

CONSOLIDATED FINANCIAL STATEMENTS AND  
SUPPLEMENTARY INFORMATION

St. Joseph's Health, Inc.  
Years Ended December 31, 2018 and 2017  
With Report of Independent Auditors

Ernst & Young LLP



St. Joseph's Health, Inc.

Consolidated Financial Statements and  
Supplementary Information

Years Ended December 31, 2018 and 2017

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## Report of Independent Auditors

The Board of Trustees  
St. Joseph's Health, Inc.

We have audited the accompanying consolidated financial statements of St. Joseph's Health, Inc. (SJH), which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### **Management's Responsibility for the Financial Statements**

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

### **Auditor's Responsibility**

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

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

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

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of St. Joseph's Health, Inc. at December 31, 2018 and 2017, and the consolidated results of its operations, changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

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

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

## Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating balance sheet at December 31, 2018 and the consolidating statements of operations and changes in net assets for the year then ended are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

*Ernst + Young LLP*

May 23, 2019

# St. Joseph's Health, Inc.

## Consolidated Balance Sheets

|  | <b>December 31</b>    |             |
|--|-----------------------|-------------|
|  | <b>2018</b>           | <b>2017</b> |
|  | <i>(In Thousands)</i> |             |
| <b>Assets</b>  |                       |             |
| Current assets:  |                       |             |
| Cash and cash equivalents  | \$ 30,783             | \$ 68,228   |
| Investments  | 233,738               | 246,191     |
| Current portion of assets whose use is limited   | 18,114                | 17,052      |
| Patient accounts receivable – less allowance for uncollectibles of<br>\$7,104 in 2018 and \$69,901 in 2017 | 83,186                | 90,748      |
| Contributions and pledges receivable   | 1,036                 | 1,299       |
| Prepaid expenses and other current assets  | 36,067                | 24,872      |
| Total current assets   | 402,924               | 448,390     |
| Assets whose use is limited – less current portion   | 47,052                | 46,908      |
| Property and equipment – net   | 366,251               | 335,964     |
| Beneficial interest in perpetual trusts  | 5,530                 | 6,139       |
| Equity investments in joint ventures   | 28,396                | 27,558      |
| Other noncurrent assets  | 11,631                | 15,651      |
| Total assets   | \$ 861,784            | \$ 880,610  |
| <b>Liabilities and net assets</b>  |                       |             |
| Current liabilities:   |                       |             |
| Current portion of long-term debt  | \$ 5,755              | \$ 5,882    |
| Accounts payable   | 52,479                | 43,905      |
| Accrued salaries and expenses  | 77,330                | 73,862      |
| Accrued interest payable   | 7,210                 | 5,359       |
| Deferred revenue   | 1,038                 | 314         |
| Current portion of estimated third-party payer settlements   | 762                   | 555         |
| Total current liabilities  | 144,574               | 129,877     |
| Long-term debt – net of current portion  | 365,663               | 372,211     |
| Estimated third-party payer settlements – net of current portion   | 9,394                 | 7,475       |
| Accrued pension liability  | 100,278               | 111,427     |
| Estimated professional liability claims payable – net of current portion                                   | 32,412                | 27,423      |
| Other liabilities  | 10,870                | 11,024      |
| Total liabilities  | 663,191               | 659,437     |
| Commitments and contingencies  |                       |             |
| Net assets:  |                       |             |
| Net assets without donor restrictions  | 179,654               | 195,350     |
| Net assets with donor restrictions   | 18,355                | 21,942      |
| Total St. Joseph's Health, Inc. net assets   | 198,009               | 217,292     |
| Non-controlling interests in joint ventures  | 584                   | 3,881       |
| Total net assets, including non-controlling interests  | 198,593               | 221,173     |
| Total liabilities and net assets   | \$ 861,784            | \$ 880,610  |

*See accompanying notes.*

St. Joseph's Health, Inc.

Consolidated Statements of Operations

|   | <b>Year Ended December 31</b> |                  |
|---|-------------------------------|------------------|
|   | <b>2018</b>                   | <b>2017</b>      |
|   | <i>(In Thousands)</i>         |                  |
| <b>Operating revenues:</b>  |                               |                  |
| Net patient service revenue   | \$ 713,470                    | \$ 788,984       |
| Provision for bad debts   | –                             | (81,377)         |
| Net patient service revenue – net of provision for bad debts                                      | <u>713,470</u>                | <u>707,607</u>   |
| Other revenue   | 93,426                        | 93,122           |
| Net assets released from restrictions – operations  | <u>1,716</u>                  | <u>2,746</u>     |
| Total operating revenues  | <b>808,612</b>                | <b>803,475</b>   |
| <b>Operating expenses:</b>  |                               |                  |
| Salaries and wages  | 385,755                       | 383,408          |
| Employee benefits   | 71,456                        | 86,239           |
| Physician fees  | 22,593                        | 22,119           |
| Supplies and other  | 280,853                       | 271,551          |
| Interest  | 11,764                        | 14,142           |
| Depreciation and amortization   | <u>33,880</u>                 | <u>33,316</u>    |
| Total operating expenses  | <b>806,301</b>                | <b>810,775</b>   |
| Operating income (loss)   | <b>2,311</b>                  | <b>(7,300)</b>   |
| Non-operating gains and losses:   |                               |                  |
| Investment return   | 6,963                         | 6,249            |
| Loss on extinguishment of debt  | –                             | (1,853)          |
| Excess (deficiency) of revenues over expenses, before non-controlling interests in joint ventures | <u>9,274</u>                  | <u>(2,904)</u>   |
| Less: net gain attributable to non-controlling interests in joint ventures                        | 3,972                         | 4,843            |
| Excess (deficiency) of revenues over expenses   | <b>5,302</b>                  | <b>(7,747)</b>   |
| <b>Other changes in net assets without donor restrictions:</b>                                    |                               |                  |
| Change in net unrealized gains and losses on investments  | (10,301)                      | 1,118            |
| Pension-related adjustments   | (6,443)                       | 22,804           |
| Net assets released from restrictions – capital acquisitions                                      | 402                           | 779              |
| Transfer of assets from (to) joint ventures   | 344                           | (425)            |
| Dissolution of joint ventures   | <u>(5,000)</u>                | <u>–</u>         |
| Change in net assets without donor restrictions   | <b>\$ (15,696)</b>            | <b>\$ 16,529</b> |

See accompanying notes.

St. Joseph's Health, Inc.

Consolidated Statements of Changes in Net Assets

|   | <b>Year Ended December 31</b> |             |
|---|-------------------------------|-------------|
|   | <b>2018</b>                   | <b>2017</b> |
|   | <i>(In Thousands)</i>         |             |
| <b>Net assets without donor restrictions:</b>                                     |                               |             |
| Change in net assets without donor restrictions                                   | <b>\$ (15,696)</b>            | \$ 16,529   |
| <b>Net assets with donor restrictions:</b>  |                               |             |
| Contributions, grants, investment income, and other support                       | <b>(857)</b>                  | 2,294       |
| Net assets released from restrictions – operations                                | <b>(1,719)</b>                | (2,746)     |
| Net assets released from restrictions – capital acquisitions                      | <b>(402)</b>                  | (779)       |
| Change in net unrealized gains and losses on investments held in perpetual trusts | <b>(609)</b>                  | 428         |
| Decrease in net assets with donor restrictions                                    | <b>(3,587)</b>                | (803)       |
| (Decrease) increase in St. Joseph's Health, Inc. net assets                       | <b>(19,283)</b>               | 15,726      |
| <b>Non-controlling interests in joint ventures:</b>                               |                               |             |
| Net gain attributable to non-controlling interests in joint ventures              | <b>3,972</b>                  | 4,843       |
| Distributions to non-controlling interests in joint ventures, net                 | <b>(7,269)</b>                | (4,782)     |
| (Decrease) increase in non-controlling interests                                  | <b>(3,297)</b>                | 61          |
| Change in net assets, including non-controlling interests                         | <b>(22,580)</b>               | 15,787      |
| Net assets at beginning of year   | <b>221,173</b>                | 205,386     |
| Net assets at end of year   | <b>\$ 198,593</b>             | \$ 221,173  |

*See accompanying notes.*

# St. Joseph's Health, Inc.

## Consolidated Statements of Cash Flows

|   | <b>Year Ended December 31</b> |                  |
|---|-------------------------------|------------------|
|   | <b>2018</b>                   | <b>2017</b>      |
|   | <i>(In Thousands)</i>         |                  |
| <b>Operating activities</b>   |                               |                  |
| Change in net assets including non-controlling interests  | \$ (22,580)                   | \$ 15,787        |
| Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities: |                               |                  |
| Depreciation and amortization   | 33,880                        | 33,316           |
| Change in net unrealized gains and losses on investments and perpetual trusts                         | 10,910                        | (1,546)          |
| Net realized gains and losses on sales of investments   | 1,870                         | 48               |
| Donor restricted contributions and other support  | 860                           | (2,294)          |
| Distributions to non-controlling interests in joint ventures, net                                     | 7,269                         | 4,782            |
| Gain on sale of certain assets and business operations of VHS Management, Inc.                        | -                             | (8,000)          |
| Equity in earnings of joint ventures  | (2,778)                       | (4,214)          |
| Loss on extinguishment of debt and amortization of financing costs and bond premium and discount      | -                             | 2,112            |
| Changes in operating assets and liabilities:  |                               |                  |
| Patient accounts receivable   | 7,562                         | 349              |
| Prepaid expenses and other assets   | (8,647)                       | 1,082            |
| Accounts payable, accrued salaries and expenses and interest payable                                  | 13,893                        | 7,806            |
| Estimated third-party payer settlements   | 2,126                         | (3,528)          |
| Accrued pension liability   | (11,149)                      | (92,634)         |
| Estimated professional liability claims payable and other liabilities                                 | 5,559                         | 4,087            |
| Net cash provided by (used in) operating activities   | <u>38,775</u>                 | <u>(42,847)</u>  |
| <b>Investing activities</b>   |                               |                  |
| Acquisition of property and equipment, net  | (61,857)                      | (44,953)         |
| Sales (purchases) of investments, net   | 441                           | (53,692)         |
| Net cash used in investing activities   | <u>(61,416)</u>               | <u>(98,645)</u>  |
| <b>Financing activities</b>   |                               |                  |
| Repayment of long-term debt   | (6,675)                       | (33,071)         |
| Issuance of long-term debt  | -                             | 105,850          |
| Distributions paid to non-controlling interests in joint ventures, net                                | (7,269)                       | (4,782)          |
| Donor restricted contributions and other support  | (860)                         | 2,294            |
| Net cash (used in) provided by financing activities   | <u>(14,804)</u>               | <u>70,291</u>    |
| Net decrease in cash and cash equivalents   | <u>(37,445)</u>               | <u>(71,201)</u>  |
| Cash and cash equivalents, beginning of year  | 68,228                        | 139,429          |
| Cash and cash equivalents, end of year  | <u>\$ 30,783</u>              | <u>\$ 68,228</u> |
| <b>Supplemental information</b>   |                               |                  |
| Cash paid for interest, net of amounts capitalized  | \$ 14,405                     | \$ 12,835        |
| Assets acquired under capitalized lease obligations   | <u>\$ 2,310</u>               | <u>\$ -</u>      |

*See accompanying notes.*



# St. Joseph's Health, Inc.

## Notes to Consolidated Financial Statements

December 31, 2018

### 1. Organization and Summary of Significant Accounting Policies

#### Organization

The accompanying consolidated financial statements include the accounts of St. Joseph's Health, Inc. (SJH), a not-for-profit holding corporation sponsored by Sisters of Charity of Saint Elizabeth, and its affiliates (collectively, the System). Affiliated members of SJH include St. Joseph's University Medical Center, Inc. and subsidiaries, St. Joseph's Hospital and Medical Center Foundation, Inc. (the Medical Center Foundation), St. Joseph's Wayne Hospital Foundation, Inc. (the Wayne Foundation), 200 Hospital Plaza Corporation (200 Hospital Plaza), SJHS Insurance Limited (the Insurance Captive), VHS Management, Inc. and subsidiary (VHS) and St. Joseph's Home Health, LLC. In September 2018, St. Joseph's Health Partners LLC was formed as a single member limited liability corporation to operate a clinically integrated network with St. Joseph's University Medical Center, Inc. as its sole owner.

In February 2019, the Sisters of Charity of Saint Elizabeth formed a subsidiary organization, Seton Ministries, Inc., which became the sole member of SJH. Effective January 1, 2019, the Wayne Foundation was merged into the Medical Center Foundation.

