



Consolidated Financial Statements,
Supplementary Information – Virtua
Obligated Group and Report of
Independent Certified Public
Accountants

Virtua Health, Inc.

December 31, 2019 and 2018



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GRANT THORNTON LLP

2001 Market St., Suite 700
Philadelphia, PA 19103-7065

D +1 215 561 4200

F +1 215 561 1066

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Trustees
Virtua Health, Inc.

We have audited the accompanying consolidated financial statements of Virtua Health, Inc., (“Virtua Health”), 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 consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors’ responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Virtua Health, Inc. as of December 31, 2019 and 2018 and the results of its operations, changes in its net assets, and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of matter

As discussed in Note B to the consolidated financial statements, in 2019, Virtua Health adopted Accounting Standard Update 2016-02, *Leases*. 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 supplementary information on pages 49-54 is presented for the purpose of additional analysis, rather than to present the financial position, results of operations and changes in net assets, and cash flows of the individual entities, and is not a required part of the consolidated financial statements. Such supplementary 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 our audits of the consolidated financial statements and certain additional procedures. These additional procedures included comparing and reconciling the information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.



Philadelphia, Pennsylvania
May 15, 2020

Virtua Health, Inc.

CONSOLIDATED BALANCE SHEETS

December 31,

(In thousands)

ASSETS	2019	2018
CURRENT ASSETS:		
Cash and cash equivalents	\$ 81,847	\$ 44,109
Assets limited as to use	24,641	24,510
Patient accounts receivable	179,546	143,641
Other current assets	78,941	57,386
Total current assets	364,975	269,646
ASSETS LIMITED AS TO USE:		
By Board of Trustees' designation	1,201,059	1,019,812
Other designated funds	233,619	273,322
Under debt agreements	-	26,617
Trust funds	19,022	5,116
Donor-restricted funds	18,171	14,075
	1,471,871	1,338,942
PROPERTY, PLANT, AND EQUIPMENT, NET	1,027,307	883,932
OTHER LONG-TERM ASSETS:		
Investment in unconsolidated joint ventures	177,549	162,949
Goodwill and other intangibles	59,192	25,980
Other assets	25,953	26,090
Beneficial interest in perpetual trust	8,445	7,459
Right of use assets	139,768	-
	410,907	222,478
TOTAL ASSETS	\$ 3,275,060	\$ 2,714,998

(Continued)

Virtua Health, Inc.

CONSOLIDATED BALANCE SHEETS - CONTINUED

December 31,

(In thousands)

	2019	2018
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Current maturities of long-term debt	\$ 12,787	\$ 11,780
Current maturities of lease liability	31,040	-
Accounts payable and accrued expenses	225,378	137,150
Accrued compensation and related liabilities	77,208	71,099
Accrued interest payable	3,648	9,841
Estimated settlements due to third-party payers, net	3,147	2,119
Total current liabilities	353,208	231,989
LONG-TERM LIABILITIES:		
Estimated settlements due to third-party payers	2,951	4,355
Self-insurance liabilities	44,488	36,006
Accrued retirement benefits	23,754	27,622
Long-term debt, net of current maturities	550,152	582,119
Lease liability, net of current maturities	110,338	-
Other liabilities	10,054	22,263
Total liabilities	1,094,945	904,354
NET ASSETS:		
Without donor restrictions:		
Virtua Health, Inc.	2,097,938	1,744,932
Noncontrolling interests	52,518	40,483
	2,150,456	1,785,415
With donor restrictions	29,659	25,229
Total net assets	2,180,115	1,810,644
TOTAL LIABILITIES AND NET ASSETS	\$ 3,275,060	\$ 2,714,998

The accompanying notes are an integral part of these statements.

Virtua Health, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS

Years ended December 31,

(In thousands)

	<u>2019</u>	<u>2018</u>
NET ASSETS WITHOUT DONOR RESTRICTIONS:		
Revenue:		
Patient service revenue	\$ 1,501,578	1,228,836
Other revenue	73,310	64,591
Equity in income of unconsolidated joint ventures	57,702	49,477
Total revenue	<u>1,632,590</u>	<u>1,342,904</u>
Expenses:		
Salaries and wages	753,270	599,161
Professional fees	29,578	19,830
Employees' fringe benefits	169,280	135,021
Other operating expenses	574,058	448,155
Interest	17,805	21,291
Depreciation and amortization	106,697	95,583
Total expenses	<u>1,650,688</u>	<u>1,319,041</u>
(LOSS) GAIN FROM OPERATIONS BEFORE GAIN ON ACQUISITION	(18,098)	23,863
Gain on acquisition of Our Lady of Lourdes Health Care Services, Inc.	<u>174,253</u>	<u>-</u>
INCOME FROM OPERATIONS (includes \$15,892 in 2019 and \$13,083 in 2018 of income attributed to noncontrolling interests)	156,155	23,863
NONOPERATING GAINS AND LOSSES:		
Investment return, net	216,479	(67,627)
Loss on extinguishment of debt	(7,880)	-
Other accrued retirement costs	(1,563)	658
Total nonoperating gain (losses), net	<u>207,036</u>	<u>(66,969)</u>
EXCESS OF (DEFICIT IN) REVENUE AND NONOPERATING GAINS (LOSSES), NET OVER EXPENSES	363,191	(43,106)
EXCESS OF REVENUE AND NONOPERATING GAINS, NET OVER EXPENSES ATTRIBUTED TO NONCONTROLLING INTERESTS	<u>(15,892)</u>	<u>(13,083)</u>
EXCESS OF (DEFICIT IN) REVENUE AND NONOPERATING GAINS (LOSSES), OVER EXPENSES ATTRIBUTED TO VIRTUA HEALTH, INC.	347,299	(56,189)

The accompanying notes are an integral part of these statements.

Virtua Health, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS - CONTINUED

Years ended December 31,

(In thousands)

	2019	2018
EXCESS OF (DEFICIT IN) REVENUE AND NONOPERATING GAINS (LOSSES), OVER EXPENSES ATTRIBUTED TO VIRTUA HEALTH, INC.	\$ 347,299	\$ (56,189)
OTHER CHANGES IN NET ASSETS WITHOUT DONOR RESTRICTIONS - VIRTUA HEALTH, INC.:		
Net assets released for property, plant, and equipment	250	7,163
Other changes in accrued retirement benefits	5,457	(4,111)
Other	-	(3)
Increase (decrease) in net assets without donor restrictions - Virtua Health, Inc.	353,006	(53,140)
NONCONTROLLING INTERESTS:		
Excess of revenues and nonoperating gains, net over expenses attributable to noncontrolling interests	15,892	13,083
Distributions	(10,715)	(12,899)
Membership interest transfer, net	6,858	8,871
Increase in net assets without donor restrictions - noncontrolling interests	12,035	9,055
NET ASSETS WITH DONOR RESTRICTIONS:		
Contributions, net	3,767	3,646
Investment return, net	393	(108)
Increase (decrease) in beneficial interest in perpetual trust	986	(1,071)
Net assets released from restrictions for operations	(1,378)	(596)
Net assets released from restrictions for property, plant, and equipment	(250)	(7,163)
Net assets acquired in acquisition of Our Lady of Lourdes Health Care Services, Inc.	912	-
Increase (decrease) in net assets with donor restrictions	4,430	(5,292)
INCREASE (DECREASE) IN NET ASSETS	369,471	(49,377)
NET ASSETS - beginning of year	1,810,644	1,860,021
NET ASSETS - end of year	\$ 2,180,115	\$ 1,810,644

The accompanying notes are an integral part of these statements.

Virtua Health, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31,

(In thousands)

	2019	2018
	<u> </u>	<u> </u>
OPERATING ACTIVITIES:		
Increase (decrease) in net assets	\$ 369,471	\$ (49,377)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Other changes in accrued retirement benefits	(5,457)	4,111
Gain on acquisition of Our Lady of Lourdes Health Care Services, Inc.	(174,253)	-
Loss from early extinguishment of debt	7,880	-
Distributions from unconsolidated joint ventures	49,863	48,086
Equity in income of unconsolidated joint ventures	(57,702)	(49,477)
Distributions to noncontrolling interests	10,715	12,899
Membership interest transfer	156	(8,871)
Restricted contributions, including change in beneficial interest in perpetual trust and net assets from acquisition	(5,665)	(2,575)
Depreciation and amortization	106,697	95,583
Amortization of premium, discount and financing costs	(2,933)	(346)
Net realized and unrealized (gains) losses on investments	(221,421)	62,832
Changes in certain assets and liabilities:		
Patient accounts receivable	13,849	(12,874)
Other assets	(9,009)	(207)
Accounts payable and accrued expenses	66,747	6,963
Accrued compensation and related liabilities	(24,470)	10,249
Accrued interest payable	(6,193)	(136)
Self-insurance liabilities	15,891	13,589
Lease liabilities	(1,332)	-
Other liabilities	1,929	(2,111)
Accrued retirement benefits	1,122	(7,271)
Estimated settlements due to third-party payers	(376)	(4,137)
Net cash provided by operating activities	<u>135,509</u>	<u>116,930</u>
INVESTING ACTIVITIES:		
Purchases of property, plant, and equipment	(102,276)	(127,621)
Purchases of investments	(469,911)	(155,492)
Sales of investments	557,888	173,605
Investment in unconsolidated joint ventures	(7,874)	(7,609)
Proceeds from sale of managed care organization	-	14
Cash paid, net for acquisition of Our Lady of Lourdes Health Care Services, Inc.	(30,457)	-
Cash paid, net for acquisition under SCSJ and other physician services	-	(4,837)
Net cash used in investing activities	<u>(52,630)</u>	<u>(121,940)</u>
FINANCING ACTIVITIES:		
Repayment of long-term debt	(241,895)	(11,395)
Proceeds from issuance of long-term debt	205,435	-
Distributions to noncontrolling interests	(10,715)	(12,899)
Net restricted contributions and pledge payments	2,034	1,180
Net cash used in financing activities	<u>(45,141)</u>	<u>(23,114)</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	37,738	(28,124)
CASH AND CASH EQUIVALENTS - beginning of year	<u>44,109</u>	<u>72,233</u>
CASH AND CASH EQUIVALENTS - end of year	<u>\$ 81,847</u>	<u>\$ 44,109</u>

The accompanying notes are an integral part of these statements.

Virtua Health, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED

Years ended December 31,

(In thousands)

	<u>2019</u>	<u>2018</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest, net of capitalized interest	<u>\$ 23,998</u>	<u>\$ 22,147</u>
Change in accrued capital expenditures in accounts payable and accrued expenses	<u>\$ 6,697</u>	<u>\$ 1,583</u>
Assets and liabilities acquired through finance leases	<u>\$ 1,218</u>	<u>\$ -</u>

The accompanying notes are an integral part of these statements.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2019 and 2018

(Dollars in thousands)

NOTE A - ORGANIZATION

Virtua Health, Inc. is a nonprofit corporation incorporated in New Jersey to establish, operate, maintain, and conduct a regional health network serving Burlington, Camden, Mercer, Ocean, and Gloucester counties in New Jersey, and Philadelphia, Pennsylvania. The consolidated financial statements include the accounts of Virtua Health, Inc., and its controlled entities (collectively, "Virtua Health"). The Virtua Health entities prior to the acquisition will be referred to as "Virtua."

Effective with business operations on July 1, 2019, Virtua Health acquired the membership interest of Our Lady of Lourdes Health Care Services, Inc. ("Lourdes"), a nonprofit corporation, from Maxis Health System ("Maxis"), a wholly controlled subsidiary of Trinity Health, pursuant to a Membership Transfer Agreement executed on June 4, 2018. The acquisition includes substantially all of the healthcare operations and certain assets and working capital of Lourdes. Lourdes includes the entity formerly known as Our Lady of Lourdes Medical Center, Inc., now known as Virtua-Our Lady of Lourdes Hospital, Inc. (Camden, New Jersey) and the entity formerly known as Lourdes Medical Center of Burlington County, Inc., now known as Virtua-Willingboro Hospital, Inc. (Willingboro, New Jersey) and most of their affiliated operations. The consideration paid was the net of a negotiated fixed price reduced by a set minimum guaranteed net balance of working capital accounts acquired by Virtua Health. See Note C for further details.

Virtua Health is composed of the following controlled entities:

Virtua Hospital Group

Virtua-Memorial Hospital Burlington County, Inc. ("Virtua-Memorial") owns and operates a 383-licensed-bed, tax exempt acute care hospital in Mount Holly, New Jersey. Virtua-Memorial provides general health care services to residents within its geographic location for a wide range of inpatient and outpatient services, including medical, surgical, cardiac, obstetrical, gynecological, oncological, pediatric, emergency, and ambulatory care. Virtua-Memorial also provides a variety of outpatient services in space leased from a third-party developer in the Virtua Health and Wellness Center in Moorestown, New Jersey.

