

CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Beacon Health System, Inc. and Affiliated Corporations
Years Ended December 31, 2020 and 2019
With Reports of Independent Auditors

Ernst & Young LLP



Beacon Health System, Inc. and Affiliated Corporations

Consolidated Financial Statements
and Supplementary Information

Years Ended December 31, 2020 and 2019

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Report of Independent Auditors

The Board of Directors
Beacon Health System, Inc. and Affiliated Corporations

We have audited the accompanying consolidated financial statements of Beacon Health System, Inc. and Affiliated Corporations (the Corporation), which comprise the consolidated balance sheets as of December 31, 2020 and 2019, 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 of America. 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 Beacon Health System, Inc. and Affiliated Corporations at December 31, 2020 and 2019, and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles

Ernst + Young LLP

March 4, 2021

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Balance Sheets

(In Thousands)

	December 31	
	2020	2019
Assets		
Current assets:		
Cash and cash equivalents	\$ 115,392	\$ 67,962
Short-term investments	56,231	13,201
Patient accounts receivable	219,756	180,883
Due from third-party payors	37,690	18,626
Other receivables	10,865	7,490
Other current assets	1,287	1,146
Inventories	30,629	24,908
Prepaid expenses	15,517	19,365
Total current assets	<u>487,367</u>	<u>333,581</u>
Assets limited as to use:		
Internally designated investments	812,663	755,371
Restricted cash	5,408	5,034
Externally designated investments – insurance trust	2,952	2,854
Board-designated endowment	30,090	27,947
Endowment and temporarily restricted investments	9,421	8,712
	<u>860,534</u>	<u>799,918</u>
Property and equipment:		
Land	53,920	51,925
Buildings and improvements	894,527	856,141
Furniture and equipment	575,924	529,342
Construction-in-progress	11,336	48,801
	<u>1,535,707</u>	<u>1,486,209</u>
Less allowances for depreciation and amortization	<u>854,141</u>	<u>794,488</u>
	<u>681,566</u>	<u>691,721</u>
Deferred charges and other assets	75,603	71,600
Interest rate swap	–	323
Total assets	<u><u>\$ 2,105,070</u></u>	<u><u>\$ 1,897,143</u></u>

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Balance Sheets (continued)
(In Thousands)

	December 31	
	2020	2019
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 69,891	\$ 55,291
Accrued salaries and benefits	51,466	39,169
Accrued expenses	625	4,294
Other current liabilities	1,263	1,125
Due to third-party payors	53,069	498
Current maturities of long-term debt	10,751	9,889
Total current liabilities	<u>187,065</u>	110,266
Noncurrent liabilities:		
Long-term debt, less current maturities	284,804	296,338
Other liabilities	49,401	17,885
Interest rate and basis swaps	18,302	14,884
	<u>352,507</u>	329,107
Total liabilities	<u>539,572</u>	439,373
Net assets:		
Without donor restrictions	1,550,141	1,443,448
With donor restrictions	15,357	14,322
Total net assets	<u>1,565,498</u>	1,457,770
Total liabilities and net assets	<u><u>\$ 2,105,070</u></u> <u>\$ 1,897,143</u>	

See accompanying notes.

Beacon Health System, Inc. and Affiliated Corporations

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

	Year Ended December 31	
	2020	2019
Unrestricted revenue, gains, and other support		
Patient service revenue	\$ 985,255	\$ 985,708
Other revenue	74,993	46,347
Net assets released from restrictions used for operations	929	926
	1,061,177	1,032,981
Expenses		
Salaries and wages	459,209	449,983
Employee benefits	94,976	108,337
Supplies and other	272,171	264,722
Professional fees and purchased services	118,841	115,961
Depreciation and amortization	62,454	60,012
Interest	7,816	7,816
	1,015,467	1,006,831
Income from operations	45,710	26,150
Nonoperating income (expenses)		
Investment income, net	64,225	90,848
Unrealized (losses) gains on swap transactions, net	(3,741)	353
Realized gain on swap termination	-	723
Loss on lease termination	-	(692)
Revenue and gains in excess of expenses	106,194	117,382

Beacon Health System, Inc. and Affiliated Corporations

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

	Year Ended December 31	
	2020	2019
Net assets without donor restrictions		
Revenue and gains in excess of expenses	\$ 106,194	\$ 117,382
Net assets released from restrictions used for capital purposes	424	815
Net assets released from restriction by donor	75	–
Increase in net assets without donor restrictions	<u>106,693</u>	118,197
Net assets with donor restrictions		
Purpose-restricted contributions	1,696	2,588
Investment income	767	1,062
Reclass of contribution restriction by donor	(75)	–
Net assets released from restrictions used for operating and capital purposes	<u>(1,353)</u>	<u>(1,741)</u>
Increase in net assets with donor restrictions	<u>1,035</u>	1,909
Change in net assets	107,728	120,106
Net assets at beginning of year	<u>1,457,770</u>	1,337,664
Net assets at end of year	<u>\$ 1,565,498</u>	<u>\$ 1,457,770</u>

See accompanying notes.