St. Joseph's University Medical Center, formerly known as St. Joseph's Hospital and Medical Center, (the University Medical Center) was founded in 1867 and is located in Paterson, New Jersey. It is an acute-care hospital with 651 licensed beds and 30 newborn bassinets. The University Medical Center is a state-designated trauma center and provides a full range of health care services. Effective January 1, 2010, St. Joseph's Wayne Medical Center and subsidiary (Wayne Medical Center) was merged with the University Medical Center and, collectively, the entities are referred to herein as the "Medical Center." Wayne Medical Center is located in Wayne, New Jersey, and is an acute-care hospital with 229 licensed beds. Wayne Medical Center provides comprehensive medical and surgical care, and emergency and diagnostic services for its community.

The Medical Center also operates St. Joseph's Healthcare and Rehab Center, a 151 bed skilled nursing facility located in Cedar Grove, New Jersey. In addition, the Medical Center includes the following wholly owned subsidiaries:

- St. Joseph's Hospital Housing Corp. (the Housing Corp.) and its subsidiaries, Genesis Property Development Holding, LLC and Genesis Property Development, LLC (collectively, Genesis), provide property-management services for non-hospital-related real estate holdings. The Housing Corp. ceased its operations in 2009.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

- St. Joseph's Healthcare Physicians, Inc.; St. Joseph's Emergency Physicians, Inc.; St. Joseph's Faculty Physicians, Inc.; and St. Joseph's Physician's, Inc. manage the Medical Center's faculty staff billing services.
- Harbor House, Inc. and its subsidiaries, Harborside Apartments, Inc. and Harborview Apartments, Inc., provide housing and services to individuals with mental illnesses.

The Medical Center is also the majority member of St. Joseph's Surgery Management, LLC (Surgery Management). Surgery Management is a limited liability corporation established to manage the surgical services at the University Medical Center. Additionally, the Medical Center was the majority member of the following entities which were dissolved in 2018: St. Joseph's Regional Cardiology, LLC (Paterson Cardiology); St. Joseph's Wayne Cardiology, LLC (Wayne Cardiology); and Blue Moon Properties, LLC (Blue Moon). Paterson Cardiology and Wayne Cardiology were limited liability corporations that each operated a cardiac catheterization laboratory. Blue Moon was a limited liability corporation that provided radiology-management services. The Medical Center paid \$5.0 million in 2018 to acquire the remaining interests in the dissolved joint ventures.

The Medical Center Foundation and the Wayne Foundation are public charities whose primary purpose is to raise funds for the University Medical Center and Wayne Medical Center, respectively, and their affiliated organizations, and other area charitable organizations.

200 Hospital Plaza is a not-for-profit organization whose purpose is to further the operations of the Medical Center by owning, managing, and operating parking facilities and any other facilities that may be deemed useful or necessary for employees, patients, visitors, doctors, and other persons affiliated with the Medical Center.

The Insurance Captive, which is a wholly owned captive insurance company domiciled in Bermuda, was established in 2007 to provide the System with general liability and professional medical liability insurance.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

VHS is a not-for-profit corporation incorporated in the state of New Jersey and is the holding company of Visiting Health Services of New Jersey, Inc. (the Agency). The Agency operated a not-for-profit home health agency that served Passaic, Bergen, and Morris counties in New Jersey. In May 2017, the System sold certain assets and business operations related to VHS to a newly formed joint venture, VHSNJ at Home, LLC, a joint venture between a subsidiary of the System, St. Joseph's Home Health, LLC, and Hackensack Meridian Home Care Services, Inc. The System realized a gain of approximately \$8.0 million on the sale, included in other revenue in the accompanying 2017 consolidated statement of operations. The System holds a 50% ownership interest in the VHSNJ at Home, LLC joint venture.

In connection with the issuance of the New Jersey Healthcare Facilities Financing Authority St. Joseph's Healthcare System Obligated Group Issue, Series 2016 Revenue Bonds in 2016, the System formed an "Obligated Group," which includes only the Medical Center. The Obligated Group issued Series 2017 Taxable Bonds in September 2017.

#### **Significant Accounting Policies**

A summary of the System's significant accounting policies is as follows:

*Principles of Consolidation:* The consolidated financial statements include the accounts of SJH and its affiliates. SJH accounts for its interests in entities in which it has significant influence but not control on the equity basis of accounting.

*Investment in Consolidated Subsidiaries:* The Medical Center was a majority member of Paterson Cardiology, Wayne Cardiology, and Blue Moon and maintained a 51% interest in each of these at December 31, 2017. In addition, the Medical Center is a majority member of Surgery Management and maintains a 56% and 59% interest at December 31, 2018 and 2017, respectively. The accounts of these consolidated subsidiaries are consolidated with those of the Medical Center. The change in the non-controlling interests are separately reported. All intercompany transactions and account balances have been eliminated in consolidation.

*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 (GAAP) consistent with the Financial Accounting Standards Board (FASB) Accounting Standards Codification 954, *Health Care Entities*, and the American Institute of Certified Public Accountants' Audit and Accounting Guide, *Health Care Entities*, and other pronouncements applicable to health care organizations.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Use of Estimates:* The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the consolidated financial statements. Estimates also affect the amounts of revenue and expenses reported during the period. Actual results could differ from those estimates. Significant estimates include collections on patient accounts receivable, estimated third-party payer settlements, valuation of goodwill, valuation of investments, accrued pension liability, estimated professional liability claims payable, and other self-insurance liabilities.

*Cash and Cash Equivalents:* Cash and cash equivalents include highly liquid investments with an original maturity of three months or less, except for amounts recorded in assets whose use is limited. The carrying amount of cash and cash equivalents reported on the consolidated balance sheets approximates fair value. The System does not hold any money market funds with significant liquidity restrictions that would be required to be excluded from cash equivalents.

*Investments and Investment Income:* Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value and are classified as other-than-trading securities. Fair value is based on quoted market prices of the investment or similar investments. Investment return (including realized gains and losses on investments, interest, and dividends) is included in the excess (deficiency) of revenues over expenses in the accompanying consolidated statements of operations, unless the income or loss is restricted by donor or law. The change in net unrealized gains and losses on investments is reported as a separate component of the change in net assets without donor restrictions, except that declines in fair value that are determined by management to be other than temporary are reported as realized losses. Donated investments are recorded at the fair value on the date of receipt.

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 financial statements.

The System reviews its investments to identify those for which fair value is below cost. The System then makes a determination as to whether the investment should be considered other-than-temporarily impaired. No such losses were recorded in 2018 or 2017. Unrealized losses on individual investment holdings were not significant.

# St. Joseph's Health, Inc.

## Notes to Consolidated Financial Statements (continued)

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

*Assets Whose Use is Limited:* Assets whose use is limited include assets held by trustees under bond indenture agreements, professional liability funds and investments held by the Insurance Captive, designated assets set aside by the Board of Trustees (the Board) over which the Board retains control and may at its discretion subsequently use for other purposes, and donor-restricted assets. Amounts available to meet current liabilities of the System have been classified as current assets in the accompanying consolidated balance sheets.

*Supplies:* Supplies are stated at the lower of cost (first in, first out) or net realizable value. Supplies are used in the provision of patient care and are not held for sale.

*Property and Equipment:* Property and equipment acquisitions are recorded at cost, except donated assets, which are recorded at fair value at the date of donation. Depreciation expense is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the accompanying consolidated statements of operations.

Estimated useful lives for the property and equipment are as follows:

|                                   |             |
|-----------------------------------|-------------|
| Land improvements                 | 15–20 years |
| Buildings and improvements        | 5–60 years  |
| Fixed and major movable equipment | 5–12 years  |

Gifts of long-lived assets, such as land, buildings, or equipment, are reported as an increase to net assets without donor 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.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Goodwill and Other Intangible Assets:* Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. Goodwill is not amortized, but instead is tested for impairment at the reporting unit level annually or more frequently if the presence of certain circumstances indicates that impairment may have occurred. The impairment review process compares the fair value of the reporting unit in which goodwill resides to the carrying value. If the carrying amount of a reporting unit exceeds its fair value, then the amount of the impairment loss must be measured. The System has selected December 31 as its annual testing date.

Acquired identified intangible assets (other than goodwill) are amortized on a straight-line basis over the period of benefit, which is five years. The System evaluates the recoverability of identifiable intangible assets whenever events or changes in circumstances indicate that an intangible asset's carrying amount may not be recoverable. Goodwill and other intangible assets are included in other noncurrent assets in the accompanying consolidated balance sheets at December 31, 2018 and 2017.

*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.

*Deferred Financing Costs:* Deferred financing costs represent costs incurred to obtain financing for various construction and renovation projects at the Medical Center and 200 Hospital Plaza. These costs are amortized over the remaining term of the applicable indebtedness using the effective interest method. The System paid financing costs of approximately \$1.0 million and wrote-off costs of approximately \$0.5 million as part of 2017 debt transactions (see Note 9).

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Beneficial Interest in Perpetual Trusts:* Perpetual trusts are arrangements in which a donor establishes and funds a perpetual trust administrated by a third party. The perpetual trusts consist of life estate gifts. Under the terms of the trusts, the Medical Center Foundation and the Wayne Foundation have an irrevocable right to receive the income earned on the trust assets in perpetuity. Income earned is without donor restrictions and included in other revenue in the accompanying consolidated statements of operations. The Medical Center Foundation and the Wayne Foundation do not control the assets held by an outside trust. The Medical Center Foundation and the Wayne Foundation recognize their respective interests in the trusts within net assets with donor restrictions to be maintained in perpetuity based on the fair value of the trust assets. Changes in the fair value of the trusts are recorded as a change in net unrealized gains and losses on investments held in perpetual trusts in the accompanying consolidated statements of changes in net assets.

*Equity Investments in Joint Ventures:* The System's investments in joint ventures are accounted for using the equity method of accounting except for joint ventures where the System holds a controlling interest.

*Other Investments:* The System's other investments are accounted for using the cost method of accounting and are included in other noncurrent assets in the accompanying balance sheets at December 31, 2018 and 2017.

*Other Assets:* Other assets consist primarily of goodwill, other intangible assets, investments held by trustee, security deposits and physician loan receivables.

*Other Liabilities:* Capital project obligations related to grant agreements with the State of New Jersey Department of Health and Human Services, Division of Mental Health Services in the amount of \$945,000 at December 31, 2018 and 2017, are included in other noncurrent liabilities in the accompanying consolidated balance sheets.

*Deferred Revenue:* Advances received from third-party payers for future services to be provided to patients are recorded as deferred revenue in the consolidated balance sheets. The System is the recipient of various awards and contracts from governmental agencies. Unearned revenue is recorded as deferred revenue in the consolidated balance sheets upon receipt. Revenue is recognized only to the extent of expenditures incurred, and are recorded in other revenue in the consolidated statements of operations.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Contributions and Pledges Receivable:* Unconditional promises to give are recorded at net realizable value based on the present value of their estimated future cash flows. Present value of such amounts is computed using a risk-free discount rate at the time of the pledge ranging from 3.5% to 4.5% at December 31, 2018 and 2017. Conditional promises to give are not included as support until the conditions are substantially met.

*Self-Insurance:* The Medical Center offers medical insurance to its employees through a health maintenance organization and a preferred provider organization (PPO). The PPO provides third-party administrative services for employees, who are enrolled in the program. The Medical Center remains self-insured for health insurance claims associated with the employees that select the PPO option. An estimated liability for employee medical benefits incurred but not reported is included within accrued salaries and expenses in the accompanying consolidated balance sheets.

The Medical Center offers workers' compensation through a high deductible structure with commercial insurance above specific amounts. The current portion of the estimated liability for worker's compensation of approximately \$6.5 million and \$4.7 million at December 31, 2018 and 2017, respectively, is included in accrued salaries and expenses, and approximately \$5.6 million at December 31, 2018 and 2017 is included as long-term in other liabilities in the accompanying consolidated balance sheets.

*Estimated Professional Liability Claims Payable:* The System's professional liability program is described in Note 11. An estimated liability for medical malpractice costs related to reported claims that exceed or are not subject to insurance coverage, if any, and incurred claims that have not been reported to the Insurance Captive or claims-made insurance carrier is recorded in the consolidated balance sheets. The Insurance Captive maintains a self-insurance reserve trust as the funding vehicle for the self-insurance program. The System recognizes a receivable for insurance recoveries at the time a liability is recorded, and records a valuation allowance for uncollectible receivables when applicable.