Virtua-Memorial and an unrelated corporation own Virtua-SCA Holdings, LLC ("SCA Holdings") in which Virtua-Memorial maintains a 51% ownership interest. The financial results are consolidated into Virtua-Memorial's financial statements. SCA Holdings' has ownership interest in multiple joint ventured ambulatory surgical centers throughout New Jersey. The purpose of SCA Holdings is to acquire, own and operate ambulatory surgical centers and to maintain a majority equity interest in such owned centers.

Virtua-Memorial and an unrelated corporation own Emmaus Holdings, LLC ("Emmaus Holdings") in which Virtua-Memorial maintains a 50.10% ownership interest. The financial results are consolidated into Virtua-Memorial's financial statements. The purpose of Emmaus Holdings is to hold a majority equity interest in an ambulatory surgery center.

Virtua-Memorial and an unrelated corporation own Virtua-USP Princeton, LLC ("Virtua-USP Princeton") in which Virtua-Memorial maintains a 68.2% ownership interest. The financial results are consolidated into Virtua-Memorial's financial statements. The purpose of Virtua-USP Princeton is to hold a majority equity interest in an ambulatory surgery center.

Virtua-West Jersey Health System, Inc. ("Virtua-West Jersey") is a 600-licensed-bed, tax-exempt health system that owns and operates two general acute care hospitals, which are located in Marlton, and Voorhees, New Jersey. Virtua-West Jersey provides general health care services to residents within its geographic location for a wide range of inpatient and outpatient services, including medical, surgical,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE A - ORGANIZATION - CONTINUED

cardiac, obstetrical, gynecological, oncological, pediatric, emergency, and ambulatory care. Virtua-West Jersey owns and operates facilities in Berlin and Camden, New Jersey, which provide emergent care and other outpatient services; and rents space in the building where the Camden facility is located, primarily to outside social services programs. Virtua-West Jersey also provides a variety of outpatient services, in space leased from a third-party developer, in two Virtua Health and Wellness Centers, one in Voorhees, New Jersey and one in Washington Township, New Jersey, as well as in a fitness center located in Voorhees, New Jersey.

Virtua-West Jersey and an unrelated corporation own Voorhees Endoscopy Holding Co., LLC ("Voorhees Endo Holding") in which Virtua-West Jersey maintains a 51% ownership interest. The financial results are consolidated into Virtua-West Jersey's financial statements. The purpose of Voorhees Endo Holding is to own a majority equity interest in an ambulatory surgical center.

Virtua-West Jersey is also the sole corporate member of West Jersey RENEW, Inc., a nonprofit corporation, which is inactive.

Lourdes Hospital Group

Virtua-Our Lady of Lourdes Hospital, Inc. ("Virtua-Lourdes"), owns and operates a 354-licensed-bed, tax exempt tertiary acute care hospital in Camden, New Jersey. Virtua-Lourdes provides general health care services to residents within its geographic location for a wide range of inpatient and outpatient services, including medical, surgical, transplants, cardiac, neurology, obstetrical, gynecological, oncological, pediatric, emergency, and ambulatory care. Virtua-Lourdes also provides a variety of outpatient services in space leased from a third-party developer in Cherry Hill, New Jersey. Our Lady of Lourdes School of Nursing, Inc. is a controlled subsidiary of Virtua-Lourdes.

Virtua-Lourdes maintains a 51% ownership interest in Centennial SurgUnit, LLC ("CS"), an ambulatory surgical center located in Voorhees, New Jersey.

Virtua-Willingboro Hospital, Inc. ("Virtua-Willingboro") owns and operates a 169-licensed-bed, tax exempt acute care hospital in Willingboro, New Jersey. Virtua-Willingboro provides general health care services to residents within its geographic location for a wide range of inpatient and outpatient services, including behavioral health, medical, surgical, cardiac, obstetrical, gynecological, oncological, pediatric, emergency, and ambulatory care.

Virtua Medical Group

Virtua Medical Group, PA ("VMG") is a not-for-profit captive professional association consisting of 605 clinicians, primarily specialty and primary care physicians. VMG provides services to Virtua's hospitals and also at many owned and leased physician-practice sites located throughout southern New Jersey.

Lourdes Medical Group

Lourdes Medical Associates, PA ("LMA") is a for-profit captive professional association consisting of 106 clinicians, primarily specialty and primary care physicians.

Health Management Services Organization, Inc. ("HMSO") is a for-profit company that maintains a minority equity interest in Lourdes Specialty Hospital of Southern New Jersey, LLC, a long-term acute care hospital located within Virtua-Willingboro. HMSO is a subsidiary of Ancillary Services, Inc. ("LAS"), a not-for-profit corporation.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE A - ORGANIZATION - CONTINUED

Lourdes Cardiology Services, PC (“LCS”) is a not-for profit captive professional corporation consisting of 51 clinicians, primarily cardiologists. LCS provides services to Virtua’s hospitals and also at many owned and leased physician-practice sites located throughout southern New Jersey.

Virtua Post-Acute and Long-Term Care

Virtua Health and Rehabilitation Center at Berlin, Inc., is a not-for-profit health care organization, which operates a 128-bed skilled nursing facility in Berlin, New Jersey.

Virtua Health and Rehabilitation Center at Mount Holly, Inc., is a not-for-profit health care organization, which operates a 180-bed skilled nursing facility in Mount Holly, New Jersey.

Virtua Home Care-Community Nursing Services (“CNS”) is a not-for-profit corporation, whose primary function is to hold the sole membership interest in VRI, Inc. (“VRI”), a for-profit organization. VRI primarily consists of fitness centers that are located in the Virtua Health and Wellness Centers in Moorestown and Washington Township, retail shops, management of a bioidentical hormone replacement therapy practice and private home health aide and companion services. The fitness center and other operations located in the Washington Township Health and Wellness Center closed as of December 31, 2018. CNS also operates a Health Promotions Solutions service line pursuant to a contract with Burlington County.

Virtua Foundation

Virtua Health Foundation, Inc. (“VHF”) is a not-for-profit corporation established to promote and support Virtua, its sole corporate member and affiliated corporations, and the health care of the population of southern New Jersey, by developing the resources necessary to attain these goals.

In 2003, Memorial Hospital of Burlington County Foundation (“MHBCF”), a not-for-profit corporation established to promote the scientific, educational, and charitable activities and policies of Virtua-Memorial, and West Jersey Health & Hospital Foundation, Inc. (“WJHHF”), a not-for-profit corporation, which raised funds for the benefit of Virtua-West Jersey, its subsidiaries, and the community, combined their operations and transferred their net assets into VHF. The restricted funds of MHBCF and WJHHF are administered in a manner consistent with the original donors’ intentions.

Lourdes Foundation

Our Lady of Lourdes Health Foundation, Inc. (“LHF”) is a not-for-profit corporation established to promote and support Lourdes, its sole corporate member and affiliated corporations, and the health care of the population of southern New Jersey, by developing the resources necessary to attain these goals.

Insurance Captive

Virtua Assurance, Inc. (“VAI”) is a for-profit captive insurance company in the state of Vermont whose sole shareholder is Virtua Health, Inc.

Virtua Population Health Management Group

VirtuaPhysicianPartners, LLC (“VPP”) is a limited liability company and clinically integrated network that enhances the access, quality, cost-efficiency and experience of healthcare for patients, and whose sole member is Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Lourdes Population Health Management Group

LHS Health Network, Inc. ("LHS") is a for-profit clinically integrated network that enhances the access, quality, cost-efficiency and experience of healthcare for patients. HMSO is the sole member of LHS.

Principles of Consolidation

Virtua Health, through Virtua-West Jersey, Virtua-Memorial and Virtua-Lourdes, owns interests in several companies that are included in the consolidated financial statements. The noncontrolling interests of these companies, Voorhees Endo Holding, SCA Holdings, Emmaus Holdings, Virtua-USP Princeton and CS are reported as a component of net assets. Significant intercompany balances and transactions have been eliminated. Ventures in which Virtua Health has financial interest and shares control equally with unrelated investors are accounted for under the equity method as discussed in Note I. As disclosed in Note K, the assets of any member in the Obligated Group may not be available to meet the obligations of other members in Virtua Health.

Basis of Accounting

The consolidated financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") consistent with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 954, *Health Care Entities*, and other pronouncements applicable to health care organizations.

Recently Adopted Accounting Pronouncement

In February 2016, the FASB issued ASU No. 2016 02, *Leases*, as amended, which requires (1) most leases to be recognized on the balance sheet and (2) disclosure about leasing arrangements. The new standard is effective for fiscal years beginning after December 15, 2018. The new standard establishes a right of use ("ROU") model that requires a lessee to recognize a ROU asset and lease liability on the balance sheet for all leases with a term longer than 12 months. Leases will be classified as finance or operating, with classification affecting the pattern and classification of expense recognition in the statement of operations.

Virtua Health adopted the new standard on January 1, 2019, and elected the option to apply the transition requirements in the standard. Consequently, financial information will not be updated and the disclosures required under the standard will not be provided for dates and periods before January 1, 2019.

The new standard provides a number of optional practical expedients in transition. Virtua Health has elected the "package of practical expedients," which permits entities to not reassess conclusions prior to the implementation of the new standard about lease identification, lease classification and initial direct costs.

The most significant effects on Virtua Health's consolidated financial statements relate to: (1) the recognition of new ROU assets and lease liabilities on the consolidated balance sheet for existing real estate and equipment operating leases; (2) the reclassification of existing liabilities for deferred rent related to the straight-line expense of rent payments for leases previously recorded as operating leases; (3) the reclassification of advance rental payments; and (4) providing significant new disclosures about leasing activities.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

The impact on the January 1, 2019 consolidated balance sheet is as follows:

- Recognize operating lease liabilities of \$130,692 based on the present value of the remaining minimum rental payments for existing operating leases.
- Recognize corresponding ROU assets of \$128,134 based on the operating lease liabilities, net of the reclassification of \$14,138 of deferred straight-line rent liabilities and advanced rental payments of \$11,580 from other assets.

The new standard also provides practical expedients for an entity's ongoing accounting. Virtua Health has elected the short-term lease recognition exemption for all leases that qualify. This means, for those leases that qualify, Virtua Health will not recognize ROU assets or lease liabilities, and this includes not recognizing ROU assets or lease liabilities for existing short-term leases of those assets in transition.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates are used in recording patient accounts receivable and patient service revenue, estimated settlements with third-party payers, useful lives of property, plant and equipment, goodwill and other intangibles, self-insurance program liabilities, accrued retirement benefits, and the reported fair values of certain assets and liabilities. Actual results could differ from those estimates.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, patient accounts receivable, assets limited as to use, investments, accounts payable and accrued expenses, estimated settlements with third-party payers and long-term debt. The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, patient accounts receivable, assets limited as to use, investments, accounts payable and accrued expenses and estimated settlements with third-party payers approximate fair value. Management's estimates of the fair value of other financial instruments are described elsewhere in the notes to the consolidated financial statements.

Cash and Cash Equivalents

Cash and cash equivalents include various checking, savings, time deposits, and money market accounts with initial maturities of three months or less. At December 31, 2019 and 2018, Virtua Health had cash balances in financial institutions that exceeded federal depository insurance limits. Management believes that credit risk related to these deposits is minimal.

Patient Accounts Receivable

Virtua Health recognizes a receivable when there is an unconditional right to payment, subject only to the passage of time. Patient accounts receivable, including billed accounts and unbilled accounts, which have the unconditional right to payment, and estimated amounts due from third-party payers for retroactive adjustments, are receivables if the right to consideration is unconditional and only the passage of time is required before payment of that consideration is due. The estimated uncollectible amounts are generally considered implicit price concessions that are a direct reduction to patient accounts receivable.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Assets Limited as to Use, Investments, and Investment Income

Investments in marketable equity, debt securities, and other investments are presented at fair value in the consolidated balance sheets as disclosed in Note G and H. Certain other investments are accounted for under the equity method of accounting as disclosed in Note I.

Assets limited as to use by the Board of Trustees' designation are resources arising from results of operations and investment returns that have been designated by the Board of Trustees for specific purposes.

Assets limited as to use - other designated funds are resources arising from results of operations that have been designated for specific purposes, such as strategic initiatives and self-funded professional liabilities.

Assets limited as to use - under debt agreements are held by a trustee under bond indenture agreements and consist of those assets designated for the payments of principal and interest due on indebtedness, and cost of issuance.

Assets limited as to use - trust funds include funds that are held by a trustee for the self-insurance workers' compensation program and assets for certain employee benefits.

Assets limited as to use - donor restricted funds are assets to be held in accordance with the donor's intentions. Donor restricted investment income is recognized as a direct increase or decrease to net assets with restrictions.

Investment income or losses (including realized and unrealized gains and losses on investments, interest, and dividends) are included in nonoperating gains and losses as investment returns, unless the income or losses are restricted by donor or law, or from those under debt agreements. Investment income or losses (including realized and unrealized gains and losses on investments, interest, and dividends) for those under debt agreements, are included in other revenue, except for interest income capitalized during construction, which is included in property, plant, and equipment, net.

