equipment and other	2,145	-	-	2,145	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2,145
Increase (decrease) in net assets without donor restrictions before discontinued operations	9,629	(3,425)	-	6,204	-	45	41	738	(214)	-	610	-	242	50	(9,034)	-	(9)	8,989	7,052
Gain (loss) from discontinued operations	-	-	-	-	66	-	-	-	-	-	66	-	-	-	-	-	-	-	66
Increase (decrease) in net assets without donor restrictions	9,629	(3,425)	-	6,204	66	45	41	738	(214)	-	676	-	242	50	(9,034)	-	(9)	8,989	7,118
Net assets with donor restrictions:																			
Restricted gifts and contributions and related items	12	-	-	12	-	-	-	-	-	-	-	-	1,161	27	-	-	-	-	1,200
Equity transfer	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net change in beneficial interest in Foundation	(320)	-	-	(320)	-	-	-	-	-	-	-	-	-	-	-	-	-	320	-
Net assets released from restriction	(10)	-	-	(10)	-	-	-	-	-	-	-	-	(1,723)	(566)	-	-	-	-	(2,299)
(Decrease) increase in net assets with donor restrictions	(318)	-	-	(318)	-	-	-	-	-	-	-	-	(562)	(539)	-	-	-	320	(1,099)
Increase (decrease) in net assets	9,311	(3,425)	-	5,886	66	45	41	738	(214)	-	676	-	(320)	(489)	(9,034)	-	(9)	9,309	6,019
Net assets at beginning of year	40,836	13,804	(5,900)	48,740	(14)	1,688	1,246	1,605	(3,121)	-	1,404	-	5,933	489	(57,157)	(2,357)	(3,024)	59,518	53,546
Net assets at end of year	\$ 50,147	\$ 10,379	\$ (5,900)	\$ 54,626	\$ 52	\$ 1,733	\$ 1,287	\$ 2,343	\$ (3,335)	\$ -	\$ 2,080	\$ -	\$ 5,613	\$ -	\$ (66,191)	\$ (2,357)	\$ (3,033)	\$ 68,827	\$ 59,565

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