*Accounting for Pension Plans:* The System's retirement plans are described in Note 10. The System recognizes the overfunded or underfunded status of the defined benefit post retirement plans in the consolidated balance sheets. Changes in the funded status of such plans are reported in the year in which the changes occur as a change in net assets without donor restrictions presented after the excess (deficiency) of revenues over expenses in the accompanying consolidated statements of operations.



## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Performance Indicator:* The consolidated statements of operations include the excess (deficiency) of revenues over expenses as the performance indicator. Changes in net assets without donor restrictions which are excluded from the performance indicator include pension-related adjustments, contributions of long-lived assets, permanent transfers of assets to and from affiliates or controlled joint venture for other than goods and services, and the net change in unrealized gains and losses on investments (except for declines in fair value that are determined by management to be other than temporary, which are reported as realized losses).

Transactions deemed by management to be ongoing, major, or central to the provision of health care services are reported as operating revenues and operating expenses and are included in operating income (loss). Investment return and certain transactions of an infrequent nature are excluded from operating income (loss).

*Classification of Net Assets:* The System separately accounts for and reports net assets without donor restrictions and net assets with donor restrictions. Net assets without donor restrictions are not externally restricted for identified purposes by donors or grantors. Net assets without donor restrictions include resources that the governing board may use for any designated purpose and resources whose use is limited by agreement between the System and an outside party other than the donor or grantor.

Net assets with donor restrictions are those whose use by the System has been limited by donors to a specific time period or purpose or have been restricted by donors as permanent endowments to be maintained in perpetuity. When the donors' intentions are met or a time restriction expires for net assets limited by donors to a specific time period or purpose, the net assets are reclassified to net assets without donor restriction and reported on the consolidated statements of operations and changes in net assets as net assets released from restrictions.

Donor-restricted contributions whose restrictions are met within the same year as received are reported within other revenue in the accompanying consolidated statements of operations. In the absence of donor specifications that income and gains on donated funds are restricted, such income and gains are reported as investment return in the accompanying consolidated statements of operations.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Tax Status:* The System and substantially all of its affiliates 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 the System are also exempt from state income taxes. Genesis, Paterson Cardiology, Wayne Cardiology, Blue Moon, and Surgery Management are limited liability corporations, which are treated as partnerships for income tax purposes, and do not require a provision for income taxes. The Insurance Captive is exempt from taxes through March 2035.

The Tax Cuts and Jobs Act (TCJA) was enacted on December 22, 2017. For tax-exempt entities, TCJA requires organizations to categorize certain fringe benefit expenses as a source of unrelated business income subject to tax, pay an excise tax on compensation above certain thresholds, and record income or losses for tax determination purposes from unrelated business activities on an activity-by-activity basis, among other provisions. Regulations necessary to implement certain aspects of TCJA are expected to be promulgated by the Internal Revenue Service (IRS) in 2019. As of and for the year ended December 31, 2018, the System has made reasonable estimates of the provision for income taxes and the compensation excise tax based on accounting guidance included in Accounting Standards Codification 740, *Income Taxes*. The System will continue to refine its calculations in future periods as additional regulations and guidance are issued by the IRS. The provision for income taxes is not material to the System's consolidated statements of operations.

*Recently Adopted Accounting Pronouncements:* In May 2014, the FASB issued Accounting Standards Update No. (ASU) 2014-09, *Revenue from Contracts with Customers*. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance in ASU 2014-09 supersedes the FASB's prior revenue recognition requirements and most industry-specific guidance. The FASB subsequently issued ASU 2015-14, *Revenue from Contracts with Customers*, which deferred the effective dates of ASU 2014-09. Based on ASU 2015-14, the provisions of ASU 2014-09 became effective for the System for annual reporting periods beginning after December 15, 2017. The System adopted ASU 2014-09 following the modified retrospective method. As a result of implementing ASU 2014-09, certain patient activity where collection is uncertain (representing approximately \$88.6 million for the year ended December 31, 2018) previously reported through December 31, 2017 as net patient service revenue and the provision for bad debts in the System's consolidated statements of operations

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

no longer meets the criteria for revenue recognition and, accordingly, the provision for bad debts after the adoption date is significantly reduced with a corresponding reduction to net patient service revenue. Such patient activity is now classified as an implicit price concession. Additionally, the provision for bad debts, when applicable, will now be presented as an expense item rather than a reduction to net patient service revenue. Other aspects of the System's implementation of ASU 2014-09 impacting net patient service revenue, which include judgments regarding collection analyses and estimates of variable consideration and the addition of certain qualitative and quantitative disclosures are included in Note 3. The adoption of ASU 2014-09 did not significantly affect other revenue activity.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities*, which eliminates the requirement for not-for-profits (NFPs) to classify net assets as unrestricted, temporarily restricted and permanently restricted. Instead, NFPs will be required to classify net assets as net assets with donor restrictions or without donor restrictions. The guidance also modified required disclosures and reporting related to net assets, investment expenses and information regarding liquidity. NFPs are also required to report all expenses by both functional and natural classification in one location. The provisions of ASU 2016-14 became effective for the System for annual periods beginning after December 15, 2017. The System adopted ASU 2016-14 effective for its December 31, 2018 consolidated financial statements. The effects of the adoption of ASU 2016-14 were applied retrospectively, except for the disclosures about liquidity and availability of resources, as permitted by ASU 2016-14. The adoption of ASU 2016-14 had no impact on the total net assets previously reported by the System as of December 31, 2017.

*Pending Accounting Pronouncements:* In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. ASU 2016-01 will require business-oriented health care not-for-profit entities to measure equity investments that do not result in consolidation and are not accounted for under the equity method at fair value and recognize any changes in fair value in the performance indicator unless the investments qualify for a new practicality exception. The practicality exception is available for equity investments without a readily determinable fair value, for which measurement would be based on cost less impairment and adjusted for observable price changes. Subsequent to the adoption of ASU 2016-01, the System will no longer be able to recognize unrealized holding gains and losses on equity securities currently classified as other-than-trading outside of the performance indicator. This ASU does not impact the accounting for investments in debt securities.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

ASU 2016-01 contains an additional provision that eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost. The amendments of this ASU are applicable for fiscal years beginning after December 15, 2018; however, early adoption is permitted for the provision relating to the elimination of the requirement to disclose the fair value of financial instruments measured at amortized cost. As such, the System has elected to early adopt this provision and will no longer disclose the fair value of debt within its consolidated financial statements. The System has not completed the process of evaluating the impact of the other provisions of ASU 2016-01 on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases*, which will require a lessee to report most leases on its balance sheet but recognize expenses on its income statement in a manner similar to current accounting. The guidance also eliminates current real estate-specific provisions. The provisions of ASU 2016-02 are effective for the System for annual periods beginning after December 15, 2018, and interim periods within those years. Early adoption is permitted. Subsequent to the adoption, the System's assets and liabilities are expected to increase to reflect the System's right to use certain assets and the corresponding liabilities associated with operating leases, with no significant impact to net assets or the performance indicator.

In January 2017, the FASB issued ASU 2017-04, *Intangibles-Goodwill and Other*. ASU 2017-04 will simplify the accounting for goodwill impairment and will remove Step 2 of the current goodwill impairment test, which requires a hypothetical purchase price allocation. Under ASU 2017-04, a goodwill impairment charge will now be recognized for the amount by which the carrying value of a reporting unit exceeds its fair value, not to exceed the carrying amount of goodwill. This guidance is effective for the System for annual periods beginning after December 15, 2021, with early adoption permitted for any impairment tests performed after January 1, 2017. The System has not completed the process of evaluating the impact of ASU 2017-04 on its consolidated financial statements.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows – Classification of Certain Cash Receipts and Cash Payments*, which addresses the following eight specific cash flow issues in order to limit diversity in practice: debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. The provisions of ASU 2016-15 are effective for the System for annual periods beginning after December 15, 2018 and interim periods thereafter. Early adoption is permitted. The System has not completed the process of evaluating the impact of ASU 2016-15 on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows – Restricted Cash*, which requires that the statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The provisions of ASU 2016-18 are effective for the System for annual periods beginning after December 15, 2018 and interim periods thereafter. Early adoption is permitted. The System has not completed the process of evaluating the impact of ASU 2016-18 on its consolidated financial statements.

In March 2017, the FASB issued ASU 2017-07, *Compensation – Retirement Benefits: Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. ASU 2017-07 addresses how employers that sponsor defined benefit pension and/or other postretirement benefit plans present the net periodic benefit cost in the income statement. Employers are required to present the service cost component of net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. Employers will present the other components of the net periodic benefit cost separately from the line item that includes the service cost and outside of any subtotal of operating income, if one is presented. The standard is effective for the System for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early adoption is permitted.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

Adoption of ASU 2017-07 will require the System to include the service cost component of net periodic benefit cost related to its defined benefit plan (approximately \$1.4 million and \$16.8 million for 2018 and 2017, respectively) within salaries and wages on the consolidated statements of operations and to present all other components (aggregate of approximately (\$4.0) million and \$8.2 million for 2018 and 2017, respectively) as a separate line item excluded from the subtotal for operating income (loss). Net periodic benefit cost is reported currently within employee benefits expense on the accompanying consolidated statements of operations.

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958); Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. ASU 2018-08 clarifies existing guidance in order to address diversity in practice in classifying grants (including governmental grants) and contracts received by not-for-profit entities, and requires entities to evaluate whether the resource provider receives commensurate value. In addition, the standard clarifies the guidance on how entities determine when a contribution is conditional, including whether the agreement includes a barrier (or barriers) that must be overcome for the recipient to be entitled to the transferred assets and a right of return of the transferred assets (or a right of release of the promisor's obligation to transfer the assets). The standard should be applied on a modified prospective basis to agreements that are not completed as of the effective date and to agreements entered into after the effective date. Retrospective application is permitted. ASU 2018-08 applies to all entities that make or receive contributions and is effective for the System for fiscal years beginning after June 15, 2018, including interim periods within those years. Early adoption is permitted. The System is in the process of evaluating the impact of ASU 2018-08 on its consolidated financial statements.

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

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

The standard also requires the customer to expense the capitalized implementation costs of a hosting arrangement that is a service contract over the term of the hosting arrangement. ASU 2018-15 is effective for the System for fiscal years beginning after December 15, 2020, and interim periods within fiscal years beginning after December 15, 2021. Early adoption is permitted, including adoption in any interim period. Either retrospective or prospective adoption is permitted. The System is in the process of evaluating the impact of ASU 2018-15 on its consolidated financial statements.

The FASB has amended certain guidance related to various disclosures in ASU No. 2018-09, *Codification Improvements*, ASU 2018-13, *Technical Corrections and Improvements to Financial Instruments—Overall (Subtopic 825-10)—Recognition and Measurement of Financial Assets and Financial Liabilities*, and ASU 2018-14, *Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20)—Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*. Among various provisions, ASU 2018-09 may result in additional assets included in an entity's fair value disclosure table if, among other criteria, net asset value has public visibility. ASU 2018-13 includes several disclosure changes involving transfers between the fair value levels and other updates related to fair value Level 3 investments. ASU 2018-13 also requires entities that use the practical expedient to measure the fair value of certain investments at their net asset values to disclose (1) the timing of liquidation of an investee's assets and (2) the date when redemption restrictions will lapse, but only if the investee has communicated this information to the entity or announced it publicly. The guidance in ASU 2018-14 requires all sponsors of defined benefit plans to provide certain new disclosures such as an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period. Among other changes, ASU No. 2018-14 eliminates the required disclosure for all sponsors of defined benefit plans to disclose the amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year. The updates noted above have effective dates as follows with early adoption permitted: ASU 2018-09: fiscal years beginning after December 15, 2018; ASU 2018-13: fiscal years beginning after December 15, 2019; and ASU 2018-14: fiscal years ending after December 15, 2021. The System has not completed the process of evaluating the impact of these ASUs on its consolidated financial statements.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*Reclassifications:* Certain reclassifications have been made to the 2017 amounts previously reported in order to conform to the current year presentation. These reclassifications had no impact on the previously reported net assets.

#### **2. Uncompensated Care**

Uncompensated care includes services provided to indigent persons who cannot afford health care due to inadequate resources and/or who are uninsured or underinsured. Uncompensated care is comprised of the costs of charity care for which state subsidies are not received (see Note 3), implicit price concessions or provision for bad debts, and the unpaid costs of care provided to beneficiaries of Medicaid and other indigent public programs.