Investments, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. As such, it is reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the consolidated balance sheets and consolidated statements of operations and changes in net assets.

Property, Plant, and Equipment

Property, plant, and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and are computed on the straight-line method. Equipment acquired under finance leases is amortized based on the straight line method over the shorter period of the lease term or the estimated useful life of the equipment. The following is the estimated useful lives by category:

Land improvements	5-25 years
Building and improvements	10-40 years
Fixed equipment	5-20 years
Furniture and fixtures	3-20 years

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Construction in progress represents amounts expended or incurred toward property and equipment projects that have not been completed. No depreciation or amortization has been recorded for these items. Interest cost incurred, net of investment income earned on borrowed funds, during the period of construction is capitalized as a component of the cost of acquiring those assets. In cases where internal cash reserves are used to fund construction, interest is capitalized based on average accumulated expenditures multiplied by the weighted-average interest rate on existing debt. Virtua had capitalized interest of \$720 for the year ended December 31, 2018.

Gifts of long-lived assets such as land, buildings, or equipment are reported as other changes in net assets without restrictions, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Leases

Virtua Health determines if an arrangement is a lease at inception of the contract. Right of use assets represent Virtua Health's right to use the underlying assets for the lease term and lease liabilities represent Virtua Health's obligation to make lease payments arising from the leases. Right of use assets and lease liabilities are recognized at commencement date based on the present value of lease payments over the lease term. Virtua Health uses an estimated incremental borrowing rate, which is derived from information available at the lease commencement date, in determining the present value of lease payments. Virtua Health determines this rate based on information obtained from its bankers, its secured debt fair value and publicly available data for instruments with similar characteristics.

Virtua Health's operating leases are primarily for real estate, including off-campus outpatient facilities, medical office buildings, and corporate and other administrative offices, as well as medical and office equipment. Finance leases are for medical equipment. The real estate lease agreements typically have initial terms of five to ten years, and equipment lease agreements typically have initial terms of three to five years. Virtua Health does not record leases with an initial term of 12 months or less ("short-term leases") in its consolidated balance sheets.

Virtua Health's real estate leases may include one or more options to renew, with renewals that typically can extend the lease term from five to ten years. The exercise of lease renewal options is at Virtua Health's sole discretion. In general, Virtua Health does not consider renewal options to be reasonably likely to be exercised, therefore, renewal options are generally not recognized as part of right of use assets and lease liabilities. The useful life of assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise. The majority of the medical equipment leases have terms of three years with no renewal options or bargain purchase options, so these assets are depreciated over their lease term.

Certain of Virtua Health's lease agreements for real estate include payments based on actual common area maintenance expenses. These variable lease payments are recognized in other operating expenses, net, but are not included in the right-of-use asset or liability balances. Virtua Health's lease agreements do not contain any material residual value guarantees, restrictions or covenants.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Impairment of Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If long-lived assets are deemed to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value. Assets to be disposed of are reported at the lower of the carrying amount or the fair value less costs to sell. As of December 31, 2019, management believes that no revisions to the remaining useful lives or write-down of long-lived assets are required.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, which is then treated as cost. The gifts are reported as net assets with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. As the donors' intentions are met, the net assets are reclassified to net assets without donor restrictions and reported in the consolidated statements of operations and changes in net assets as other revenue for operating purposes and as other changes in net assets without donor restrictions for acquisitions of property, plant, and equipment.

Goodwill and Other Intangibles

Goodwill represents the excess of the purchase price over the estimated fair value of the net assets of businesses acquired. Other intangibles represent a certificate of need to perform cardiology services in Camden County, New Jersey, a license to operate long-term care beds, and various other state licenses, all of which were acquired for future use and have an indefinite useful life, as well as a trade name that is being amortized over its expected useful life of ten years. For the years ended December 31, 2019 and 2018, Virtua Health added goodwill and intangibles of \$33,212 and \$10,867, respectively. These additions related to the acquisition of Lourdes as described in Note A, and a surgical center, respectively.

Goodwill and other intangibles at December 31, 2019 and 2018, are as follows:

	<u>2019</u>	<u>2018</u>
Goodwill	\$ 34,063	\$ 21,922
Other intangibles:		
Certificate of need	18,200	-
Long-term care bed license	3,100	3,100
Trademark, net accumulated amortization of \$105	1,995	-
Other intangibles, net accumulated amortization of \$1,779	1,834	958
	<u>25,129</u>	<u>4,058</u>
	<u>\$ 59,192</u>	<u>\$ 25,980</u>

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Goodwill and other intangibles that are considered to have an indefinite useful life are not amortized but are tested for impairment at least annually and whenever events or circumstances change that indicate impairment may have occurred. Virtua Health first assesses qualitative factors to determine whether it is necessary to perform quantitative impairment tests for goodwill. If the result of the qualitative assessment conclude that it is more likely than not that goodwill is not impaired, a quantitative impairment test is not required. If a quantitative impairment test is required, Virtua Health's testing consists of performing an internal valuation analysis and considering other publicly available market information. If the carrying amount of goodwill exceeds the estimated fair value, an impairment charge to current operations is recorded to reduce the carrying value to the estimated fair value. Virtua Health completed the quantitative impairment test of its goodwill and other intangibles and determined there were no impairments for the years ended December 31, 2019 and 2018. Other intangibles that have a finite useful life have expected amortization expense of \$2,022 over the next five years.

Other Assets

Other assets at December 31, 2019 and 2018, are as follows:

	<u>2019</u>	<u>2018</u>
Advanced rental payments	\$ -	\$ 11,580
Insurance recoveries	17,654	12,014
Other	8,299	2,496
	<u>\$ 25,953</u>	<u>\$ 26,090</u>

Advance rental payments were being expensed over the term of the lease agreements, until the effective date of adoption of ASU No. 2016-02, *Leases*.

Beneficial Interest in Perpetual Trust

Virtua Health has recorded its portion of the fair value of a trust. The trust is perpetual in nature, and the original corpus cannot be violated. The trust is recorded as a net asset with donor restrictions.

Net Assets With Donor Restrictions

Net assets with donor restrictions represent those net assets whose use has been limited by donors to a specific time period, purpose, or to be maintained in perpetuity. The income from net assets that are to be maintained in perpetuity may be used to support nursing scholarships and to support various other needs, in accordance with donor stipulations. Income from net assets with donor restrictions is expended according to donor intent.

Virtua Health follows the requirements of the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"). Virtua Health's endowments consist of numerous individual funds established for a variety of purposes and consist solely of donor-restricted endowment funds. As required, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Virtua Health has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Virtua Health classifies net assets with donor restrictions related to endowment funds at the original value of gifts donated to the permanent endowment, the original value of subsequent gifts donated to the permanent endowment, and accumulations to the permanent endowment made in accordance with the directions of the applicable donor gift instruments.

Virtua Health's investment policies for its endowment assets are consistent with the policies and objectives of its overall investments. The assets are invested in a manner that is intended to produce a positive rate of return while assuming a low level of risk. From time to time, the fair value of assets associated with the donor-restricted endowment funds may fall below the level that the donor requires Virtua Health to maintain in perpetual duration.

Changes in donor restricted funds related to endowments for the years ended December 31, 2019 and 2018, are as follows:

	2019	2018
Endowment net assets - beginning of year	\$ 1,710	\$ 1,733
Investment return - net realized and unrealized gains (losses)	92	(23)
Endowment net assets - end of year	\$ 1,802	\$ 1,710

Patient Service Revenue

Virtua Health has negotiated agreements with third-party payers including health insurance companies and has rates set by government regulations (for payers such as Medicare and Medicaid) that provide for reimbursement at amounts different from established charges. Reimbursement methodologies include prospectively determined rates per discharge, per diem rates, reimbursed costs, and discounted charges.

Patient service revenues are recorded at the amounts that reflect the consideration to which Virtua Health expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payers (including managed care payers and government programs, i.e., Medicare and Medicaid) and others, and they include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews and investigations. Generally, patients and third-party payers are billed several days after the services are performed or shortly after discharge. Patient service revenue is recognized in the period in which the performance obligations are satisfied under contracts by transferring services to customers.

Performance obligations are determined based on the nature of the services provided. Virtua Health recognizes revenues for performance obligations satisfied over time based on actual charges incurred in relation to total expected charges. Virtua Health believes that this method provides an appropriate depiction of the transfer of services over the term of performance obligations based on the inputs needed to satisfy the obligations. Generally, performance obligations satisfied over time relate to patients receiving inpatient acute care services. Virtua Health measures performance obligations from admission to the point when there are no further services required for the patient, which is generally the time of discharge. Virtua Health recognizes revenues for performance obligations satisfied at a point in time, which generally relate to patients receiving outpatient services, when: (1) services are provided; and (2) when it is believed the patient does not require additional services.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Virtua Health determines estimates of contractual adjustments and discounts based on government regulations, contractual agreements, discount policies and historical experience, as applicable. Virtua Health determines its estimate of implicit price concessions based on historical collection experience within each class of patients using a portfolio approach to account for patient contracts as collective groups rather than individually.

Performance Indicator

The consolidated statements of operations and changes in net assets include, as the performance indicator, the excess of (deficit in) revenue over expenses. Transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as revenue and expenses. Changes in net assets without donor restrictions that are excluded from the excess of (deficit in) revenue over expenses include net assets released from restrictions for property, plant, and equipment, and other changes in accrued retirement benefits.

Advertising Costs

Virtua Health expenses advertising costs as incurred. For the years ended December 31, 2019 and 2018, Virtua Health incurred advertising costs of \$8,748 and \$5,994, respectively, which are included in other operating expenses in the accompanying consolidated statements of operations and changes in net assets.

Tax Status

Virtua Health, excluding HMSO, LMA, VAI, VPP, VRI, CS, Voorhees Endo Holding, SCA Holdings, Virtua-USP Princeton and Emmaus Holdings, 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. The not-for-profit affiliates of Virtua Health, except for VMG, are also exempt from state income taxes. Income taxes are not material to the consolidated financial statements.

NOTE C - ACQUISITION

On July 1, 2019, Virtua acquired the membership interest of Lourdes, as described in Note A. The acquisition includes substantially all of the healthcare operations and certain assets and working capital of Lourdes. Virtua Health accounted for this business combination by applying the acquisition method and, accordingly, the gain on bargain purchase was valued as the excess of assets acquired over liabilities assumed, less cash paid. In determining the gain on bargain purchase, all assets acquired and liabilities assumed were measured at fair value as of the Lourdes acquisition date. The results of the operations of Lourdes have been included in the accompanying consolidated financial statements since the acquisition date.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE C - ACQUISITION - CONTINUED

The estimated fair values of the Lourdes assets acquired and liabilities assumed at the Lourdes acquisition date are as follows:

Assets	
Patient accounts receivable	\$ 49,754
Other current assets	17,075
Property and equipment	139,081
Investments in unconsolidated joint ventures	5,900
Goodwill and other intangibles	33,648
Other assets	6,092
Right of use assets	<u>22,370</u>
Total assets acquired	<u>273,920</u>
Liabilities	
Accounts payable and accrued expenses	8,335
Accrued compensation and related liabilities	30,579
Lease liability	<u>22,370</u>
Total liabilities assumed	<u>61,284</u>
Excess of assets acquired over liabilities assumed	<u>\$ 212,636</u>
Net assets acquired	
Net assets without donor restrictions	\$ 204,710
Net assets with donor restrictions	912
Non-controlling interest	<u>7,014</u>
Excess of assets acquired over liabilities assumed	<u>212,636</u>
Net assets without donor restrictions	204,710
Cash paid, net for acquisition of Lourdes	<u>(30,457)</u>
Gain on acquisition of Lourdes	<u>\$ 174,253</u>

The following are the results of Lourdes from the date of acquisition that have been included in the consolidated statement of operations and changes in net assets for the year ended December 31, 2019:

Total revenues	\$ 257,278
Deficit of expenses over revenue and nonoperating gains (losses), net attributable to Lourdes	\$ (23,496)
Decrease in net assets without donor restrictions	\$ (23,496)
Decrease in net assets	\$ (14,921)

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE C - ACQUISITION - CONTINUED

The following are the unaudited proforma results for the years ended December 31, 2019 and 2018, respectively, as if the acquisition had occurred on January 1, 2018. The unaudited pro forma financial information excludes the gain on purchase of Lourdes and is not necessarily indicative of the results of operations as they would have been, had the transaction been effected on January 1, 2018:

	Unaudited Proforma	
	2019	2018
Total revenues	\$ 1,893,273	\$ 1,894,708
Excess of (deficit in) revenue and nonoperating gains (losses), net over expenses attributed to Virtua Health, Inc.	\$ 158,878	\$ (88,060)

NOTE D - LIQUIDITY AND AVAILABILITY OF RESOURCES

At December 31, 2019 and 2018, the adjusted working capital was \$1,212,668 and \$1,057,469 and the adjusted average days' cash on hand was 303 days and 317 days, respectively, both of which include the assets limited as to use by Board of Trustees' designation.