The System provides charity care to patients who meet certain criteria defined by the New Jersey Department of Health (DOH) without charge or at amounts less than established rates. The System receives partial payment for the charity care it provides based upon the approved submission of patient claims once they are qualified for the program (see Note 3).

The estimated costs of charity care incurred by the System based on adjudicated claims was approximately \$58.8 million and \$53.0 million for years ended December 31, 2018 and 2017, respectively. The estimated cost of these charity care services was determined using a ratio of cost to gross charges and applying that ratio to the gross charges associated with providing care to charity patients for the period. Gross charges associated with providing care to charity patients include only the related charges for those patients who are financially unable to pay and qualify under the System's charity care policy and that do not otherwise qualify for payment from a governmental program. Because the collection of amounts determined to qualify as charity care is not pursued, it is not reported as revenue.

For the year ended December 31, 2018 and for services provided subsequent to the adoption of ASU 2014-09 on January 1, 2018, for uninsured patients who did not qualify for charity care the expected uncollected amounts are classified as an implicit price concession, based on a published financial assistance policy, which reduces net patient service revenue (\$88.6 million in 2018). For similar patient services provided prior to December 31, 2017 prior to the adoption of ASU 2014-09, the uncollected amounts were classified as provision for bad debts (\$81.4 million in 2017).



## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

*For Periods Commencing January 1, 2018*

Effective January 1, 2018 upon the adoption of ASU 2014-09, net patient service revenue is reported at the amount that reflects the consideration to which the System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payers (including health insurers and government programs), and others and includes variable consideration (reductions to revenue) for retroactive revenue adjustments due to settlement of ongoing and future audits, reviews, and investigations.

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

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

Generally, the System bills patients and third-party payers several days after the services are performed and/or the patient is discharged. Net patient service revenue is recognized as performance obligations are satisfied.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

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

As substantially all of its performance obligations relate to contracts with a duration of less than one year, the System has elected to apply the optional exemption provided in ASU 2014-09 and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period for patients who remain admitted at that time (in-house patients). The performance obligations for in-house patients are generally completed when the patients are discharged, which for the majority of the System's in-house patients occurs within days or weeks after the end of the reporting period.

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

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

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

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

Net patient service revenue for the year ended December 31, 2018 by major payer sources, based on primary insurance designation, is as follows (in thousands):

|  |                   |
|--|-------------------|
| Medicare   | \$ 272,411        |
| Medicaid   | 184,592           |
| Commercial carriers and managed care organizations | 253,370           |
| Self-pay   | 3,097             |
|  | <u>\$ 713,470</u> |

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

Net patient service revenue for the year ended December 31, 2018 by line of business is as follows (in thousands):

|                                |                   |
|--------------------------------|-------------------|
| Hospital                       | \$ 689,318        |
| Physician services             | 10,065            |
| Skilled nursing long-term care | 14,087            |
|                                | <u>\$ 713,470</u> |

The System has elected the practical expedient allowed under ASU 2014-09 and does not adjust the promised amount of consideration from patients and third-party payers for the effects of a significant financing component due to the System's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, the System does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

At December 31, 2018, accounts receivable is comprised of the following components (in thousands):

|                     |                  |
|---------------------|------------------|
| Patient receivables | \$ 71,090        |
| Contract assets     | <u>12,096</u>    |
|                     | <u>\$ 83,186</u> |

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

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

#### *For Periods Through December 31, 2017*

Prior to the adoption of ASU 2014-09, the System recognized patient service revenue at the estimated net realizable amounts associated with services provided to patients who have third-party payor coverage on the basis of contractual or formula-driven rates for the services rendered (see description of third-party payor payment programs below) and included estimated retroactive revenue adjustments due to ongoing and future audits, reviews and investigations. Under the System's policy for self-pay qualifying patients, a patient who had no insurance and was ineligible for any government assistance program had his or her bill reduced to an amount which would be billed to a commercially insured patient.

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

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

Patient service revenue for the year ended December 31, 2017, net of contractual allowances and discounts (but before the provision for bad debts), recognized from these major payer sources, based on primary insurance designation, is as follows (in thousands):

|                    |                   |
|--------------------|-------------------|
| Third-party payers | \$ 785,974        |
| Self-pay           | <u>3,010</u>      |
|                    | <u>\$ 788,984</u> |

Net patient service revenue (after contractual allowances and discounts) recognized during the year ended December 31, 2017 from the System's payer sources is as follows:

|                          |             |
|--------------------------|-------------|
|                          | <u>2017</u> |
| Medicare                 | 38%         |
| Medicaid                 | 27          |
| Managed care             | 23          |
| Other third-party payers | 11          |
| Self-pay                 | <u>1</u>    |
| Total                    | <u>100%</u> |

Deductibles, copayments and coinsurance under third-party payment programs within the self-pay and third-party payer amounts above are the patient's responsibility and the System considers these amounts in its determination of the provision for bad debts based on collection experience.

Patient accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the System analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. For receivables associated with services provided to patients who have third-party coverage, the System analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary. For receivables associated with self-pay patients, the System records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates and the

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts. The Medical Center's allowance for doubtful accounts for self-pay patients represented 84% of self-pay accounts receivable at December 31, 2017. The Medical Center did not change its charity care or uninsured discount policies during 2017.

#### *Third-Party Payment Programs*

The System provides care to patients under Medicare, Medicaid, and other third-party contractual arrangements. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. The Medicare program pays for most services at predetermined rates. However, certain services and specified expenses are reimbursed on a reasonable-cost basis. The New Jersey Medicaid program pays the Medical Center at predetermined rates for inpatient services. New Jersey Medicaid outpatient services are reimbursed on a reasonable cost basis. The System recognizes patient service revenue associated with services provided to patients who have other third-party payer coverage on the basis of contractual rates for the services rendered. The System has entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and PPOs. The basis for payment to the System under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

For uninsured patients that do not qualify for charity care, the System recognizes revenue on the basis of its standard rates for services provided or, if qualified, based on a discounted rate pursuant to the financial assistance policy.

Medicare and Medicaid regulations require annual retroactive settlements for cost-based reimbursements through cost reports filed by the System. These retroactive settlements are recorded in the consolidated financial statements in the year of the settlement or when amounts can be estimated. A portion of the accrual for estimated settlements with third-party payers has been classified as long-term because such amounts, by their nature or by virtue of regulation or legislation, are not expected to be paid within one year. The estimated settlements recorded at December 31, 2018 and 2017 could differ from actual settlements based on the results of cost report audits. At December 31, 2018, Medicare cost reports for all years through 2014, except 2010 and 2012, have been audited and settled. Medicaid cost reports have been audited and settled through 2014. Net patient service revenue was increased by approximately \$1.4 million during 2018 (none in 2017), as a result of changes in estimates of prior-year settlements.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

There are various proposals at the federal and state levels that could, among other things, significantly reduce payment rates or modify payment methods. The ultimate outcome of these proposals and other market changes, including the potential effects of or revisions to health care reform that has been or will be enacted by the federal or state governments, cannot presently be determined. Future changes in the Medicare and Medicaid programs and any reduction of funding could have an adverse impact on the System.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. The System is not aware of any pending or threatened investigations involving allegations of potential wrongdoing which could have a material adverse effect on the accompanying consolidated financial statements. Action for noncompliance may include repayment of amounts, fines, penalties, and exclusion from the Medicare and Medicaid programs.

#### *State Subsidy Funds*

The New Jersey Health Care Subsidy Fund was established for various purposes, including the distribution of charity care payments to hospitals statewide. The amount of the fund allocation is based on a formula using prior-year claim data for each hospital. Additionally, the State of New Jersey Delivery System Reform Incentive Payment Pool (the Pool) is available to certain hospitals that are able to establish performance improvement activities in one of eight specified clinical improvement areas. Amounts received from the Pool are subject to the satisfaction of certain performance criteria, with adjustments to the Pool allocations processed prospectively. The amounts of state subsidy and Pool funds included in net patient service revenue for the years ended December 31, 2018 and 2017 are as follows (in thousands):

|   | <u>2018</u>      | <u>2017</u>      |
|---|------------------|------------------|
| Charity care payments                     | \$ 38,285        | \$ 43,891        |
| Delivery system reform incentive payments | 12,237           | 8,821            |
|   | <u>\$ 50,522</u> | <u>\$ 52,712</u> |

The System expects to receive approximately \$17.5 million in charity care payments from the state for the period from January 1, 2019 to June 30, 2019. Amounts for payments subsequent to June 30, 2019 have yet to be determined by the State of New Jersey.

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**4. Investments, Assets Whose Use is Limited and Liquidity**

Investments and assets whose use is limited, stated at fair value, as of December 31, 2018 and 2017 consist of the following (in thousands):

|   | <u>2018</u>       | <u>2017</u>       |
|---|-------------------|-------------------|
| Investments                                       | \$ 233,738        | \$ 246,191        |
| Assets whose use is limited:                      |                   |                   |
| By bond indenture agreements                      | 15,254            | 18,430            |
| Assets held for captive insurance program         | 34,079            | 31,752            |
| Donor restricted assets                           | 15,833            | 13,778            |
| Total assets whose use is limited                 | <u>65,166</u>     | <u>63,960</u>     |
| Less current assets whose use is limited          | <u>18,114</u>     | <u>17,052</u>     |
| Noncurrent assets whose use is limited            | <u>47,052</u>     | <u>46,908</u>     |
| Total investments and assets whose use is limited | <u>\$ 298,904</u> | <u>\$ 310,151</u> |

The composition of investments and assets whose use is limited as of December 31, 2018 and 2017 is as follows (in thousands):

|   | <u>2018</u>       | <u>2017</u>       |
|---|-------------------|-------------------|
| Cash and cash equivalents                         | \$ 25,873         | \$ 27,449         |
| U.S. government securities and agency obligations | 59,254            | 84,201            |
| Corporate and foreign debt securities             | 148,065           | 181,609           |
| Asset-backed and mortgage-backed securities       | 7,189             | –                 |
| Marketable equity securities                      | 53,062            | 4,523             |
| Investments held by trustee                       | 1,578             | 1,578             |
| Municipal bonds                                   | 3,823             | 4,636             |
| Mutual funds – fixed income                       | 60                | 6,155             |
| Total   | <u>\$ 298,904</u> | <u>\$ 310,151</u> |



St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

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

Return on investments for the years ended December 31, 2018 and 2017 is as follows (in thousands):

|   | <u>2018</u>       | <u>2017</u>     |
|---|-------------------|-----------------|
| Return on investments:  |                   |                 |
| Net assets without donor restrictions:  |                   |                 |
| Investment return:  |                   |                 |
| Interest and dividend income  | \$ 8,833          | \$ 6,216        |
| Net realized gains and losses on sales of investments                             | (1,870)           | 33              |
|   | <u>6,963</u>      | <u>6,249</u>    |
| Change in net unrealized gains and losses on investments                          | (10,301)          | 1,118           |
|   | <u>(3,338)</u>    | <u>7,367</u>    |
| Net assets with donor restrictions:   |                   |                 |
| Investment income   | 18                | 15              |
| Net realized gains and losses on sales of investments                             | -                 | (1)             |
|   | <u>18</u>         | <u>14</u>       |
| Change in net unrealized gains and losses on investments held in perpetual trusts | (609)             | 428             |
|   | <u>(591)</u>      | <u>442</u>      |
| Total return on investments   | <u>\$ (3,929)</u> | <u>\$ 7,809</u> |

*Liquidity and Availability*

As of December 31, 2018, the System has a working capital surplus of \$258.4 million and days cash on hand of 125 (based on normal expenditures).

Financial assets available for general expenditure within one year of the balance sheet date consist of the following:

|                                    |                   |
|------------------------------------|-------------------|
| Cash and cash equivalents          | \$ 30,783         |
| Investments                        | 233,738           |
| Patient accounts receivable, net   | 83,186            |
| Physician services receivable, net | 4,673             |
|                                    | <u>\$ 352,380</u> |

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

#### **4. Investments, Assets Whose Use is Limited and Liquidity (continued)**

The System has assets for donor-restricted purposes, held under board indenture agreements and for the captive insurance program, which are not readily available for general expenditures.

Additionally, the System maintains a \$1.0 million line of credit, as described in Note 9. As of December 31, 2018, there was no balance outstanding on the line of credit. As of December 31, 2018, the System was in compliance with debt covenants.

#### **5. Fair Value of Financial Instruments**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A three-level hierarchy for fair value measurements exists based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

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

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

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**5. Fair Value of Financial Instruments (continued)**

The following tables present the financial instruments carried at fair value by caption on the consolidated balance sheets based on the valuation hierarchy defined above:

|   | December 31, 2018 |                   |                 |                   |
|---|-------------------|-------------------|-----------------|-------------------|
|   | Level 1           | Level 2           | Level 3         | Total             |
| Investments, assets whose use is limited and beneficial interest in perpetual trusts: |                   |                   |                 |                   |
| Cash and cash equivalents   | \$ 25,873         | \$ -              | \$ -            | \$ 25,873         |
| Marketable equity securities  | 53,062            | -                 | -               | 53,062            |
| U.S. government securities and agency obligations                                     | -                 | 59,254            | -               | 59,254            |
| Corporate and foreign debt securities   | -                 | 148,065           | -               | 148,065           |
| Asset-backed and mortgage-backed securities   | -                 | 7,189             | -               | 7,189             |
| Municipal bonds   | -                 | 3,823             | -               | 3,823             |
| Mutual funds – fixed income   | -                 | 60                | -               | 60                |
| Investments held by trustee   | -                 | 1,578             | -               | 1,578             |
| Beneficial interest in perpetual trusts   | -                 | -                 | 5,530           | 5,530             |
| Total   | <u>\$ 78,935</u>  | <u>\$ 219,969</u> | <u>\$ 5,530</u> | <u>\$ 304,434</u> |
| Assets held in pension plan:  |                   |                   |                 |                   |
| Cash and cash equivalents   | \$ 6,087          | \$ -              | \$ -            | \$ 6,087          |
| Marketable equity securities  | 185,856           | -                 | -               | 185,856           |
| U.S. government securities  | 49,153            | -                 | -               | 49,153            |
| Corporate bonds   | 64,002            | -                 | -               | 64,002            |
| Foreign obligations   | -                 | 5,013             | -               | 5,013             |
| Other debt securities   | -                 | 21,641            | -               | 21,641            |
|   | <u>\$ 305,098</u> | <u>\$ 26,654</u>  | <u>\$ -</u>     | <u>\$ 331,752</u> |
| Investments measured at net asset value:  |                   |                   |                 |                   |
| Fund of funds   |                   |                   |                 | 1,584             |
|   |                   |                   |                 | <u>\$ 333,336</u> |

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**5. Fair Value of Financial Instruments (continued)**

|   | December 31, 2017 |                   |                 |                   |
|---|-------------------|-------------------|-----------------|-------------------|
|   | Level 1           | Level 2           | Level 3         | Total             |
| Investments, assets whose use is limited and beneficial interest in perpetual trusts: |                   |                   |                 |                   |
| Cash and cash equivalents   | \$ 27,449         | \$ –              | \$ –            | \$ 27,449         |
| Marketable equity securities  | 4,523             | –                 | –               | 4,523             |
| U.S. government securities and agency obligations                                     | 889               | 83,312            | –               | 84,201            |
| Corporate and foreign debt securities   | –                 | 181,609           | –               | 181,609           |
| Municipal bonds   | –                 | 4,636             | –               | 4,636             |
| Mutual funds – fixed income   | –                 | 6,155             | –               | 6,155             |
| Investments held by trustee   | –                 | 1,578             | –               | 1,578             |
| Beneficial interest in perpetual trusts   | –                 | –                 | 6,139           | 6,139             |
| Total   | <u>\$ 32,861</u>  | <u>\$ 277,290</u> | <u>\$ 6,139</u> | <u>\$ 316,290</u> |
| Assets held in pension plan:  |                   |                   |                 |                   |
| Cash and cash equivalents   | \$ 1,740          | \$ –              | \$ –            | \$ 1,740          |
| Marketable equity securities  | 209,341           | –                 | –               | 209,341           |
| U.S. government securities  | 82,593            | –                 | –               | 82,593            |
| Corporate bonds   | 44,204            | –                 | –               | 44,204            |
| Foreign obligations   | –                 | 4,683             | –               | 4,683             |
| Other debt securities   | –                 | 10,086            | –               | 10,086            |
|   | <u>\$ 337,878</u> | <u>\$ 14,769</u>  | <u>\$ –</u>     | <u>\$ 352,647</u> |
| Investments measured at net asset value:  |                   |                   |                 |                   |
| Fund of funds   |                   |                   |                 | 1,853             |
|   |                   |                   |                 | <u>\$ 354,500</u> |

Fair value for Level 1 assets is based upon quoted market prices. Fair value for Level 2 assets is estimated based on quoted prices for similar instruments, pricing metrics, and other valuation considerations (e.g., credit quality and prevailing interest rates).

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**5. Fair Value of Financial Instruments (continued)**

Level 3 investments include the beneficial interest in perpetual trusts and fair value is determined based upon information provided by the trustees. Such information is based on the pro rata interest in the net assets of the trusts.

Attributes relating to the nature and risk of the fund of funds limited partnership investment as of December 31, 2018 and 2017 are as follows (in thousands):

|                              | <b>2018</b>       | <b>2017</b>       | <b>Unfunded</b>   | <b>Redemption</b> | <b>Other</b>      | <b>Redemption</b>    |
|------------------------------|-------------------|-------------------|-------------------|-------------------|-------------------|----------------------|
|                              | <b>Fair Value</b> | <b>Fair Value</b> | <b>Commitment</b> | <b>Frequency</b>  | <b>Redemption</b> | <b>Notice Period</b> |
| Assets held in pension plan: |                   |                   |                   |                   |                   |                      |
| Limited liability            |                   |                   |                   |                   |                   |                      |
| partnership – PMF            |                   |                   |                   |                   | Discretion of     | Discretion of        |
| TEI Fund                     | <u>\$ 1,584</u>   | <u>\$ 1,853</u>   | None              | Illiquid          | Fund              | Fund                 |

The PMF TEI Fund operates as a feeder fund. The PMF TEI Fund's investment objective is to manage a portfolio of investment funds, including limited partnerships, limited liability companies, offshore corporations, other foreign investment vehicles, and cash to preserve value while prioritizing liquidity to investors over active management, until such time as a related portfolio has been liquidated.

There were no transfers between levels of the System's or the Plan's investments for the years ended December 31, 2018 and 2017.

The change in fair value measurements for the beneficial interest in perpetual trusts with unobservable inputs at December 31, 2018 and 2017 are presented as follows (in thousands):

|   | <b>2018</b>     | <b>2017</b>     |
|---|-----------------|-----------------|
| Balance – January 1                       | \$ 6,139        | \$ 5,711        |
| Change in net unrealized gains and losses | (609)           | 428             |
| Balance – December 31                     | <u>\$ 5,530</u> | <u>\$ 6,139</u> |

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**6. Property and Equipment**

Property and equipment as of December 31, 2018 and 2017 consist of the following (in thousands):

|  | <u>2018</u>              | <u>2017</u>       |
|--|--------------------------|-------------------|
| Land   | \$ 12,008                | \$ 11,831         |
| Land improvements                              | 8,607                    | 8,602             |
| Buildings and improvements                     | 471,237                  | 468,708           |
| Fixed and major movable equipment              | <u>333,346</u>           | <u>263,403</u>    |
| Total property and equipment                   | <b>825,198</b>           | 752,544           |
| Less accumulated depreciation and amortization | <u>(483,654)</u>         | <u>(450,122)</u>  |
|  | <b>341,544</b>           | 302,422           |
| Construction in progress                       | <u>24,707</u>            | <u>33,542</u>     |
| Property and equipment – net                   | <u><b>\$ 366,251</b></u> | <u>\$ 335,964</u> |

The System recorded capitalized interest of approximately \$2.1 million in 2018 (none in 2017).

As of December 31, 2018, the System completed a significant phase of its installation of a new electronic health record system. Substantially, all property of the Medical Center serves as collateral under debt agreements (see Note 9).

**7. Goodwill and Other Intangible Asset**

In 2010, the System recorded goodwill and an intangible asset in connection with the acquisition of two radiology practices. At December 31, 2018 and 2017, goodwill was approximately \$2.1 million. The intangible asset is fully amortized. Goodwill is included in other assets in the accompanying consolidated balance sheets.

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**8. Equity Investments in Joint Ventures**

The System's investments in unconsolidated entities accounted for under the equity method of accounting as of December 31, 2018 and 2017 consist of the following (in thousands):

| Name of Joint Venture     | Ownership Percentage | 2018             |                   |                  |                 |                   |                   |
|---------------------------|----------------------|------------------|-------------------|------------------|-----------------|-------------------|-------------------|
|                           |                      | Total Assets     | Total Liabilities | Total Revenue    | Net Income      | Equity Investment | Share of Earnings |
| Simeon Dialysis, LLC      | 35%                  | \$ 66,096        | \$ 931            | \$ 25,459        | \$ 5,165        | \$ 22,808         | \$ 1,808          |
| Wayne Valley Imaging, LLC | 50%                  | 1,092            | 29                | 2,166            | 755             | 557               | 378               |
| VHSNJ at Home, LLC        | 50%                  | 11,182           | 3,161             | 13,660           | 506             | 4,011             | 253               |
| Eufaula Dialysis, LLC     | 20%                  | 5,373            | 437               | 8,484            | 1,695           | 987               | 339               |
|                           |                      | <u>\$ 83,743</u> | <u>\$ 4,558</u>   | <u>\$ 49,769</u> | <u>\$ 8,121</u> | <u>\$ 28,363</u>  | <u>\$ 2,778</u>   |

| Name of Joint Venture     | Ownership Percentage | 2017             |                   |                  |                 |                   |                   |
|---------------------------|----------------------|------------------|-------------------|------------------|-----------------|-------------------|-------------------|
|                           |                      | Total Assets     | Total Liabilities | Total Revenue    | Net Income      | Equity Investment | Share of Earnings |
| Simeon Dialysis, LLC      | 35%                  | \$ 64,941        | \$ 757            | \$ 22,885        | \$ 4,327        | \$ 22,464         | \$ 1,515          |
| Wayne Valley Imaging, LLC | 50%                  | 1,161            | 279               | 2,226            | 780             | 479               | 390               |
| VHSNJ at Home, LLC        | 50%                  | 10,723           | 3,208             | 5,639            | (485)           | 3,758             | (242)             |
| Eufaula Dialysis, LLC     | 20%                  | 4,633            | 350               | 6,013            | 626             | 857               | 125               |
|                           |                      | <u>\$ 81,458</u> | <u>\$ 4,594</u>   | <u>\$ 36,763</u> | <u>\$ 5,248</u> | <u>\$ 27,558</u>  | <u>\$ 1,788</u>   |

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**9. Long-Term Debt**

Long-term debt as of December 31, 2018 and 2017 consists of the following (in thousands):

|   | <u>2018</u>       | <u>2017</u>       |
|---|-------------------|-------------------|
| New Jersey Healthcare Facilities Financing Authority – \$246,845 St. Joseph's Healthcare System Obligated Group Issue, Series 2016 Revenue Bonds <sup>(a)</sup> | \$ 238,040        | \$ 241,740        |
| St. Joseph's Hospital and Medical Center – \$81,200 St. Joseph's Healthcare System Obligated Group, Series 2017 Taxable Bonds <sup>(b)</sup>                    | 81,200            | 81,200            |
| Passaic Authority – \$29,620 200 Hospital Plaza Corporation Project, Series 2010 County Guaranteed Parking Revenue Bonds <sup>(c)</sup>                         | 1,360             | 2,015             |
| Passaic Authority – \$24,650 200 Hospital Plaza Corporation Project, Series 2017 County Guaranteed Parking Revenue Bonds <sup>(d)</sup>                         | 24,505            | 24,650            |
| Promissory note with Urban Enterprise Zone, bearing interest at 2.25%, maturing in 2021   | 150               | 350               |
| Promissory note bearing interest of 6.04%, maturing in 2020 <sup>(e)</sup>  | 1,770             | 2,895             |
| Capital lease <sup>(f)</sup>  | 2,310             | –                 |
| Term loan bearing interest at a rate of 6.5%, maturing in 2020  | –                 | 397               |
| Total long-term debt  | <u>349,335</u>    | <u>353,247</u>    |
| Original issue premium  | 26,353            | 29,419            |
| Original issue discount   | (2,142)           | (2,258)           |
| Net deferred financing costs  | (2,128)           | (2,315)           |
| Current portion of long-term debt   | (5,755)           | (5,882)           |
| Long-term debt – net of current portion of long-term debt   | <u>\$ 365,663</u> | <u>\$ 372,211</u> |



## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

- (a) The New Jersey Health Care Facilities Financing Authority (NJHCFFA) Series 2016 Revenue Bonds (the Series 2016 Bonds) bear interest at rates ranging from 3.00% to 5.00%. The Series 2016 Bonds mature annually, commencing July 1, 2017 through July 1, 2048. The proceeds of the Series 2016 Bonds were used by the System to advance refund the outstanding principal balance of NJHCFFA Series 2008 Bonds and the (a) renovation of inpatient nursing care units; (b) renovation and equipment upgrades within ambulatory surgery and neuro-interventional suites; (c) build out of clinic facilities; and (d) upgrade and installation of information technology systems for clinical information systems, pharmaceutical dispensing technology, imaging and other minor equipment.
- (b) The St. Joseph's Hospital and Medical Center Series 2017 Taxable Bonds (the Series 2017 Bonds) were issued in September 2017 and consist of two term bonds of \$40.6 million, which bear interest at 3.926% and 4.584% and are due at July 1, 2022 and July 1, 2027, respectively. The proceeds of the Series 2017 Bonds were used to provide funding for additional contributions to the defined benefit pension plan (see Note 10). The Series 2017 Bonds are secured by a Series 2017 Note which was issued on a parity with other obligations under the Master Indenture for the Series 2016 Bonds.
- (c) The Passaic Authority Series 2010 County Guaranteed Parking Revenue Bonds (the Series 2010 Bonds) bear interest at rates ranging from 2% to 5%. The Series 2010 Bonds were scheduled to mature between 2014 and 2042; a portion of the Series 2010 Bonds was advance refunded in 2017 (see (d) below). Funds were paid into escrow to repay the debt through the final redemption date in May 2020. The proceeds of the Series 2010 Bonds were used by 200 Hospital Plaza to finance a portion of project costs associated with the design and construction of a mixed-use parking/retail structure. 200 Hospital Plaza is subject to certain operating covenants under its Master Indenture Agreement and the maintenance of certain financial ratios. At December 31, 2018 and 2017, 200 Hospital Plaza was in compliance with such financial covenants.
- (d) The Passaic Authority Series 2017 County Guaranteed Parking Revenue Bonds (the PA Series 2017 Bonds) bear interest at rates ranging from 2% to 5%. The PA Series 2017 Bonds mature between 2018 and 2042. The proceeds of the PA Series 2017 Bonds were used by 200 Hospital Plaza to advance refund the Series 2010 Bonds and pay certain costs of issuance relating to the PA Series 2017 Bonds.

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

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

- (e) Surgery Management entered into a loan agreement to purchase equipment and to make leasehold improvements to the surgical facility. On June 1, 2015, the amount advanced was converted to a loan payable over a five-year period bearing interest equal to the five-year US Treasury rate of 3.79% plus 2.25%. The loan is collateralized by substantially all of the assets of Surgery Management and guaranteed by all members as contained in the loan agreement. The System is not a guarantor of this loan. The loan is subject to a debt service coverage ratio, which is tested annually. Management is not aware of any noncompliance with this ratio as of December 31, 2018 and 2017.
- (f) The System has guaranteed an equipment lease for a joint venture in the amount of \$2.3 million at December 31, 2018.

The Series 2016 Bonds and Series 2017 Bonds are secured by (i) amounts held in the revenue fund created under the Master Indenture Agreement, (ii) the gross receipts of the Obligated Group (see Note 1), and (iii) a first mortgage lien on various properties of the University Medical Center and Wayne Medical Center as defined in the Master Indenture Agreement. The Obligated Group is subject to various operating covenants under the Master Indenture Agreement and maintenance of certain financial ratios. At December 31, 2018 and 2017, the Obligated Group was in compliance with such financial covenants.

Required principal payments on long-term debt for the next five years and thereafter as of December 31, 2018 are as follows (in thousands):

| <b>Years Ending December 31</b> |                   |
|---------------------------------|-------------------|
| 2019                            | \$ 6,553          |
| 2020                            | 6,165             |
| 2021                            | 5,556             |
| 2022                            | 45,895            |
| 2023                            | 5,045             |
| Thereafter                      | 280,121           |
|                                 | <u>\$ 349,335</u> |

At December 31, 2018, the System has unused letters of credit of: \$0.7 million, expiring in March 2020; \$1.3 million, expiring in January 2020; \$2.4 million, expiring in January 2020; \$1.7 million expiring in January 2020; \$1.1 million expiring in January 2020; and \$0.3 million, expiring in February 2020.

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

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

The System maintains a line of credit (currently with an available amount of \$1.0 million) which expires in February 2020, with interest at LIBOR plus 0.75%. There are no amounts outstanding as of December 31, 2018 and 2017.

#### **10. Pension Plans**

The Medical Center maintains a noncontributory defined benefit pension plan (the Plan) covering substantially all of the employees of the Medical Center as well as an executive SERP plan. The Plan provides benefits based on the participant's years of service and compensation. The Plan is operated as a church plan under the Code. Under church plan status, the Plan is not subject to the minimum funding or other requirements of the Employee Retirement Income Security Act of 1974. In addition, benefits under the Plan are not covered by the Pension Benefit Guaranty Corporation.

The Medical Center has been involved with litigation challenging the church plan status of the Plan which was settled in 2018. The settlement does not make the Plan subject to ERISA.

The System issued long-term debt in September 2017 (see Note 9) with net proceeds of approximately \$80.0 million, the purpose of which was to provide funding for additional contributions paid into the Plan. In addition to the 2017 funding into the Plan, management froze the Plan and closed it to new participants effective December 31, 2017, initiated a defined contribution retirement program on January 1, 2018, and intends to continue annual funding to the Plan so that in conjunction with investment earnings thereon, the plan assets will exceed the projected benefit obligation by the year 2026. As a result of freezing the Plan, a curtailment occurred in 2017 which reduced the projected benefit obligation by approximately \$30.3 million.

The Medical Center contributed approximately \$15.0 million to the Plan in 2018 and expects to contribute approximately \$6.0 million to the Plan in 2019.

The defined contribution plan established January 1, 2018 provides for annual contributions for eligible employees of between 2% and 5% of pay based on the employee's years of service with a matching contribution of 1% to 1.5%. Eligible employees begin to accrue benefits from their hire or rehire date. The System funds the defined contribution expense on a current basis. The Medical Center contributed \$10.5 million to the defined contribution plan in 2018.

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**10. Pension Plans (continued)**

The funded status of the Plan as of December 31, 2018 and 2017 is set forth as follows (in thousands):

|  | <u>2018</u>       | <u>2017</u>       |
|--|-------------------|-------------------|
| Change in benefit obligation:                    |                   |                   |
| Projected benefit obligation – beginning of year | \$ 465,927        | \$ 440,123        |
| Service cost and administrative expenses         | 1,368             | 16,806            |
| Interest cost                                    | 18,547            | 19,664            |
| Actuarial (gain) loss                            | (36,201)          | 34,907            |
| Benefit payments and expected expenses           | (16,027)          | (15,271)          |
| Curtailment                                      | –                 | (30,302)          |
| Projected benefit obligation – end of year       | <u>433,614</u>    | <u>465,927</u>    |
| Change in Plan assets:                           |                   |                   |
| Fair value of Plan assets – beginning of year    | 354,500           | 237,112           |
| Actual return on Plan assets                     | (20,548)          | 39,061            |
| Employer contributions                           | 15,000            | 93,800            |
| Benefit payments and actual expenses             | (15,616)          | (15,473)          |
| Fair value of Plan assets – end of year          | <u>333,336</u>    | <u>354,500</u>    |
| Accrued pension liability                        | <u>\$ 100,278</u> | <u>\$ 111,427</u> |
| Accumulated benefit obligation                   | <u>\$ 433,614</u> | <u>\$ 465,927</u> |

At December 31, 2018 and 2017, net assets without donor restrictions include unrecognized losses of \$106.8 million and \$100.4 million, respectively. Approximately \$2.0 million of unrecognized losses are expected to be recognized in net periodic benefit costs in 2019.

At December 31, 2018 and 2017, the mortality assumption was determined using the RP-2014 mortality tables with blue collar adjustments adjusted backwards to 2006 with scale MP-2014 and projected with improvement scales (2018: MP-2018; 2017: MP-2017).

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**10. Pension Plans (continued)**

Weighted-average assumptions used in determining the benefit obligation as of December 31, 2018 and 2017 were as follows:

|                               | <u>2018</u> | <u>2017</u> |
|-------------------------------|-------------|-------------|
| Discount rate                 | 4.64%       | 4.03%       |
| Rate of compensation increase | N/A         | N/A         |

Net periodic pension (benefit) cost for the years ended December 31, 2018 and 2017 are as follows (in thousands):

|  | <u>2018</u>       | <u>2017</u>      |
|--|-------------------|------------------|
| Service cost and administrative expenses | \$ 1,368          | \$ 16,806        |
| Interest cost                            | 18,547            | 19,664           |
| Expected return on Plan assets           | (24,285)          | (19,251)         |
| Amortization of prior service cost       | -                 | 87               |
| Amortization of net loss                 | 1,778             | 7,713            |
| Net periodic pension (benefit) cost      | <u>\$ (2,592)</u> | <u>\$ 25,019</u> |

Weighted-average assumptions used in determining the net periodic pension costs for the years ended December 31, 2018 and 2017 were as follows:

|  | <u>2018</u> | <u>2017</u> |
|--|-------------|-------------|
| Discount rate                            | 4.03%       | 4.53%       |
| Expected long-term return on Plan assets | 6.75        | 7.25        |
| Rate of compensation increase            | N/A         | 3.00        |

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**10. Pension Plans (continued)**

The discount rate was determined using the hypothetical portfolio method at December 31, 2018 and 2017.

To develop the expected long-term rate of return on Plan assets, the System considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio. This approach resulted in the selection of the 6.75% and 7.25% long-term rate of return on Plan assets' assumption for 2018 and 2017, respectively.

The date used to determine the Plan's measurements is December 31.

The Plan's weighted-average asset allocation as of December 31, 2018 and 2017, by asset category, is as follows:

| <b>Asset Category</b>   | <b>2018</b> | <b>2017</b> |
|-------------------------|-------------|-------------|
| Equity securities       | 57          | 59%         |
| Debt securities         | 43          | 40          |
| Alternative investments | —           | 1           |
|                         | <b>100%</b> | <b>100%</b> |

The Plan's investment policy includes the following asset allocation guidelines:

| <b>Asset Category</b>   | <b>Target</b> | <b>Range</b> |
|-------------------------|---------------|--------------|
| Domestic equity         | 35.0%         | 6-36%        |
| International equity    | 23.0          | 4-24         |
| Fixed income            | 40.0          | 40-90        |
| Alternative investments | 2.0           | 0-5          |

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

#### 10. Pension Plans (continued)

The asset allocation policy was developed in consideration of the long-term financial objectives of the Plan, which include ensuring that there is an adequate level of assets to support benefit obligations and maintaining liquidity sufficient to cover current benefit obligations.

In addition to the broad asset allocation guidelines described above, the following policies apply to individual asset classes:

- Fixed-income investments are oriented toward risk-adverse, investment-grade securities with an average quality of "A" or higher. Up to 10% of the portfolio may be invested in bonds rated below investment grade. With the exception of US government securities, fixed-income investments are diversified among individual securities and sectors.
- Equity investments are diversified among industries and economic sectors. International equity holdings are also diversified by country. Limitations are placed on the overall allocation to any individual security.

Pension benefit payments, which reflect expected future service and salary, as appropriate, are expected to be paid as follows (in thousands):

| <b>Years Ending December 31</b> |           |
|---------------------------------|-----------|
| 2019                            | \$ 17,435 |
| 2020                            | 18,916    |
| 2021                            | 20,260    |
| 2022                            | 21,470    |
| 2023                            | 22,656    |
| 2024–2028                       | 126,244   |

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

#### **11. Professional Liability Insurance**

Effective February 1, 2007, the Insurance Captive began providing the University Medical Center with claims-made professional and general liability insurance. The Insurance Captive policy provides coverage of \$1 million per occurrence and \$3 million annual aggregate. The Insurance Captive has a self-insurance program for a first excess layer above the primary layer. The first excess layer is on a claims-made basis with retentions of \$4 million for individual claims and \$17 million in the aggregate. The Insurance Captive maintains a self-insurance reserve trust as the funding vehicle for the self-insurance program (see Note 4). The Insurance Captive has a second excess layer of insurance of \$10 million annual aggregate, a third excess layer of insurance of \$20 million annual aggregate, and a fourth layer of \$15 million annual aggregate each maintained with separate commercial carriers.