In addition to cash flows provided by operating activities, the financial assets available for general expenditure within one year of the consolidated balance sheet date consist of the following at December 31, 2019 and 2018:

	2019	2018
Cash	\$ 81,847	\$ 44,109
Patient accounts receivable	179,546	143,641
Assets limited as to use by Board of Trustees' designation	1,201,059	1,019,812
	1,462,452	1,207,562
Available line of credit	76,029	75,967
	\$ 1,538,481	\$ 1,283,529

NOTE E - CHARITY CARE AND STATE SUBSIDY

Virtua Health provides care to all in need of medical assistance. Many patients cared for at Virtua Health do not have health insurance or the ability to pay for the cost of their care. Virtua Health does not directly receive compensation for the operating expense incurred providing care to these patients. Uninsured patients may qualify for financial assistance under the provisions of two separate programs. Individuals with incomes up to 300% of the federal poverty guidelines, whose individual or family assets do not exceed \$7,500 and \$15,000, respectfully, can qualify for assistance under the New Jersey Hospital Care Payment Assistance Program ("NJHCPAP"). With the objective of increasing eligibility for financial assistance to a greater number of uninsured patients, Virtua Health established its own assistance program whose qualification criterion is less restrictive than the NJHCPAP, as there is no asset test and those with incomes up to 500% of the federal poverty guidelines are eligible. Patients qualifying for these programs receive services without charge or at amounts less than established charges. Virtua Health maintains records to identify and monitor the level of financial assistance provided under both programs. The records include the amount of patient service revenue categorized as charity care.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE E - CHARITY CARE AND STATE SUBSIDY - CONTINUED

Under a provision of the Affordable Care Act, the State of New Jersey opted to accept federal government funding to expand the eligibility for enrolling in the state's Medicaid program.

The cost of providing charity care, based on Virtua Health's estimated cost-to-charge ratios, for the years ended December 31, 2019 and 2018, is as follows:

	2019	2018
NJHCPAP	\$ 18,142	\$ 10,300
Virtua Health Program	8,201	8,001
	\$ 26,343	\$ 18,301

Virtua Health received \$2,528 and \$1,151 of State of New Jersey Charity Care Subsidy Funds for the years ended December 31, 2019 and 2018, respectively. These amounts are included in patient service revenue in the consolidated statements of operations and changes in net assets.

NOTE F - PATIENT SERVICE REVENUE

Patient service revenue recognized from major payer sources based on primary insurance designation for the years ended December 31, 2019 and 2018, is as follows:

	2019	2018
Managed care	65%	68%
Medicare and Medicaid (fee for service plans only)	25	25
Other third-party payers	8	5
Self-pay	2	2
	100%	100%

Inpatient acute care services for Medicare and Medicaid program beneficiaries and outpatient services for Medicare beneficiaries are paid at prospectively determined rates per discharge or outpatient service. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors.

Outpatient services for Medicaid beneficiaries, defined Medicare program pass-through items, and certain other costs provisionally reimbursed by Medicare, are paid based on a cost reimbursement methodology or tentative rate. These are ultimately subjected to certain cost limitations or contingent on actual data for the year, with final settlement determined after submission of annual cost reports by Virtua Health and audits thereof, by the programs' fiscal intermediaries.

The Centers for Medicare and Medicaid Services ("CMS") previously approved the State of New Jersey's proposal under Section 1115 of the Social Security Act to implement a mandatory Medicaid managed care program, which requires certain Medicaid beneficiaries to enroll in approved managed care plans. In addition, certain Medicare beneficiaries may opt for coverage through federally approved managed care plans. Payments to Virtua Health for these Medicaid and Medicare beneficiaries are based upon the rates negotiated with these plans.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE F - PATIENT SERVICE REVENUE - CONTINUED

The Medicare cost reports have been audited and finalized through December 31, 2016, except for those of Virtua-Memorial, which have not been finalized for December 31, 2011 and 2016. The Medicaid cost reports have been audited and finalized through December 31, 2016. Virtua Health also has outstanding appeal issues relating to prior-year settled cost reports. Differences between the estimated settlements and the amounts settled are recorded in the year of settlement. Estimated favorable results of appeal items are recorded when realization is reasonably assured. These estimates are included in estimated settlements due to third-party payers in the consolidated balance sheets. Management uses the expected-value method when determining these amounts. In the opinion of management, adequate provision has been made for any adjustment, which may result from the final settlement of these cost reports, and any appeal issues. For the years ended December 31, 2019 and 2018, patient service revenue includes net favorable settlements and adjustments for cost reports, audit and appeal items from prior years of \$3,916 and \$7,077, respectively.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation, and noncompliance could result in significant regulatory action, including fines and penalties. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Virtua Health believes that it is in compliance with applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquiries have been made, compliance with such laws and regulations can be subjected to future government review and interpretations as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medicaid programs. Virtua Health has a corporate compliance program to monitor compliance with these laws and regulations.

NOTE G - ASSETS LIMITED AS TO USE

Investments and assets limited as to use, stated at fair value as of December 31, 2019 and 2018, consist of the following:

	2019	2018
By Board of Trustees' designation:		
Mutual and private placement funds - fixed income	\$ 583,307	\$ 514,097
Mutual and private placement funds - equity	617,752	505,715
	\$ 1,201,059	\$ 1,019,812
Other designated funds:		
Mutual and private placement funds - fixed income	\$ 121,174	\$ 142,792
Mutual and private placement funds - equity	128,700	140,473
	249,874	283,265
Less assets limited as to use that are required for current liabilities	(16,255)	(9,943)
	\$ 233,619	\$ 273,322

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE G - ASSETS LIMITED AS TO USE - CONTINUED

	2019	2018
	<u> </u>	<u> </u>
Under debt agreements:		
Cash and short-term investments	\$ 8,386	\$ 27,504
U.S. government obligations	-	13,680
	<u>8,386</u>	<u>41,184</u>
Less assets limited as to use that are required for current liabilities	<u>(8,386)</u>	<u>(14,567)</u>
	<u>\$ -</u>	<u>\$ 26,617</u>
Under debt agreements, assets are maintained for the following purposes:		
Debt service reserve fund	\$ -	\$ 26,513
Debt service interest fund	2,941	9,620
Debt service principal fund	5,380	5,051
Debt service cost of issuance fund	65	-
	<u>\$ 8,386</u>	<u>\$ 41,184</u>
Trust funds:		
Cash and short-term investments	\$ 982	\$ 604
Mutual and private placement funds - fixed income	951	2,111
Mutual and private placement funds - equity	1,489	1,510
Split dollar investments	14,941	-
Investment contract	659	891
	<u>\$ 19,022</u>	<u>\$ 5,116</u>
Donor-restricted funds:		
Cash and short-term investments	\$ 1,094	\$ 81
Mutual and private placement funds - fixed income	8,313	6,920
Mutual and private placement funds - equity	8,764	7,074
	<u>\$ 18,171</u>	<u>\$ 14,075</u>

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE G - ASSETS LIMITED AS TO USE - CONTINUED

Investment income and realized and unrealized gains and losses, net of fees for assets limited as to use and cash equivalents for the years ended December 31, 2019 and 2018, are composed of the following:

	<u>2019</u>	<u>2018</u>
Other revenue - investment returns	<u>\$ 303</u>	<u>\$ 61</u>
Nonoperating gains (losses), net:		
Investment return:		
Interest and dividend income	\$ 504	\$ 197
Net realized gains and losses on sales of investments	80,713	26,020
Net change in unrealized gains and losses on trading securities	140,308	(88,735)
Investment management fees	<u>(5,046)</u>	<u>(5,109)</u>
	<u>\$ 216,479</u>	<u>\$ (67,627)</u>
Net assets with donor restrictions - net realized and unrealized loss	<u>\$ 393</u>	<u>\$ (108)</u>

NOTE H - FAIR VALUE MEASUREMENTS

Fair Value Measurements

Virtua Health classifies its investments into: Level 1, which refers to securities valued using quoted prices from active markets for identical assets; Level 2, which refers to securities not traded on an active market, but for which observable market inputs are readily available; and Level 3, which refers to securities valued based on significant unobservable inputs. Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

Asset Valuation Techniques

Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2019 and 2018.

Mutual Funds - Fair value estimates for publicly traded mutual funds are based on quoted market prices and/or other market data for the same or comparable instruments and transactions in establishing the prices. Such mutual funds are actively traded and are classified as Level 1.

U.S. Government Obligations - The fair value of the U.S. government obligations reported as Level 2 has been determined using quoted market prices for similar instruments.

Split dollar - Cash surrender value - The cash surrender value of the split dollar investment is the amount of assets available today if the policies were terminated. Per the insurance carrier, the surrender value is made up of the accumulation value minus any unpaid policy charges minus any indebtedness minus any surrender charges.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE H - FAIR VALUE MEASUREMENTS - CONTINUED

Investment Contract - The fair value of the investment contract is provided by the respective insurance company and is equal to the funds deposited by Virtua Health and accrued income. The investment contract is reported as Level 3.

Beneficial Interest in Perpetual Trust - The estimated fair value of the beneficial interest in perpetual trust is determined based upon information provided by the trustee. Such information is based on the pro rata interest in the net assets of the trust. The assets held in the trust consist primarily of cash equivalents and marketable securities. The fair value of the perpetual trust is measured using the fair value of the underlying investments and is reported as Level 3.

Private Placement Funds - The fair value of private placement funds has been determined using the net asset value ("NAV") of the funds as provided by the respective fund managers. The NAV is used as a practical expedient to estimate fair value and is excluded from the fair value hierarchy. The underlying investments of these funds consist of securities with readily determinable market values.

The valuation methods as described above may produce a fair value that may not be indicative of what management would realize upon disposition or reflective of future fair values. Furthermore, although management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

As of December 31, 2019 and 2018, there were no withdrawal restrictions or unfunded commitments on investments reported at NAV.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE H - FAIR VALUE MEASUREMENTS - CONTINUED

The information as of December 31, 2019 and 2018, about Virtua Health's financial assets that are measured at fair value on a recurring basis using the market approach, is as follows:

	December 31, 2019			
	Total	Level 1	Level 2	Level 3
Assets				
Cash and short-term investments	\$ 10,462	\$ 10,462	\$ -	\$ -
Mutual funds:				
U.S. equity	2,031	2,031	-	-
International equity	234	234	-	-
U.S. fixed income	1,389	1,389	-	-
International fixed income	90	90	-	-
Real estate	92	92	-	-
Split dollar - cash surrender value	14,941	-	14,941	-
Investment contract	659	-	-	659
Beneficial interest in perpetual trust	8,445	-	-	8,445
	<u>38,343</u>	<u>\$ 14,298</u>	<u>\$ 14,941</u>	<u>\$ 9,104</u>
Private placement funds (at NAV):				
Fixed income ^(a)	712,266			
Domestic equity ^(b)	413,314			
International equity ^(c)	341,034			
	<u>1,466,614</u>			
	<u>\$ 1,504,957</u>			

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE H - FAIR VALUE MEASUREMENTS - CONTINUED

	December 31, 2018			
	Total	Level 1	Level 2	Level 3
Assets				
Cash and short-term investments	\$ 28,189	\$ 28,189	\$ -	\$ -
Mutual funds:				
U.S. equity	2,307	2,307	-	-
International equity	441	441	-	-
U.S. fixed income	1,826	1,826	-	-
International fixed income	165	165	-	-
Real estate	105	105	-	-
U.S. government obligations	13,680	-	13,680	-
Investment contract	891	-	-	891
Beneficial interest in perpetual trust	7,459	-	-	7,459
	<u>55,063</u>	<u>\$ 33,033</u>	<u>\$ 13,680</u>	<u>\$ 8,350</u>
Private placement funds (at NAV):				
Fixed income ^(a)	663,328			
Domestic equity ^(b)	351,422			
International equity ^(c)	301,098			
	<u>1,315,848</u>			
	<u>\$ 1,370,911</u>			

(a) Fixed income - Seeks favorable returns comparable to the broad fixed-income market by investing in bonds representing diverse sectors and maturities.

(b) Domestic equity - Seeks to provide long-term capital growth, by investing in common stocks of U.S. companies with various capitalizations, while managing volatility and maintaining diversification.

(c) International equity - Seeks high, long-term returns comparable to the broad international stock market by investing in companies from developed and emerging countries around the world.

Transfers Between Levels

The availability of observable market data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported during the reporting period.

There were no transfers into or out of the levels per the tables above, for the years ended December 31, 2019 and 2018.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE H - FAIR VALUE MEASUREMENTS - CONTINUED

The table below sets forth the change in the fair value of investments measured using significant unobservable inputs (Level 3) for the years ended December 31, 2019 and 2018, as follows:

	Investment contract	Beneficial interest in perpetual trusts	Total
Balance - December 31, 2017	\$ 2,845	\$ 8,530	\$ 11,375
Net realized gains	141	-	141
Net unrealized losses	(116)	(1,071)	(1,187)
Purchases	172	-	172
Sales	(2,151)	-	(2,151)
Balance - December 31, 2018	891	7,459	8,350
Net realized gains	79	-	79
Net unrealized (losses) gains	(69)	986	917
Purchases	650	-	650
Sales	(892)	-	(892)
Balance - December 31, 2019	<u>\$ 659</u>	<u>\$ 8,445</u>	<u>\$ 9,104</u>

NOTE I - INVESTMENT IN UNCONSOLIDATED JOINT VENTURES

Virtua Health and physicians located throughout New Jersey have joined together, along with other non-related for-profit investors, to expand surgical and certain other services within the physicians' local communities through jointly owned ventures. These ventures are for-profit organizations. Virtua Health also has ownership in a medical revenue cycle joint venture that provides billing services to physician practices.

Specifically related to the Voorhees Endo Holding, SCA Holdings, Virtua-USP Princeton and Emmaus Holdings joint ventures ("Holding Companies"), Virtua Health consolidates these joint ventures. The operating agreements of the physician ventures that are within the Holding Companies do not allow Virtua Health or the Holding Companies to control operating or financial decisions related to the ventures. Regardless of the proportionate ownership of capital investment in these physician ventures, all decisions are made by the respective venture's operating board. In each case, the operating board is composed equally of members appointed by Virtua Health and the physician investors as a group. Accordingly, Virtua Health and the Holding Companies account for their interest in these physician ventures on the equity method of accounting.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE I - INVESTMENT IN UNCONSOLIDATED JOINT VENTURES - CONTINUED

The balances for these statements are as follows:

	Membership percentage		Investment in unconsolidated affiliates		Equity earnings in unconsolidated affiliates	
	December 31,		December 31,		Year ended December 31,	
	2019	2018	2019	2018	2019	2018
Virtua-Memorial:						
Memorial Ambulatory Surgery Center, LLC	59.77%	55.59%	\$ 662	\$ 547	\$ 781	\$ 616
Vantage Surgical Center, LLC	51.00%	51.00%	2,075	1,742	702	755
Burlington County Endoscopy Center, LLC	52.00%	52.00%	6,983	6,869	3,301	3,121
SCA Holdings:	51.00%	51.00%				
Seashore Surgical Institute, LLC ^(a)			7,240	7,273	1,589	1,770
Surgicare of Central Jersey, LLC ^(a)			14,750	14,568	2,696	1,966
Bergen-Passaic Eye Surgery Center ^(a)			6,159	5,620	2,903	2,537
Virtua-USP Princeton	68.20%	68.20%				
Surgical Specialist at Princeton, LLC ^(b)			10,587	10,594	3,743	2,913
Emmaus Holdings, LLC ^(c)	50.10%	50.10%				
Emmaus Surgical Center, LLC			7,289	7,086	1,305	176
Virtua-West Jersey:						
Summit Surgical, LLC	61.67%	62.30%	9,239	9,678	2,586	2,415
South Jersey Musculoskeletal Institute, LLC	53.90%	52.60%	2,005	1,530	4,053	3,735
Ambulatory Surgery Center at Virtua Washington Township, LLC	61.54%	62.06%	1,437	1,077	1,819	890
Jersey Shore, LLC	53.57%	51.26%	11,356	11,052	1,904	2,025
Ramapo Valley Surgical	51.00%	53.91%	9,144	9,321	1,339	1,375
Virtua Adult Imaging Services	50.00%	50.00%	5,457	5,091	3,190	2,454
Center for Ambulatory and Minimally Invasive Surgery, LLC	54.42%	55.11%	12,640	12,969	3,023	3,229
Freehold Endoscopy Associates, LLC	60.00%	60.00%	8,253	8,188	2,914	2,612
Gastro-Surgi Center of New Jersey, LLC	51.00%	51.00%	12,318	12,333	3,011	2,867
Fresenius Medical Care, LLC	30.00%	30.00%	636	951	(102)	74
Virtua Penn Radiation Oncology Leasing, LLC	50.00%	50.00%	9,788	6,730	3,058	489
Virtua Penn Radiation Oncology Partners, LLC	51.00%	51.00%	17,543	15,597	1,946	1,325
Mt. Laurel Endoscopy	51.00%	-	673	-	353	-
USTRC Gloucester LLC	29.00%	-	674	-	-	-
Voorhees Endo Holding:						
The Voorhees NJ Endoscopy ASC, LLC ^(d)	51.00%	51.00%	13,255	12,853	9,406	9,074
VRI:						
Acentus Practice Management, LLC	50.00%	50.00%	1,513	1,280	1,859	3,059
HMSO						
LTACH	20.00%	-	5,873	-	323	-
			<u>\$ 177,549</u>	<u>\$ 162,949</u>	<u>\$ 57,702</u>	<u>\$ 49,477</u>

(a) As of December 31, 2019, SCA Holdings owns 51.00% of Seashore Surgical Institute, LLC, 55.00% of Surgicare of Central Jersey, LLC, and 56.13% of Bergen-Passaic Eye Surgery Center. Virtua-Memorial holds a 51.00% membership percentage of SCA Holdings and effectively owns a 26.01% interest in Seashore Surgical Institute, LLC, a 28.05% interest in Surgicare of Central Jersey, LLC, and a 28.63% interest in Bergen-Passaic Eye Surgery Center. As of December 31, 2018, SCA Holdings owned 52.11% of Seashore Surgical Institute, LLC, 55.00% of Surgicare of Central Jersey, LLC, and 56.13% of Bergen-Passaic Eye Surgery Center. Virtua-Memorial held a 51.00% membership percentage of SCA Holdings and effectively owned a 26.58% interest in Seashore Surgical Institute, LLC, a 28.05% interest in Surgicare of Central Jersey, LLC, and a 28.63% interest in Bergen-Passaic Eye Surgery Center.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE I - INVESTMENT IN UNCONSOLIDATED JOINT VENTURES - CONTINUED

- (b) Virtua-USP Princeton owns 56.85% of Surgical Specialists at Princeton, LLC as of December 31, 2019 and owned 55.00% as of December 31, 2018. Virtua-Memorial holds a 68.2% membership percentage of Virtua-USP Princeton and thus effectively owns a 38.77% interest in Surgical Specialists at Princeton, LLC at December 31, 2019 and effectively owned 37.51% at December 31, 2018.
- (c) Emmaus Holdings, LLC owns 50.10% of the Emmaus Surgical Center, LLC as of December 31, 2018. Virtua-Memorial holds a 50.10% membership percentage in Emmaus Holdings and thus effectively owned a 25.10% interest in the Emmaus Surgical Center, LLC.
- (d) Voorhees Endo Holding owns 51% of The Voorhees NJ Endoscopy ASC, LLC as of December 31, 2019 and 2018. Virtua-West Jersey holds a 51% membership percentage in The Voorhees Endo Holding and thus effectively owns a 26% interest in the Voorhees NJ Endoscopy ASC, LLC.

Operating revenues for the combined group of ventures accounted for under the equity method of accounting were \$286,924 and \$239,859 for the years ended December 31, 2019 and 2018, respectively.

Virtua Health provides employee leasing, rental, and management services to several of its joint ventures. The total revenue, included in other revenue, from these services was \$18,190 and \$15,764 for the years ended December 31, 2019 and 2018, respectively. The total amounts receivable, included in other current assets, related to these services are \$3,173 and \$2,289 at December 31, 2019 and 2018, respectively.

NOTE J - PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment at December 31, 2019 and 2018, consisted of the following:

	2019	2018
Land	\$ 112,599	\$ 94,249
Land improvements	78,330	69,104
Buildings and improvements	809,102	682,799
Fixed equipment	252,110	250,099
Furniture and equipment	850,630	778,375
	2,102,771	1,874,626
Less accumulated depreciation and amortization	(1,153,870)	(1,048,003)
	948,901	826,623
Construction in progress	78,406	57,309
	\$ 1,027,307	\$ 883,932

Depreciation and amortization expense related to property, plant, and equipment was \$106,697 and \$95,583 for the years ended December 31, 2019 and 2018, respectively.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE K - LONG-TERM DEBT

Long-term debt at December 31, 2019 and 2018, consisted of the following:

	<u>2019</u>	<u>2018</u>
New Jersey Health Care Facilities Financing Authority (“NJHCFFA”):		
\$60,000 Virtua Health Issue, Series 2004 Variable Rate Revenue Bonds - less issuance cost of \$223 and \$248 at December 31, 2019 and 2018, respectively ^(a)	\$ 46,717	\$ 48,477
\$379,645 Virtua Health Issue, Series 2009A Fixed Rate Revenue Bonds - less net original issue discount and issuance cost of \$5,668 at December 31, 2018 ^(b)	-	224,447
\$185,000 Virtua Health Issue, Series 2009B-E Variable Rate Revenue Bonds - less issuance cost of \$1,341 and \$1,403 at December 31, 2019 and 2018, respectively ^(c)	183,659	183,597
\$140,020 Virtua Health Issue, Series 2013 Fixed Rate Revenue and Refunding Bonds - plus net original issue premium and issuance cost of \$4,812 and \$5,648 at December 31, 2019 and 2018, respectively ^(d)	126,547	137,378
\$205,435 Virtua Health Issue, Series 2019 Fixed Rate Refunding Bonds - less issuance cost of \$637 at December 31, 2019 ^(e)	204,798	-
Finance lease obligations, with various interest rates, secured by lease equipment	<u>1,218</u>	<u>-</u>
	562,939	593,899
Less current maturities of long-term debt	<u>(12,787)</u>	<u>(11,780)</u>
	<u>\$ 550,152</u>	<u>\$ 582,119</u>

(a) The NJHCFFA Variable Rate Revenue Bonds, Virtua Health Issue, Series 2004 (the “Series 2004 Bonds”) were issued for the purpose of refinancing the 2001 Capital Asset Program loan and funding and reimbursing costs of various capital improvements and equipment purchases by Virtua-Memorial and Virtua-West Jersey. Annual principal payments range from \$1,860 to \$6,385, maturing on July 1 of each year through 2033. Interest is payable monthly at a variable rate not to exceed 10%. The interest rate was 1.18% and 1.64% at December 31, 2019 and 2018, respectively. The Series 2004 Bonds are variable rate demand bonds secured by an irrevocable letter of credit with a bank, which expires on May 31, 2021. No amounts were outstanding on the letter of credit at December 31, 2019 and 2018.

(b) The NJHCFFA Fixed Rate Revenue Bonds, Virtua Health Issue, Series 2009A (the “Series 2009A Bonds”) bear interest between 5.50% and 5.75%, payable on January 1 and July 1. The outstanding bonds were refunded on April 4, 2019 through the issue of the Series 2019 refunding bonds. Bond proceeds were used for constructing and equipping the Voorhees replacement hospital, funding capitalized interest, funding a Debt Service Reserve Fund, and paying certain finance costs.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE K - LONG-TERM DEBT - CONTINUED

- (c) NJHCFFA Variable Rate Revenue Bonds, Virtua Health Issue, Series 2009B-E (the "Series 2009B-E Bonds") were issued in connection with the Series 2009A Bonds for the purpose of constructing and equipping the Voorhees replacement hospital, funding capitalized interest, and paying certain finance costs. Annual principal payments range from \$34,820 to \$39,245, mature beginning on July 1, 2039 annually through 2043. Interest is payable monthly at a variable rate not to exceed 12%. The interest rates were 1.30%, 1.35%, 1.03%, and 1.03% at December 31, 2019 and 1.28%, 1.25%, 1.65%, and 1.60% at December 31, 2018, respectively. The Series 2009B-E Bonds are variable rate demand bonds secured by irrevocable letters of credit with two banks; with one bank for Series B-C providing two letters of credit for a total of \$100,000, which expire on January 2, 2023; and another bank for Series D-E providing two letters of credit for a total of \$85,000, which expire on January 2, 2021. No amounts were outstanding on the letters of credit at December 31, 2019 and 2018.
- (d) The NJHCFFA Fixed Rate and Revenue Refunding Bonds, Virtua Health Issue, Series 2013 (the "Series 2013 Bonds") were issued to refund the outstanding Series 1998 Bonds and certain Series 2009A Bonds and pay for costs of issuance of the Series 2013 Bonds. The Series 2013 Bonds bear interest between 3.00% and 5.00%, payable on January 1 and July 1. Annual principal payments range from \$4,975 to \$15,515, maturing on July 1 of each year through 2029.
- (e) The NJHCFFA Fixed Rate and Refunding Bonds, Virtua Health Issue, Series 2019 (the "Series 2019 Bonds") were issued to refund the outstanding Series 2009A Bonds. Interest is payable monthly at a rate of 3.20%. Principal payments range from \$5,630 to \$27,880 maturing on July 1, 2020 and then annually beginning in 2030 through 2038. The bonds were issued as a private placement at a fixed rate with a bank as the direct purchasing bank.