The Insurance Captive is registered under the Bermuda Insurance Act of 1978 and the Related Regulations (the Insurance Act) and is obliged to comply with various provisions of the Insurance Act regarding solvency and liquidity. The minimum statutory capital and surplus at December 31, 2018 and 2017 was \$3.1 million and \$2.7 million, respectively, and the actual statutory capital and surplus was \$1.9 million and \$4.8 million, respectively. As the actual statutory capital and surplus was less than the minimum requirement at December 31, 2018, the Insurance Captive will receive additional loss funding contributed by the System in 2019 to restore the statutory compliance regarding solvency. In addition, a minimum liquidity ratio must be maintained whereby relevant assets, as defined by the Insurance Act, must exceed 75% of relevant liabilities. As of December 31, 2018 and 2017, the liquidity ratio was met.

Prior to the inception of the Insurance Captive, the University Medical Center maintained its primary professional liability insurance coverage of \$1 million for individual claims and \$3 million in the aggregate on a claims-made basis with a commercial carrier. The first excess layer was on a claims-made basis with retentions of \$4 million for individual claims and \$7 million in the aggregate. A second excess layer of coverage was maintained with a commercial carrier.

Effective March 1, 2009, the Insurance Captive began providing Wayne Medical Center with claims-made professional and general liability insurance, and Wayne Medical Center began participating in the self-insurance program for a first excess layer above the primary layer. Prior to March 1, 2009, Wayne Medical Center maintained primary professional liability insurance coverage on a claims-made basis with a commercial carrier.



St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**11. Professional Liability Insurance (continued)**

The estimated undiscounted professional liabilities for asserted claims and for incidents that have been incurred but not reported included in the consolidated balance sheets as of December 31, 2018 and 2017 are as follows (in thousands):

|   | <u>2018</u>      | <u>2017</u>      |
|---|------------------|------------------|
| Estimated professional liability claims payable,<br>included in accrued salaries and expenses | \$ 7,225         | \$ 6,762         |
| Noncurrent estimated professional liability claims payable                                    | <u>32,412</u>    | <u>27,423</u>    |
| Total estimated professional liability claims payable   | <u>\$ 39,637</u> | <u>\$ 34,185</u> |

The System's estimates for professional liability for asserted claims and for incidents that have been incurred but not reported are based upon complex actuarial calculations, which utilize factors such as historical claim experience for the System and related industry factors, trending models, estimates for the payment patterns of future claims, and present value discounting factors. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Revisions to estimated amounts resulting from actual experience differing from project expectations are recorded in the period the information becomes known.

**12. Concentrations of Credit Risk**

The System grants credit without collateral to its patients, most of whom are insured under third-party payer agreements. Major concentrations of net accounts receivable from patients and third-party payers as of December 31, 2018 and 2017 are as follows:

|  | <u>2018</u> | <u>2017</u> |
|--|-------------|-------------|
| Medicare   | 20%         | 14%         |
| Medicaid   | 9           | 9           |
| Horizon Blue Cross Blue Shield of New Jersey               | 2           | 9           |
| Amerigroup   | 4           | 6           |
| Aetna  | 4           | 4           |
| Managed care organizations and other<br>third-party payers | 57          | 54          |
| Self-pay patients  | 4           | 4           |
|  | <u>100%</u> | <u>100%</u> |

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**12. Concentrations of Credit Risk (continued)**

The System invests its surplus operating funds in fixed-income funds. These funds generally invest in highly liquid U.S. government and agency obligations. Investments in fixed-income funds are not insured or guaranteed by the U.S. government. The System deposits cash with various financial institutions in which the amounts may exceed federally insured limits.

**13. Other Revenue**

Other revenue at December 31, 2018 and 2017 consists of the following (in thousands):

|   | <u>2018</u>      | <u>2017</u>      |
|---|------------------|------------------|
| Physician billing revenue   | \$ 51,044        | \$ 50,921        |
| Grant income  | 13,336           | 14,964           |
| Gain on sale of certain assets and business operations of<br>VHS Management, Inc. | –                | 8,000            |
| Qualcare sale of stock  | 322              | 1,867            |
| Equity in earnings of joint ventures  | 2,778            | 1,788            |
| Rental income   | 3,597            | 3,757            |
| Accountable care organization gainsharing   | 6,798            | –                |
| Parking revenue   | 4,060            | 3,870            |
| Contributions   | 2,516            | 2,429            |
| Fundraising   | 5,052            | 4,505            |
| Other   | 3,923            | 1,021            |
| Total   | <u>\$ 93,426</u> | <u>\$ 93,122</u> |

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

#### 14. Operating Leases

The System leases equipment and office space under various noncancelable operating leases. Future minimum payments due under noncancelable operating leases with a term of one year or greater as of December 31, 2018 are as follows (in thousands):

|            |    |       |
|------------|----|-------|
| 2019       | \$ | 4,758 |
| 2020       |    | 4,185 |
| 2021       |    | 3,004 |
| 2022       |    | 2,536 |
| 2023       |    | 2,458 |
| Thereafter |    | 7,998 |

Payments made under operating leases amounted to approximately \$6.0 million in 2018 and \$5.6 million in 2017.

#### 15. Net Assets With Donor Restrictions

Net assets with donor restrictions which are available for future periods or for specific purposes as of December 31, 2018 and 2017 are available for the following purposes (in thousands):

|                                       | <u>2018</u>      | <u>2017</u>      |
|---------------------------------------|------------------|------------------|
| Capital acquisitions and improvements | \$ 726           | \$ 1,748         |
| Scholarship fund                      | 75               | 82               |
| Research                              | 954              | 1,210            |
| Other health care programs            | 9,131            | 10,825           |
|                                       | <u>\$ 10,886</u> | <u>\$ 13,865</u> |

At December 31, 2018 and 2017, net assets with donor restrictions for permanent endowment in the amount of \$7.5 million and \$8.1 million, respectively, consist of endowment funds to be held in perpetuity, and the beneficial interest in perpetual trusts. The assets in the perpetual trusts are held and managed by an independent trustee. The income earned on the beneficial interest in the perpetual trusts does not have donor restrictions. The income from the endowment funds is expendable to support health care services.

St. Joseph's Health, Inc.

Notes to Consolidated Financial Statements (continued)

**15. Net Assets With Donor Restrictions (continued)**

The Board classifies donor-restricted assets based upon the explicit directions of the donor and the provisions of the New Jersey Uniform Prudent Management of Institutional Funds Act (UPMIFA). The Board has determined that, absent donor stipulations to the contrary, the provisions of New Jersey State law do not impose a donor restriction on the income or capital appreciation derived from the original gift.

**16. Functional Expenses**

The System's functional expenses for the years ended December 31, 2018 and 2017 are as follows (in thousands):

|                               | <b>2018</b>                                 |  |                           |
|-------------------------------|---|--|---------------------------|
|                               | <b>Health Care<br/>Program<br/>Expenses</b> | <b>General and<br/>Administrative<br/>Expenses</b> | <b>Total<br/>Expenses</b> |
| Salaries and wages            | \$ 332,383                                  | \$ 53,372  | \$ 385,755                |
| Employee benefits             | 61,559                                      | 9,897  | 71,456                    |
| Physician fees                | 19,516                                      | 3,077  | 22,593                    |
| Supplies and other            | 280,853                                     | –  | 280,853                   |
| Interest                      | 10,284                                      | 1,480  | 11,764                    |
| Depreciation and amortization | 29,485                                      | 4,395  | 33,880                    |
|                               | <b>\$ 734,080</b>                           | <b>\$ 72,221</b>                                   | <b>\$ 806,301</b>         |

|                               | <b>2017</b>                                 |  |                           |
|-------------------------------|---|--|---------------------------|
|                               | <b>Health Care<br/>Program<br/>Expenses</b> | <b>General and<br/>Administrative<br/>Expenses</b> | <b>Total<br/>Expenses</b> |
| Salaries and wages            | \$ 330,360                                  | \$ 53,048  | \$ 383,408                |
| Employee benefits             | 74,295                                      | 11,944   | 86,239                    |
| Physician fees                | 19,106                                      | 3,013  | 22,119                    |
| Supplies and other            | 271,551                                     | –  | 271,551                   |
| Interest                      | 12,363                                      | 1,779  | 14,142                    |
| Depreciation and amortization | 28,994                                      | 4,322  | 33,316                    |
|                               | <b>\$ 736,669</b>                           | <b>\$ 74,106</b>                                   | <b>\$ 810,775</b>         |

## St. Joseph's Health, Inc.

### Notes to Consolidated Financial Statements (continued)

#### **17. Commitments and Contingencies**

Various lawsuits and claims arising in the normal course of operations are pending or are in progress against the System. Such lawsuits and claims are either specifically covered by insurance, provided for through estimated self-insurance liabilities, or are not material. While the outcome of these lawsuits cannot be determined at this time, management believes that any loss, which may arise from these actions will not have a material adverse effect on the consolidated financial position or results of operations of the System.

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

The System has evaluated subsequent events through May 23, 2019, the date the accompanying consolidated financial statements were issued. Except as disclosed in Note 1, no subsequent events have occurred that require disclosure in or adjustment to the consolidated financial statements.

## Supplementary Information

## St. Joseph's Health, Inc.

### Consolidating Balance Sheet (In Thousands)

December 31, 2018

|  | St. Joseph's<br>University Medical<br>Center and<br>Subsidiaries | St. Joseph's Hospital<br>and Medical Center<br>Foundation, Inc. | St. Joseph's<br>Wayne Hospital<br>Foundation, Inc. | VHS<br>Management,<br>Inc. and<br>Subsidiary | 200 Hospital<br>Plaza Corp. | St. Joseph's<br>Health, Inc. | SJHS Insurance<br>Limited | Eliminations | Total      |
|--|--|---|--|--|-----------------------------|------------------------------|---------------------------|--------------|------------|
| <b>Assets</b>                                      |  |   |  |  |                             |                              |                           |              |            |
| Current assets:                                    |  |   |  |  |                             |                              |                           |              |            |
| Cash and cash equivalents                          | \$ 28,002  | \$ 1,634  | \$ 689   | \$ 258                                       | \$ 200                      | \$ -                         | \$ -                      | \$ -         | \$ 30,783  |
| Investments  | 227,576  | 3,170   | 2,992  | -  | -                           | -                            | -                         | -            | 233,738    |
| Current portion of assets whose use is limited     | 9,123  | -   | -  | -  | 1,766                       | -                            | 7,225                     | -            | 18,114     |
| Patient accounts receivable, net                   | 83,186   | -   | -  | -  | -                           | -                            | -                         | -            | 83,186     |
| Contributions and pledges receivable               | -  | 992   | 44   | -  | -                           | -                            | -                         | -            | 1,036      |
| Prepaid expenses and other current assets          | 35,462   | 35  | 7  | -  | 254                         | -                            | 1,455                     | (1,146)      | 36,067     |
| Due from affiliates                                | 402  | -   | 135  | -  | -                           | -                            | -                         | (537)        | -          |
| Total current assets                               | 383,751  | 5,831   | 3,867  | 258  | 2,220                       | -                            | 8,680                     | (1,683)      | 402,924    |
| Assets whose use is limited – less current portion | 12,519   | 4,264   | 908  | -  | 2,507                       | -                            | 26,854                    | -            | 47,052     |
| Property and equipment – net                       | 343,689  | -   | -  | -  | 22,562                      | -                            | -                         | -            | 366,251    |
| Beneficial interest in perpetual trusts            | -  | 4,767   | 763  | -  | -                           | -                            | -                         | -            | 5,530      |
| Equity investments in joint ventures               | 28,396   | -   | -  | -  | -                           | -                            | -                         | -            | 28,396     |
| Other noncurrent assets                            | 41,964   | 979   | 87   | -  | -                           | 3,178                        | -                         | (34,577)     | 11,631     |
| Total assets                                       | \$ 810,319   | \$ 15,841   | \$ 5,625   | \$ 258                                       | \$ 27,289                   | \$ 3,178                     | \$ 35,534                 | \$ (36,260)  | \$ 861,784 |

*The System presents its interests in its controlled affiliates using the cost method of accounting.*

St. Joseph's Health, Inc.