Original issue discounts/premiums and debt issuance costs for indebtedness are being amortized over the term of the related debt using the effective interest method.

Under the terms of its bond trust agreements, Virtua Health has the option to convert the variable rate demand bonds to a fixed rate term mode. For all series of variable rate demand bonds backed by bank letters of credit and subjected to remarketing agreements, in the event that any or all of the bonds are tendered by the bondholder and are unable to be remarketed, the letters of credit are drawn upon by the bond trustee to purchase the unremarketed bonds. Draws for this purpose under the letters of credit are repaid with interest over a period of one to three years under existing term-out provisions, noting certain bonds have a one-year interest-only period prior to the repayment period. All series of variable rate demand bonds are subjected to mandatory tender for purchase prior to the expiration of the letter of credit if a substitute facility has not been made effective. The Series 2009 B-C Bonds have a three-year loan provision for converting a letter of credit draw for the purchase of bonds in connection with the letter of credit expiration.

The Series 2004, 2009B-E, 2013 and 2019 Bonds are all secured equally and ratably on a parity basis by notes issued under the master trust indenture (the "Master Trust Indenture"), with Virtua Health, Inc., Virtua-West Jersey, and Virtua-Memorial as obligated issuers (the "Virtua Obligated Group"). The notes are secured by a pledge of gross receipts of the Virtua Obligated Group and a mortgage on the Voorhees replacement hospital. The Virtua Obligated Group is obligated to pay the principal or redemption price and interest on the bonds under loan agreements with the NJHCFFA. The Master Trust Indenture and other bond agreements require the Virtua Obligated Group to comply with certain financial covenants. At December 31, 2019 and 2018, the Virtua Obligated Group has complied with all financial covenants related to the bonds.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE K - LONG-TERM DEBT - CONTINUED

Future Principal Payments

Principal payments on long-term debt for the next five years and thereafter are as follows:

Years ending December 31,	
2020	\$ 12,787
2021	13,188
2022	13,599
2023	14,115
2024	14,694
Thereafter	<u>491,945</u>
	<u>\$ 560,328</u>

Lines and Letters of Credit

Virtua Health has a revolving credit line in place with a bank for \$30,000, with the interest rate based on the lower of the London Inter Bank Offered Rate ("LIBOR") plus 65 basis points (the one-month LIBOR was 1.76% and 2.52% at December 31, 2019 and 2018, respectively), or the bank's prime rate minus 150 basis points (the prime rate was 4.75% and 5.50% at December 31, 2019 and 2018, respectively), which expires on December 31, 2020. There were no amounts outstanding under the line of credit at December 31, 2019 and 2018. The line of credit has a provision for letters of credit. There was \$3,971 in letters of credit commitments at December 31, 2019, which was not drawn upon, with expiration dates in 2020 in connection with Virtua Health's insurance captive, a capital project and a site requirement.

Virtua Health has bank agreements for two additional lines of credit of \$25,000 for each line with expiration dates in December 2020 and January 2021. The interest rate for one line is based on the lower of LIBOR, plus 65 basis points, or the prime rate minus 150 basis points, with the rate on the other line at lower of LIBOR, plus 55 basis points, or the prime rate minus 150 basis points. There were no amounts outstanding on the lines of credit at December 31, 2019 and 2018.

Fair Value

Virtua Health uses current quoted market prices in estimating the fair value of its revenue bonds. The fair value of long-term debt at December 31, 2019 and 2018 is \$607,206 and \$613,174, respectively. Fair value of long-term debt was determined using the market approach, which is considered a Level 2 measurement.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE L - LEASES

The following table presents the components of Virtua Health's right of use assets and liabilities related to leases and their classification as of December 31, 2019:

<u>Component of lease balances</u>	<u>Classification in consolidated balance sheet</u>	<u>2019</u>
Assets		
Operating lease assets	Right of use assets	\$ 139,768
Finance lease assets	Net property, plant, and equipment	<u>1,218</u>
Total leased assets		<u>\$ 140,986</u>
Liabilities		
Operating lease liabilities		
Current	Current maturities of lease liability	\$ 31,040
Long-term	Lease liability, net of current maturities	<u>110,338</u>
Total operating lease liabilities		<u>141,378</u>
Finance lease liabilities		
Current	Current maturities of long-term debt	322
Long-term	Long-term debt, net of current maturities	<u>896</u>
Total finance lease liabilities		<u>1,218</u>
Total lease liabilities		<u>\$ 142,596</u>

The following table presents the components of lease expense and their classification in the consolidated statement of operations and changes in net assets for the year ended December 31, 2019:

<u>Component of lease balances</u>	<u>Classification in consolidated statement of operations and changes in net assets</u>	<u>2019</u>
Operating lease expense	Other operating expenses	\$ 40,218
Finance lease expense:		
Amortization of leased assets	Depreciation and amortization	131
Interest on lease liabilities	Interest expense	<u>15</u>
Total finance lease expense		146
Variable and short-term lease expense	Other operating expenses	<u>20,490</u>
Total lease expense		<u>\$ 60,854</u>

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE L - LEASES - CONTINUED

The weighted-average lease terms and discount rates for operating and finance leases at December 31, 2019 is as follows:

	<u>2019</u>
Weighted-average remaining lease term (years)	
Operating leases	4.95 years
Finance leases	4.00 years
Weighted-average discount rate	
Operating leases	3.20%
Finance leases	3.43%

Cash flow related to leases for the year ended December 31, 2019 is as follows:

	<u>2019</u>
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash outflows from operating leases	\$ 31,080
Operating cash outflows from finance leases	\$ 131
Financing cash outflows from finance leases	\$ 15
Right-of-use assets obtained in exchange for lease obligations:	
Operating leases	\$ 15,037
Finance leases	\$ 1,349

The future minimum rental commitments for all noncancelable operating and finance leases as of December 31, 2019 are as follows:

	<u>Operating leases</u>	<u>Finance leases</u>	<u>Total</u>
Years ending December 31,			
2020	\$ 35,749	\$ 358	\$ 36,107
2021	31,939	358	32,297
2022	23,532	259	23,791
2023	15,482	187	15,669
2024	13,712	141	13,853
Thereafter	38,653	-	38,653
Total lease payments	<u>159,067</u>	<u>1,303</u>	<u>160,370</u>
Less: Imputed interest	<u>(17,689)</u>	<u>(85)</u>	<u>(17,774)</u>
	141,378	1,218	142,596
Less: Current maturities	<u>(31,040)</u>	<u>(322)</u>	<u>(31,362)</u>
Lease liability, net of current maturities	<u>\$ 110,338</u>	<u>\$ 896</u>	<u>\$ 111,234</u>

Prior to the adoptions of ASU 2016-02, *Leases*, rent expense for operating lease agreements for the year ended December 31, 2018 totaled \$57,748.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE M - RETIREMENT BENEFIT PLANS

Defined Contribution Plans

Virtua Health sponsors the Virtua Health 401(k) savings plan covering all nonbargaining unit employees and a group of bargaining unit employees. Employer contributions to the Virtua Health 401(k) savings plan are based on a formula as defined by the plan document.

Virtua Health also has a supplemental executive retirement plan ("SERP") that covers a group of management designated by the Board of Trustees. The contributions to the plan are determined annually. The accrued benefit amount of this SERP as of December 31, 2019 and 2018, was \$2,902 and \$5,368, respectively, and is recorded in accrued retirement benefits in the consolidated balance sheets. This plan was terminated in 2019. Virtua Health received a \$814 refund for un-vested contributions. The accrued benefit amount for 2019 will be distributed to the vested participants in June 2020.

The amount of expense related to these two plans was \$18,670 and \$16,304 for the years ended December 31, 2019 and 2018, respectively, and is included in employees' fringe benefits in the consolidated statements of operations and changes in net assets.

Beginning in 2019, Virtua Health and key executives entered into jointly owned split dollar agreements through an insurance company. Total funding as of December 31, 2019 was \$17,525, which is recorded in assets limited as to use - trust funds within the consolidated balance sheet. The value held by the insurance company along with additional security on the policy is collateral held to secure the return on Virtua Health's funding plus interest. The agreements allow for the key executives to borrow specified amounts to be repaid by the proceeds of the life insurance policies. Any remaining death proceeds are distributed to the executive's beneficiary as agreed upon by the parties.

Defined Benefit Plan

Virtua Health has a noncontributory defined benefit pension plan (the "Virtua Pension Equity Plan"), which 1) covered employees as defined, 2) accrued benefit formulas as defined, and 3) who met prescribed eligibility requirements. Effective December 31, 2019, the Virtua Pension Equity Plan froze benefits for all remaining non-union employees who were still accruing a benefit. This freeze was treated as a curtailment event. The Virtua Pension Equity Plan uses a measurement date of December 31. The mortality table used for projecting the benefit obligations is the Pri-2012 for the year ended December 31, 2019, and the RP-2014 for the year ended December 31, 2018.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE M - RETIREMENT BENEFIT PLANS - CONTINUED

The information at December 31, 2019 and 2018, and for the years then ended, about the Virtua Pension Equity Plan is as follows:

	<u>2019</u>	<u>2018</u>
Weighted-average assumptions used to determine benefit obligations - end of year:		
Discount rate	3.40%	4.26%
Rate of compensation increase	3.00%	3.00%
Accumulated benefit obligation - end of year	<u>\$ 253,418</u>	<u>\$ 241,556</u>
Changes in benefit obligations:		
Benefit obligations - beginning of year	\$ 241,571	\$ 268,432
Service cost	1,425	1,132
Interest cost	10,040	9,690
Actuarial gain (loss)	20,339	(17,065)
Benefits paid	(19,949)	(21,353)
Special termination benefits	-	735
Curtailments	(8)	-
Benefit obligations - end of year	253,418	241,571
Changes in plan assets:		
Fair value of plan assets - beginning of year	219,277	250,722
Actual return on plan assets	34,265	(10,092)
Employer contribution	-	-
Benefits paid	(19,949)	(21,353)
Fair value of plan assets - end of year	<u>233,593</u>	<u>219,277</u>
Funded status of the plan - end of year	<u>\$ (19,825)</u>	<u>\$ (22,294)</u>
Amounts recognized in the consolidated balance sheets - noncurrent accrued retirement benefits	<u>\$ (19,825)</u>	<u>\$ (22,294)</u>
Amounts recognized in net assets without restrictions:		
Actuarial loss	\$ 116,954	\$ 122,217
Prior service cost	64	258
Total amounts recognized in net assets without restrictions	<u>\$ 117,018</u>	<u>\$ 122,475</u>

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE M - RETIREMENT BENEFIT PLANS - CONTINUED

	2019	2018
Components of net periodic benefit cost recognized in employee fringe benefits:		
Service cost	\$ 1,425	\$ 1,132
Components recognized in nonoperating gains and losses in other accrual retirement costs:		
Interest cost	10,040	9,690
Expected return on plan assets	(13,042)	(14,946)
Amortization of actuarial loss	4,372	3,852
Amortization of prior service credit	11	11
Curtailment loss	182	-
Special termination benefits	-	735
	1,563	(658)
Total net periodic benefit cost	2,988	474
Other changes in accrued retirement benefits recognized in net assets without restrictions:		
Current-year actuarial loss	(892)	7,974
Recognized actuarial loss	(4,372)	(3,852)
Recognition of prior service cost	(193)	(11)
	(5,457)	4,111
Total recognized in net assets without restrictions	(5,457)	4,111
Total recognized in net periodic benefit cost and change in net assets without restrictions	\$ (2,469)	\$ 4,585
Weighted-average assumptions used to determine net periodic benefit cost:		
Discount rate	4.26%	3.74%
Expected long-term rate of return on plan assets	6.20%	6.20%
Rate of compensation increase	3.00%	3.00%

To develop the expected long-term rate of return on assets assumption, Virtua Health considered the historical returns and the future expectations for returns for each asset class, as well as the target allocation of the pension portfolio. This resulted in the selection of the 6.20% expected return on plan assets for 2019 and 2018, respectively.

The Virtua Pension Equity Plan amortizes prior service cost as a result of plan amendments on a straight-line basis over the expected average future lifetime of active participants expected to benefit under the plan. Plan amendments for the prior West Jersey Health System Retirement Plan were amortized on a decreasing-amount basis, based on the expected future service of active participants as of the date first recognized in each future year.

The estimated net actuarial loss and prior service benefit that is expected to be amortized from net assets without restrictions into net periodic pension cost for the year ending December 31, 2020 is \$4,207 and \$3, respectively.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE M - RETIREMENT BENEFIT PLANS - CONTINUED

Plan Assets

The pension plan's actual weighted-average asset allocations and target asset allocations, by asset category as of December 31, 2019 and 2018, are as follows:

Asset Category	Target Allocation	2019	2018
Fixed income	30% - 80%	69%	69%
Equity securities	20% - 65%	27	27
Alternative investments/real estate	0% - 10%	4	4
		100%	100%

The investment policy and strategy for the pension plan assets has established guidelines for an asset mix that provides diversification to absorb risk while not sacrificing investment returns.

The fair value of the common/collective trust funds has been determined using the NAV of the funds as provided by the respective fund managers. There were no withdrawal restrictions or unfunded commitments on such funds.

The plan assets in the defined benefit pension plan measured at fair value, using NAV, at December 31, 2019 and 2018, are as follows:

	2019	2018
Common/collective trust funds:		
Fixed income ^(a)	\$ 160,427	\$ 150,271
Domestic equity ^(b)	36,958	35,290
International equity ^(c)	26,098	24,065
U.S. real estate ^(d)	10,110	9,651
	\$ 233,593	\$ 219,277

(a) Fixed income - Seeks favorable returns comparable to the broad fixed-income market by investing in bonds representing diverse sectors and maturities.

(b) Domestic equity - Seeks to provide a long-term capital growth, by investing primarily in common stocks of U.S. companies with various capitalizations, while managing volatility and maintaining diversification.

(c) International equity - Seeks long-term returns comparable to the broad international stock market by investing in companies from developed and emerging countries around the world.

(d) U.S. real estate - Employs a multiadvisor, multifund approach to private core and enhanced core real estate investments with a focus on high current income. Manages risk through property type and regional diversification and generally limits portfolio leverage to 30%.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE M - RETIREMENT BENEFIT PLANS - CONTINUED

Cash Flows

Contributions

Virtua Health intends to make contributions to the plan assets, as necessary, that will ensure compliance with all provisions of the Pension Protection Act of 2006, as amended ("PPA").

Estimated future benefit payments:		
2020	\$	17,370
2021		17,976
2022		18,199
2023		18,093
2024		17,255
2025-2029		81,453

Multi-employer Plan

Certain Virtua Health employees represented by a bargaining unit participate in a multi-employer pension plan based on a union-negotiated agreement. For these employees, Virtua Health contributes to the Central Pension Fund of the International Union of Operating Engineers and Participating Employers (the "Multi-employer Plan"). Participation in the Multi-employer Plan commences on the first of the month after the employee's successful completion of 90 days of employment. Contributions to the Multi-employer Plan are based on union employee worked hours and a negotiated contribution rate in accordance with the union's contractual arrangement.

Under the Employee Retirement Income Security Act of 1974, as amended by the Multi-employer Pension Plan Amendments Act of 1980, the risks of participating in multi-employer plans are different from single-employer plans in the following respects:

- Assets contributed to the multi-employer plan by one employer may be used to provide benefits to employees of other participating employers.
- If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be borne by the remaining participating employers.
- If the employer chooses to stop participating in some of its multi-employer plans, the employer may be required to pay those plans an amount based on the underfunded status of the plan, referred to as a withdrawal liability.

Until such events above occur, Virtua Health's share, if any, of the unfunded vested liabilities cannot be determined. As of December 31, 2019, Virtua Health has no plans to withdraw from the Multi-employer Plan.

Virtua Health's participation in the Multi-employer Plan for the years ended December 31, 2019 and 2018, is outlined below:

- The Multi-employer Plan's Employer Identification Number is 36-6052390, and the three-digit plan number is 001.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE M - RETIREMENT BENEFIT PLANS - CONTINUED

- The PPA zone status is based on information that Virtua Health received from the Multi-employer Plan's sponsor and is certified by the Multi-employer Plan's actuary. The Multi-employer Plan is in the green zone, which indicates that it is at least 80% funded. The most recent PPA zone status available in 2019 and 2018 is for the Multi-employer Plan years ended January 31, 2019 and 2018, respectively.
- A financial improvement plan or a rehabilitation plan is neither pending nor has one been implemented for the Multi-employer Plan.
- Virtua Health was not required to pay a surcharge to the Multi-employer Plan.
- On March 15, 2018, the bargaining unit members voted to ratify a new three-year collective bargaining agreement to which the Multi-employer Plan is subjected. The contract expires on February 28, 2021.
- Virtua Health contributed \$4,245 and \$4,272 to the Multi-employer Plan for the years ended December 31, 2019 and 2018, respectively. Virtua Health did not contribute more than 5% of the total contributions to the Multi-employer Plan and was not listed in the Form 5500 for the Multi-employer Plan years ended January 31, 2019 and 2018.

At the date the consolidated financial statements were issued, the Form 5500 was not available for the Multi-employer Plan year ended January 31, 2019.

NOTE N - CONTINGENCIES AND COMMITMENTS

Self-Insured Malpractice and General Liability and Litigation

Virtua Health's captive insurance company, VAI, commenced business principally to reinsure the primary layer of exposure underwritten by a third-party insurer for claims-made-basis hospital professional liability, physicians professional liability, and occurrence-basis general liability. For the years ended December 31, 2019 and 2018, malpractice professional liability coverage is limited to \$1,000 per claim and \$3,000 aggregate per facility, and general liability coverage is limited to \$1,000 per claim. In addition to the primary layer by VAI, Virtua Health maintains excess coverage from third-party insurers for amounts above the limits insured by VAI.

The reserves for reported claims and claims incurred but not reported ("IBNR") are reported gross of expected insurance recoveries. The reserves for reported claims and claims IBNR are reported within accounts payable and accrued expenses and self-insurance liabilities in the consolidated balance sheets. In addition, the expected insurance recoveries are reported in other current assets and other assets in the consolidated balance sheets.

The loss reserves are management's best estimate based on actuarial estimates of the ultimate net cost of settling losses on incurred claims. The estimates are reviewed and adjusted, as necessary, as experience develops or new information becomes known. Management believes that the loss reserves are adequate; however, the ultimate settlement of losses may vary significantly from the amounts recorded in the accompanying consolidated financial statements.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE N - CONTINGENCIES AND COMMITMENTS - CONTINUED

Claims reserve activity for the years ended December 31, 2019 and 2018 is as follows:

	<u>2019</u>	<u>2018</u>
Claims reserves and IBNR - beginning of the year	\$ 48,369	\$ 34,168
Less: Insurance recoveries on unpaid claims	<u>(15,314)</u>	<u>(8,181)</u>
Claims reserves and IBNR, net - beginning of the year	33,055	25,987
Incurred related to:		
Current year	9,354	8,260
Prior year	298	3,093
Total incurred	<u>9,652</u>	<u>11,353</u>
Change in IBNR	5,778	680
Paid related to:		
Current year	(124)	(209)
Prior year	<u>(4,127)</u>	<u>(4,756)</u>
Total incurred	<u>(4,251)</u>	<u>(4,965)</u>
Claims reserves and IBNR, net - end of the year	44,234	33,055
Add: Insurance recoveries on unpaid claims	<u>24,379</u>	<u>15,314</u>
Claims reserves and IBNR - end of the year	<u>\$ 68,613</u>	<u>\$ 48,369</u>

Virtua Health is not a party to, nor are any of its properties the subject of, any material pending legal proceedings other than ordinary, routine litigation incidental to the business.

Self-Funded Healthcare Plan for Employees

Virtua Health has a self-funded healthcare employee benefit plan that is administered by a third-party administrator. Virtua Health obtains an excess insurance policy for claims to a member in excess of \$1,000. The reserves for claims that are not paid at December 31, 2019 and 2018 totaled \$8,192 and \$6,051, respectively, and are reported within accounts payable and accrued expenses in the consolidated balance sheets.

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE O - NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions at December 31, 2019 and 2018, are restricted for the following programs:

	<u>2019</u>	<u>2018</u>
Temporarily - Subject to expenditure for specific purpose:		
Property, plant, and equipment and other	\$ 18,080	\$ 16,058
Education and nursing scholarships	3,134	1,712
	<u>21,214</u>	<u>17,770</u>
Permanently - Investment in perpetuity whose income is expendable to support:		
Scholarships and other	<u>8,445</u>	<u>7,459</u>
	<u>\$ 29,659</u>	<u>\$ 25,229</u>

NOTE P - CONCENTRATIONS OF CREDIT RISK

Virtua Health grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer agreements. The mix of accounts receivable from patients and third-party payers at December 31, 2019 and 2018, is as follows:

	<u>2019</u>	<u>2018</u>
Managed care	28%	31%
Medicare and Medicaid	37	37
Self-pay	12	14
Other third-party payers	<u>23</u>	<u>18</u>
	<u>100%</u>	<u>100%</u>

Virtua Health, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

December 31, 2019 and 2018

(Dollars in thousands)

NOTE Q - FUNCTIONAL EXPENSES

Virtua Health’s primary mission is to provide health care services to its patients. The majority of all operating expenses incurred by Virtua Health are related to the provision of health care services. Virtua Health provides general health care services to residents within its geographic location. Expenses related to providing these services for the years ended December 31, 2019 and 2018, are as follows:

	Healthcare Services	General and Administrative	Total
<u>2019</u>			
Salaries and wages	\$ 626,312	\$ 126,958	\$ 753,270
Professional fees	24,290	5,288	29,578
Employers’ fringe benefits	133,364	35,916	169,280
Other operating expenses	497,289	76,769	574,058
Interest	17,800	5	17,805
Depreciation and amortization	85,463	21,234	106,697
	<u>\$ 1,384,518</u>	<u>\$ 266,170</u>	<u>\$ 1,650,688</u>
	Healthcare Services	General and Administrative	Total
<u>2018</u>			
Salaries and wages	\$ 497,739	\$ 101,422	\$ 599,161
Professional fees	18,317	1,513	19,830
Employers’ fringe benefits	107,057	27,964	135,021
Other operating expenses	396,357	51,798	448,155
Interest	21,287	4	21,291
Depreciation and amortization	76,526	19,057	95,583
	<u>\$ 1,117,283</u>	<u>\$ 201,758</u>	<u>\$ 1,319,041</u>

NOTE R - SUBSEQUENT EVENTS

Virtua Health has evaluated its December 31, 2019 consolidated financial statements for subsequent events through May 15, 2020, the date the consolidated financial statements were issued. Virtua Health is not aware of any subsequent events, which require recognition or disclosure in the consolidated financial statements, except as follows:

In March 2020, the World Health Organization declared COVID-19, the disease caused by the novel coronavirus, a pandemic, which continues to spread throughout the United States. The spread of COVID-19 has caused significant global financial market volatility. Management is closely monitoring the financial implications to Virtua Health. Due to the significant uncertainties around the disruptions related to COVID-19, as well as its impact on global economies and Virtua Health specifically, it is not determinable as to whether there will ultimately be a material impact on Virtua Health’s financial position or its operations. This uncertainty is due in part to not knowing what the full impact of financial assistance provided under the Coronavirus Aid, Relief and Economic Security Act (“CARES Act”), or any other legislative actions or programs, will be.

SUPPLEMENTARY INFORMATION

Virtua Health, Inc.