Consolidating Balance Sheet (continued)  
(In Thousands)

December 31, 2018

|   | St. Joseph's<br>University Medical<br>Center and<br>Subsidiaries | St. Joseph's Hospital<br>and Medical Center<br>Foundation, Inc. | St. Joseph's<br>Wayne Hospital<br>Foundation, Inc. | VHS<br>Management,<br>Inc. and<br>Subsidiary | 200 Hospital<br>Plaza Corp. | St. Joseph's<br>Health, Inc. | SJHS Insurance<br>Limited | Eliminations | Total      |
|---|--|---|--|--|-----------------------------|------------------------------|---------------------------|--------------|------------|
| <b>Liabilities and net assets</b>   |  |   |  |  |                             |                              |                           |              |            |
| Current liabilities:  |  |   |  |  |                             |                              |                           |              |            |
| Current portion of long-term debt   | \$ 5,085   | \$ -  | \$ -   | \$ -   | \$ 670                      | \$ -                         | \$ -                      | \$ -         | \$ 5,755   |
| Accounts payable  | 51,478   | 66  | 26   | -  | 8                           | -                            | 2,039                     | (1,138)      | 52,479     |
| Accrued salaries and expenses   | 70,087   | -   | -  | 18   | -                           | -                            | 7,225                     | -            | 77,330     |
| Accrued interest payable  | 7,032  | -   | -  | -  | 178                         | -                            | -                         | -            | 7,210      |
| Due to affiliates   | -  | 337   | 59   | -  | 149                         | -                            | -                         | (545)        | -          |
| Deferred revenue  | 974  | 64  | -  | -  | -                           | -                            | -                         | -            | 1,038      |
| Current portion of estimated third-party<br>payer settlements               | 762  | -   | -  | -  | -                           | -                            | -                         | -            | 762        |
| Total current liabilities   | 135,418  | 467   | 85   | 18   | 1,005                       | -                            | 9,264                     | (1,683)      | 144,574    |
| Long-term debt – net of current portion                                     | 338,991  | -   | -  | -  | 26,672                      | -                            | -                         | -            | 365,663    |
| Estimated third-party payer settlements – net of<br>current portion         | 9,394  | -   | -  | -  | -                           | -                            | -                         | -            | 9,394      |
| Accrued pension liability   | 100,278  | -   | -  | -  | -                           | -                            | -                         | -            | 100,278    |
| Estimated professional liability claims payable –<br>net of current portion | 18,754   | -   | -  | -  | -                           | -                            | 24,301                    | (10,643)     | 32,412     |
| Other liabilities   | 10,687   | 79  | -  | -  | 104                         | -                            | -                         | -            | 10,870     |
| Total liabilities   | 613,522  | 546   | 85   | 18   | 27,781                      | -                            | 33,565                    | (12,326)     | 663,191    |
| Commitments and contingencies   |  |   |  |  |                             |                              |                           |              |            |
| Net assets:   |  |   |  |  |                             |                              |                           |              |            |
| Net assets without donor restrictions                                       | 177,937  | 6,264   | 3,746  | 240  | (492)                       | 3,178                        | 1,969                     | (13,188)     | 179,654    |
| Net assets with donor restrictions  | 18,276   | 9,031   | 1,794  | -  | -                           | -                            | -                         | (10,746)     | 18,355     |
| Total St. Joseph's Health, Inc. net assets                                  | 196,213  | 15,295  | 5,540  | 240  | (492)                       | 3,178                        | 1,969                     | (23,934)     | 198,009    |
| Non-controlling interests in joint ventures                                 | 584  | -   | -  | -  | -                           | -                            | -                         | -            | 584        |
| Total net assets including non-controlling interests                        | 196,797  | 15,295  | 5,540  | 240  | (492)                       | 3,178                        | 1,969                     | (23,934)     | 198,593    |
| Total liabilities and net assets  | \$ 810,319   | \$ 15,841   | \$ 5,625   | \$ 258                                       | \$ 27,289                   | \$ 3,178                     | \$ 35,534                 | \$ (36,260)  | \$ 861,784 |



St. Joseph's Health, Inc.

Consolidating Statement of Operations  
(In Thousands)

Year Ended December 31, 2018

|   | St. Joseph's<br>University<br>Medical Center<br>and Subsidiaries | St. Joseph's<br>Hospital and<br>Medical Center<br>Foundation, Inc. | St. Joseph's<br>Wayne Hospital<br>Foundation, Inc. | VHS<br>Management,<br>Inc. and<br>Subsidiary | 200 Hospital<br>Plaza Corp. | St. Joseph's<br>Health, Inc. | SJHS<br>Insurance<br>Limited | Eliminations | Total       |
|---|--|--|--|--|-----------------------------|------------------------------|------------------------------|--------------|-------------|
| <b>Operating revenues:</b>  |  |  |  |  |                             |                              |                              |              |             |
| Net patient service revenue   | \$ 713,470   | \$ –   | \$ –   | \$ –   | \$ –                        | \$ –                         | \$ –                         | \$ –         | \$ 713,470  |
| Other revenue   | 85,324   | 4,374  | 678  | –  | 4,060                       | –                            | 5,156                        | (6,166)      | 93,426      |
| Net assets released from restrictions – operations  | –  | 1,682  | 34   | –  | –                           | –                            | –                            | –            | 1,716       |
| Total operating revenues  | 798,794  | 6,056  | 712  | –  | 4,060                       | –                            | 5,156                        | (6,166)      | 808,612     |
| <b>Operating expenses:</b>  |  |  |  |  |                             |                              |                              |              |             |
| Salaries and wages  | 385,755  | 410  | 381  | –  | –                           | –                            | –                            | (791)        | 385,755     |
| Employee benefits   | 71,455   | 97   | 93   | –  | –                           | –                            | –                            | (189)        | 71,456      |
| Physician fees  | 22,593   | –  | –  | –  | –                           | –                            | –                            | –            | 22,593      |
| Supplies and other  | 269,856  | 4,524  | 469  | –  | 1,909                       | –                            | 9,281                        | (5,186)      | 280,853     |
| Interest  | 10,643   | –  | –  | –  | 1,121                       | –                            | –                            | –            | 11,764      |
| Depreciation and amortization   | 32,229   | 16   | –  | –  | 1,635                       | –                            | –                            | –            | 33,880      |
| Total operating expenses  | 792,531  | 5,047  | 943  | –  | 4,665                       | –                            | 9,281                        | (6,166)      | 806,301     |
| Operating income (loss)   | 6,263  | 1,009  | (231)  | –  | (605)                       | –                            | (4,125)                      | –            | 2,311       |
| <b>Non-operating gains and losses:</b>  |  |  |  |  |                             |                              |                              |              |             |
| Investment return   | 4,504  | 278  | 422  | –  | –                           | –                            | 1,759                        | –            | 6,963       |
| Excess (deficiency) of revenues over expenses,<br>before non-controlling interests in joint ventures                        | 10,767   | 1,287  | 191  | –  | (605)                       | –                            | (2,366)                      | –            | 9,274       |
| Less: net gain attributable to non-controlling interests<br>in joint ventures   | 3,972  | –  | –  | –  | –                           | –                            | –                            | –            | 3,972       |
| Excess (deficiency) of revenues over expenses   | 6,795  | 1,287  | 191  | –  | (605)                       | –                            | (2,366)                      | –            | 5,302       |
| <b>Other changes in net assets without donor restrictions:</b>  |  |  |  |  |                             |                              |                              |              |             |
| Change in net unrealized gains and losses on investments  | (7,705)  | (184)  | (458)  | –  | –                           | –                            | (1,954)                      | –            | (10,301)    |
| Pension-related adjustments   | (6,443)  | –  | –  | –  | –                           | –                            | –                            | –            | (6,443)     |
| Net assets released from restrictions – capital acquisitions  | 402  | –  | –  | –  | –                           | –                            | –                            | –            | 402         |
| Transfer of assets from (to) joint ventures   | 7,607  | (2,161)  | –  | (2,461)                                      | (4,083)                     | –                            | 1,442                        | –            | 344         |
| Dissolution of joint ventures   | (5,000)  | –  | –  | –  | –                           | –                            | –                            | –            | (5,000)     |
| Change in interest in net assets without donor restrictions of St. Joseph's<br>Hospital and Medical Center Foundation, Inc. | (1,058)  | –  | –  | –  | –                           | –                            | –                            | 1,058        | –           |
| Change in interest in net assets without donor restrictions of St. Joseph's<br>Wayne Hospital Foundation, Inc.              | (267)  | –  | –  | –  | –                           | –                            | –                            | 267          | –           |
| Change in net assets without donor restrictions   | \$ (5,669)   | \$ (1,058)   | \$ (267)   | \$ (2,461)                                   | \$ (4,688)                  | \$ –                         | \$ (2,878)                   | \$ 1,325     | \$ (15,696) |

The System presents its interests in its controlled affiliates using the cost method of accounting.

## St. Joseph's Health, Inc.

### Consolidating Statement of Changes in Net Assets (In Thousands)

Year Ended December 31, 2018

|   | St. Joseph's<br>University<br>Medical Center<br>and Subsidiaries | St. Joseph's<br>Hospital and<br>Medical Center<br>Foundation, Inc. | St. Joseph's<br>Wayne Hospital<br>Foundation, Inc. | VHS<br>Management,<br>Inc. and<br>Subsidiary | 200 Hospital<br>Plaza Corp. | St. Joseph's<br>Health, Inc. | SJHS<br>Insurance<br>Limited | Eliminations | Total       |
|---|--|--|--|--|-----------------------------|------------------------------|------------------------------|--------------|-------------|
| <b>Net assets without donor restrictions:</b>   |  |  |  |  |                             |                              |                              |              |             |
| Change in net assets without donor restrictions   | \$ (5,669)   | \$ (1,058)   | \$ (267)   | \$ (2,461)                                   | \$ (4,688)                  | \$ –                         | \$ (2,878)                   | \$ 1,325     | \$ (15,696) |
| <b>Net assets with donor restrictions:</b>  |  |  |  |  |                             |                              |                              |              |             |
| Contributions, grants, investment income, and other support   | (441)  | (509)  | 93   | –  | –                           | –                            | –                            | –            | (857)       |
| Changes in interest in restricted net assets of<br>St. Joseph's Hospital and Medical Foundation, Inc. | (2,191)  | –  | –  | –  | –                           | –                            | –                            | 2,191        | –           |
| Changes in interest in restricted net assets of<br>St. Joseph's Wayne Hospital Foundation, Inc.       | 60   | –  | –  | –  | –                           | –                            | –                            | (60)         | –           |
| Net assets released from restrictions – operations  | –  | (1,682)  | (34)   | –  | –                           | –                            | –                            | (3)          | (1,719)     |
| Net assets released from restrictions – capital acquisitions  | (402)  | –  | –  | –  | –                           | –                            | –                            | –            | (402)       |
| Change in net unrealized gains and losses on investments<br>held in perpetual trusts                  | (609)  | (526)  | (86)   | –  | –                           | –                            | –                            | 612          | (609)       |
| Change in net assets with donor restrictions  | (3,583)  | (2,717)  | (27)   | –  | –                           | –                            | –                            | 2,740        | (3,587)     |
| Decrease in St. Joseph's Health, Inc. net assets  | (9,252)  | (3,775)  | (294)  | (2,461)                                      | (4,688)                     | –                            | (2,878)                      | 4,065        | (19,283)    |
| <b>Non-controlling interests in joint ventures:</b>   |  |  |  |  |                             |                              |                              |              |             |
| Net gain attributable to non-controlling interests in joint ventures                                  | 3,972  | –  | –  | –  | –                           | –                            | –                            | –            | 3,972       |
| Distributions to non-controlling interests in joint ventures, net                                     | (7,269)  | –  | –  | –  | –                           | –                            | –                            | –            | (7,269)     |
| Decrease in non-controlling interests   | (3,297)  | –  | –  | –  | –                           | –                            | –                            | –            | (3,297)     |
| Change in net assets including non-controlling interests  | (12,549)   | (3,775)  | (294)  | (2,461)                                      | (4,688)                     | –                            | (2,878)                      | 4,065        | (22,580)    |
| Net assets at beginning of year   | 209,346  | 19,070   | 5,834  | 2,701  | 4,196                       | 3,178                        | 4,847                        | (27,999)     | 221,173     |
| Net assets at end of year   | \$ 196,797   | \$ 15,295  | \$ 5,540   | \$ 240                                       | \$ (492)                    | \$ 3,178                     | \$ 1,969                     | \$ (23,934)  | \$ 198,593  |

*The System presents its interests in its controlled affiliates using the cost method of accounting.*

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