COMBINING BALANCE SHEET INFORMATION - VIRTUA OBLIGATED GROUP

December 31, 2019

ASSETS	Virtua Obligated Group	Reclassifying/ Eliminating Entries	Total	Virtua Health, Inc.	Virtua-Memorial Hospital of Burlington County	Virtua- West Jersey Health System
CURRENT ASSETS:						
Cash and cash equivalents	\$ 65,486	\$ -	\$ 65,486	\$ 414	\$ 9,404	\$ 55,668
Assets limited as to use	8,386	(7,891)	16,277	8,386	570	7,321
Patient accounts receivable	114,564	-	114,564	-	37,101	77,463
Due from affiliates, net	223,104	(17,658)	240,762	34,781	-	205,981
Other current assets	42,123	-	42,123	26,083	5,294	10,746
Total current assets	<u>453,663</u>	<u>(25,549)</u>	<u>479,212</u>	<u>69,664</u>	<u>52,369</u>	<u>357,179</u>
ASSETS LIMITED AS TO USE:						
By Board of Trustees' designation	1,137,828	-	1,137,828	14,164	139,263	984,401
Other designated funds	212,701	-	212,701	-	-	212,701
Trust funds	19,022	-	19,022	18,817	205	-
Donor-restricted funds	1,169	-	1,169	-	1,169	-
	<u>1,370,720</u>	<u>-</u>	<u>1,370,720</u>	<u>32,981</u>	<u>140,637</u>	<u>1,197,102</u>
PROPERTY, PLANT, AND EQUIPMENT, NET	803,397	-	803,397	-	148,500	654,897
OTHER LONG-TERM ASSETS:						
Due from affiliates, net	56,083	(795,260)	851,343	469,888	381,455	-
Investment in unconsolidated joint ventures	170,163	(5,511)	175,674	5,511	55,745	114,418
Goodwill and other intangibles	22,108	-	22,108	-	14,699	7,409
Other assets	17,937	-	17,937	17,655	236	46
Beneficial interest in perpetual trust	8,445	-	8,445	-	8,445	-
Right of use assets	69,427	-	69,427	21,523	20,725	27,179
	<u>344,163</u>	<u>(800,771)</u>	<u>1,144,934</u>	<u>514,577</u>	<u>481,305</u>	<u>149,052</u>
TOTAL ASSETS	<u>\$ 2,971,943</u>	<u>\$ (826,320)</u>	<u>\$ 3,798,263</u>	<u>\$ 617,222</u>	<u>\$ 822,811</u>	<u>\$ 2,358,230</u>
LIABILITIES AND NET ASSETS						
CURRENT LIABILITIES:						
Current maturities of long-term debt	\$ 12,787	\$ (11,800)	\$ 24,587	\$ 12,465	\$ 792	\$ 11,330
Current maturities of lease liability	14,539	-	14,539	3,812	2,778	7,949
Accounts payable and accrued expenses	129,779	-	129,779	51,699	13,261	64,819
Due to affiliates, net	-	(434)	434	-	434	-
Accrued compensation and related liabilities	44,844	-	44,844	24,566	6,655	13,623
Accrued interest payable	3,647	(3,488)	7,135	3,647	184	3,304
Estimated settlements due to third-party payers, net	3,279	-	3,279	-	1,719	1,560
Total current liabilities	<u>208,875</u>	<u>(15,722)</u>	<u>224,597</u>	<u>96,189</u>	<u>25,823</u>	<u>102,585</u>
LONG-TERM LIABILITIES:						
Estimated settlements due to third-party payers	2,127	-	2,127	-	1,372	755
Self-insurance liabilities	44,488	-	44,488	44,488	-	-
Accrued retirement benefits	23,754	-	23,754	22,727	-	1,027
Due to affiliates, net	-	(262,436)	262,436	-	-	262,436
Long-term debt, net of current maturities	550,152	(542,651)	1,092,803	549,256	8,226	535,321
Lease liability, net of current maturities	56,313	-	56,313	21,917	18,651	15,745
Other liabilities	7,636	-	7,636	1,898	2,353	3,385
Total liabilities	<u>893,345</u>	<u>(820,809)</u>	<u>1,714,154</u>	<u>736,475</u>	<u>56,425</u>	<u>921,254</u>
NET ASSETS (DEFICIENCY)						
Without donor restrictions:						
Virtua Obligated Group	2,007,420	(5,511)	2,012,931	(128,104)	713,282	1,427,753
Noncontrolling interests	44,973	-	44,973	-	38,478	6,495
	<u>2,052,393</u>	<u>(5,511)</u>	<u>2,057,904</u>	<u>(128,104)</u>	<u>751,760</u>	<u>1,434,248</u>
With donor restrictions						
	<u>26,205</u>	<u>-</u>	<u>26,205</u>	<u>8,851</u>	<u>14,626</u>	<u>2,728</u>
Total net assets (deficiency)	<u>2,078,598</u>	<u>(5,511)</u>	<u>2,084,109</u>	<u>(119,253)</u>	<u>766,386</u>	<u>1,436,976</u>
TOTAL LIABILITIES AND NET ASSETS (DEFICIENCY)	<u>\$ 2,971,943</u>	<u>\$ (826,320)</u>	<u>\$ 3,798,263</u>	<u>\$ 617,222</u>	<u>\$ 822,811</u>	<u>\$ 2,358,230</u>

Virtua Health, Inc.

COMBINING STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS INFORMATION -
VIRTUA OBLIGATED GROUP

For the year ended December 31, 2019

	Virtua Obligated Group	Eliminating Entries	Total	Virtua Health, Inc.	Virtua-Memorial Hospital of Burlington County	Virtua-West Jersey Health System, Inc. Total	Virtua-West Jersey Health System, Inc. Voorhees	Virtua-West Jersey Health System, Inc. Marlton
NET ASSETS WITHOUT DONOR RESTRICTIONS:								
Revenue:								
Patient service revenue	\$ 1,057,430	\$ -	\$ 1,057,430	\$ -	\$ 333,020	\$ 724,410	\$ 579,192	\$ 145,218
Other revenue	83,073	(317,608)	400,681	357,302	12,841	30,538	28,571	1,967
Equity in income of unconsolidated joint ventures	55,520	-	55,520	-	17,020	38,500	31,864	6,636
Total revenue	1,196,023	(317,608)	1,513,631	357,302	362,881	793,448	639,627	153,821
Expenses:								
Salaries and wages	462,595	-	462,595	122,363	111,657	228,575	179,803	48,772
Professional fees	38,906	-	38,906	614	14,504	23,788	17,947	5,841
Employees' fringe benefits	131,501	(56,635)	188,136	102,657	27,427	58,052	47,500	10,552
Other operating expenses	378,852	(243,537)	622,389	113,939	171,875	336,575	272,377	64,198
Interest	17,789	-	35,225	17,729	391	17,105	14,195	2,910
Depreciation and amortization	89,661	(17,436)	89,661	-	18,026	71,635	60,037	11,598
Total expenses	1,119,304	(317,608)	1,436,912	357,302	343,880	735,730	591,859	143,871
INCOME FROM OPERATIONS BEFORE GAIN ON ACQUISITION	76,719	-	76,719	-	19,001	57,718	47,768	9,950
Gain on acquisition of Our Lady of Lourdes Health Care Services, Inc.	174,253	-	174,253	174,253	-	-	-	-
INCOME FROM OPERATIONS	250,972	-	250,972	174,253	19,001	57,718	47,768	9,950
NONOPERATING GAINS AND LOSSES:								
Investment return, net	199,731	(2,467)	202,198	2,105	22,377	177,716	147,084	30,632
Loss on extinguishment of debt	(7,880)	-	(7,880)	-	-	(7,880)	(6,522)	(1,358)
Other accrued retirement costs	(1,563)	-	(1,563)	(1,563)	-	-	-	-
Total nonoperating gains (losses), net	190,288	(2,467)	192,755	542	22,377	169,836	140,562	29,274
EXCESS OF REVENUE AND NONOPERATING GAINS (LOSSES), NET OVER EXPENSES	441,260	(2,467)	443,727	174,795	41,378	227,554	188,330	39,224
EXCESS OF REVENUE AND NONOPERATING GAINS, NET OVER EXPENSES ATTRIBUTED TO NONCONTROLLING INTERESTS	(15,067)	-	(15,067)	-	(10,459)	(4,608)	(3,814)	(794)
EXCESS OF REVENUE AND NONOPERATING GAINS, OVER EXPENSES ATTRIBUTED TO VIRTUA OBLIGATED GROUP	426,193	(2,467)	428,660	174,795	30,919	222,946	184,516	38,430
OTHER CHANGES IN NET ASSETS WITHOUT DONOR RESTRICTIONS - VIRTUA OBLIGATED GROUP								
Net assets released for property, plant, and equipment	250	-	250	-	53	197	163	34
Other changes in accrued retirement benefits	5,457	-	5,457	5,457	-	-	-	-
Transfers with affiliates, net	(69,220)	-	(69,220)	(31,222)	8,651	(46,649)	(38,608)	(8,041)
Increase in net assets without donor restrictions - Virtua Obligated Group	362,680	(2,467)	365,147	149,030	39,623	176,494	146,071	30,423
NONCONTROLLING INTERESTS:								
Excess of revenues and nonoperating gains, net over expenses attributable to noncontrolling interests	15,067	-	15,067	-	10,459	4,608	3,814	794
Distributions	(10,421)	-	(10,421)	-	(6,010)	(4,411)	(3,652)	(759)
Others	(156)	-	(156)	-	(156)	-	-	-
Increase in net assets without donor restrictions - noncontrolling interests	4,490	-	4,490	-	4,293	197	162	35
NET ASSETS WITH DONOR RESTRICTIONS:								
Contributions, net	3,169	-	3,169	1,506	825	838	693	145
Increase in beneficial interest in perpetual trust	986	-	986	-	986	-	-	-
Net assets released from restrictions for operations	(1,252)	-	(1,252)	(1,129)	(46)	(77)	(64)	(13)
Net assets released from restrictions for property, plant, and equipment	(250)	-	(250)	-	(53)	(197)	(163)	(34)
Transfers with affiliates, net	-	-	-	(39)	8	31	26	5
Increase in net assets with donor restrictions	2,653	-	2,653	338	1,720	595	492	103
INCREASE IN NET ASSETS	369,823	(2,467)	372,290	149,368	45,636	177,286	146,725	30,561
NET ASSETS (DEFICIENCY) - beginning of year	1,708,775	(3,044)	1,711,819	(268,621)	720,750	1,259,690	1,044,934	214,756
NET ASSETS (DEFICIENCY) - end of year	\$ 2,078,598	\$ (5,511)	\$ 2,084,109	\$ (119,253)	\$ 766,386	\$ 1,436,976	\$ 1,191,659	\$ 245,317

DEBT SERVICE COVERAGE RATIO CALCULATION - VIRTUA OBLIGATED GROUP

December 31, 2019

(Dollars in thousands)

1 Funds available for debt service:	
Excess of revenue and gains over expenses and losses	\$ 426,193
Add (deduct):	
Interest expense	17,789
Joint venture interest	(4)
Depreciation and amortization expenses	89,661
Joint venture depreciation and amortization expenses	(254)
Provision for other non-cash expenses	60,384
Joint venture provision for other non-cash expenses	<u>(635)</u>
Total	<u>\$ 593,134</u>
2 Maximum annual debt service requirement:	<u>\$ 39,444</u>
3 Debt service coverage ratio:	
<u>Funds available for debt service</u>	<u>\$ 593,134</u>
Maximum annual debt service requirement	<u>\$ 39,444</u>
Debt service coverage ratio	<u>15.04</u>

- * "Funds Available for Debt Service" shall mean, in any Fiscal Year, for any one or more Members of the Obligated Group or, as the context requires, the entire Obligated Group, the sum of: (i) the excess of revenues over expenses, as determined in accordance with generally accepted accounting principles; (ii) interest expense with respect to interest requirements on all Long-Term Indebtedness then outstanding; and (iii) all depreciation expense, amortization of financing charges and other noncash expenses deducted in determining the excess of revenues over expenses for such Fiscal Year, all as determined in accordance with accounting principles generally accepted in the United States of America. In the event that the Fiscal Year of any Member of the Obligated Group ends on a date other than the last day of any Fiscal Year under consideration, the Funds Available for Debt Service for such Fiscal Year will include the amounts for such Member of the Obligated Group for its most recent Fiscal Year.

Virtua Health, Inc.

CUSHION RATIO CALCULATION - VIRTUA OBLIGATED GROUP

December 31, 2019

(Dollars in thousands)

1	Cash and cash equivalents and assets limited as to use by Board of Trustees' designation as of December 31, 2019:	
	Cash and cash equivalents	\$ 65,486
	Less: Joint venture's cash and cash equivalents	(4,497)
	Assets limited as to use by Board of Trustees' designation	<u>1,137,828</u>
	Total	<u>\$ 1,198,817</u>
2	Maximum annual debt service requirement:	<u>\$ 39,444</u>
3	Cushion ratio:	
	<u>Cash and cash equivalents and assets limited as to use by Board of Trustees' designation</u>	<u>\$ 1,198,817</u>
	Maximum annual debt service requirement	<u>\$ 39,444</u>
	Cushion ratio	<u>30.39</u>

DAY'S CASH ON HAND CALCULATION - VIRTUA OBLIGATED GROUP

December 31, 2019

(Dollars in thousands)

Cash and cash equivalents and assets limited as to use by Board of Trustees' designation as of December 31, 2019:

Cash and cash equivalents	\$ 65,486
Less: Joint venture's cash and cash equivalents	(4,497)
Assets limited as to use by Board of Trustees' designation	<u>1,137,828</u>

Adjusted cash and cash equivalents	<u>\$ 1,198,817</u>
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2019 operating expenses	\$ 1,119,304
Less: Joint venture operating expenses	(5,593)
Less: Depreciation and amortization	(89,661)
Add: Joint venture depreciation and amortization	<u>254</u>

Cash operating expenses	1,024,304
Divided by 365 days	<u>/365</u>

Daily cash operating expenses	<u>\$ 2,806</u>
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Day's cash on hand	<u><u>427</u></u>
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Virtua Health, Inc.

DEBT TO CAPITALIZATION RATIO CALCULATION - VIRTUA OBLIGATED GROUP

December 31, 2019

(Dollars in thousands)

1 Long-term indebtedness at December 31, 2019:	
Long-term debt	<u>\$ 562,939</u>
2 Capitalization amount:	
Long-term debt	\$ 562,939
Net assets without donor restrictions - Virtua Obligated Group	<u>2,007,420</u>
Total	<u>\$ 2,570,359</u>
3 Debt to capitalization ratio:	
<u>Long-term indebtedness</u>	<u>\$ 562,939</u>
Capitalization amount	<u>\$ 2,570,359</u>
Debt to capitalization ratio	<u>0.22</u>



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