Beacon Health System, Inc. and Affiliated Corporations

Consolidated Statements of Cash Flows

(In Thousands)

	Year Ended December 31	
	2020	2019
Operating activities		
Change in net assets	\$ 107,728	\$ 120,106
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	62,454	60,012
Unrealized losses (gains) on swap transactions, net	3,741	(353)
Gain on swap termination	–	(723)
Loss on lease termination	–	692
Unrealized gains on investments	(55,834)	(49,467)
Restricted contributions and investment income	(2,463)	(3,650)
Changes in operating assets and liabilities:		
Patient accounts receivable	(38,873)	(18,548)
Other receivables, inventories, and prepaid expenses	(5,389)	(5,104)
Other assets	(5,115)	(15,723)
Investments – trading	(4,408)	(35,394)
Accounts payable, accrued salaries and benefits, and accrued expenses	23,366	2,119
Due to/from third-party payors, net	33,507	22,669
Other long-term liabilities	31,367	6,680
Net cash provided by operating activities	150,081	83,316
Investing activities		
Additions to property and equipment	(51,982)	(89,432)
Proceeds from property and equipment	488	129
Net cash used in investing activities	(51,494)	(89,303)
Financing activities		
Principal payments on long-term debt and other debt obligations	(10,216)	(10,915)
Restricted contributions and investment income	2,463	3,650
Net cash used in financing activities	(7,753)	(7,265)
Increase (decrease) in cash and cash equivalents and restricted cash	90,834	(13,252)
Cash and cash equivalents and restricted cash at beginning of year	86,197	99,449
Cash and cash equivalents and restricted cash at end of year	\$ 177,031	\$ 86,197
Reconciliation of cash and cash equivalents and restricted cash to the consolidated balance sheets:		
Cash and cash equivalents	\$ 115,392	\$ 67,962
Short-term investments	56,231	13,201
Restricted cash included in assets limited as to use	5,408	5,034
	\$ 177,031	\$ 86,197
Supplemental disclosure of cash flow information		
Interest paid	\$ 7,844	\$ 7,901

See accompanying notes.

Beacon Health System, Inc. and Affiliated Corporations

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

December 31, 2020

1. Organization and Basis of Consolidation

The accompanying consolidated financial statements represent the accounts of Beacon Health System, Inc. (the Corporation) and its various affiliated corporations under the control of the Corporation (collectively, BHS). The Corporation is an Indiana not-for-profit corporation exempt from federal income tax under Internal Revenue Code (the Code) Section 501(a) as an organization described in Section 501(c)(3) and a public charity as described in Section 509(a)(3). The Corporation is the sole corporate member of the following entities:

- Elkhart General Hospital, Inc. (EGH)
- Memorial Hospital of South Bend, Inc. (MHSB)
- Beacon Health Foundation, Inc. (BHF), formerly Memorial Health Foundation, Inc.
- Beacon Medical Group, Inc. (BMG), formerly Memorial Health System, Inc.
- Beacon Health Ventures, Inc. (BHV)
- Community Occupational Medicine, Inc. (COM)
- CHA ACO, LLC (CHA ACO)
- Beacon Health, LLC (BH)
- Community Hospital of Bremen, Inc. (CHB)
- BPL Acquisitions, LLC
- Beacon Specialty Surgery, LLC (BSS)

Beacon Health System, Inc. and Affiliated Corporations

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

1. Organization and Basis of Consolidation (continued)

EGH, MHSB, CHB, BMG, and BHF are also exempt from federal income tax under Section 501(a) of the Code as organizations described in Section 501(c)(3) and as public charities described in Sections 509(a)(1) and 509(a)(2). BHV and COM are Indiana for-profit corporations. EGH is a 365-licensed-bed (254 available) acute care community hospital located in Elkhart, Indiana. MHSB is a 657-licensed-bed (409 available) acute care trauma center located in South Bend, Indiana. CHB is a 24-bed critical access hospital located in Bremen, Indiana. EGH, MHSB, and CHB (collectively, the Hospitals) provide inpatient, outpatient, and 24-hour emergency care services for residents of Elkhart; South Bend; and Bremen, Indiana, and the surrounding communities.

BHF is organized primarily to promote and encourage philanthropic activities for the support of the Corporation and its affiliates.

BHV manages the taxable operations of the Corporation, including home care and other non-acute health care services.

COM primarily promotes population health management.

CHA ACO coordinates high-quality care for Medicare beneficiaries participating in the Medicare Shared Savings Programs.

BMG operates the physician enterprise of the Corporation.

BH improves and expands delivery and quality of health care services for the Corporation.

BPL Acquisitions, LLC is a real estate holding company established to purchase land.

BSS, formerly Memorial Spine and Neuroscience Center, LLC, previously a joint venture that is now fully owned by BMG, is an outpatient surgery center specializing in neurologic, spine, and pain control procedures.

All significant intercompany accounts and transactions have been eliminated in consolidation.

Beacon Health System, Inc. and Affiliated Corporations

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

1. Organization and Basis of Consolidation (continued)

The Corporation owns a less-than-majority ownership or controlling interest in the following:

- 50% interest in Community Health Alliance LLC, an Indiana physician hospital organization
- 45% interest in LaPorte Medical Group Surgery Center, LLP, an outpatient surgery center
- 50% interest in Valparaiso Medical Development, LLC, a professional medical building venture
- 25% interest in Magnetic Resonance Imaging, LLC, an imaging and radiology center
- 33% interest in Michiana Information Health Network, Inc., a health information exchange
- 40% interest in Elkhart Health, Fitness & Aquatics, Inc., a health fitness and aquatics center
- 10% interest in Alick's Home Medical Equipment, Inc., a home medical equipment provider
- 54% interest in South Bend Specialty Surgery Center, LLC, an outpatient surgery center. Although the Corporation owns a majority financial interest in this entity, it does not possess a controlling interest in the entity, and therefore does not consolidate the LLC.
- 50% interest in Franciscan Beacon Health, an acute care hospital located in LaPorte, Indiana

Aggregate financial information relating to these investments is as follows:

	<u>2020</u>	<u>2019</u>
Assets	\$ 136,505	\$ 104,900
Liabilities	33,050	19,427
Net income	2,862	11,880

Beacon Health System, Inc. and Affiliated Corporations

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

1. Organization and Basis of Consolidation (continued)

At December 31, 2020 and 2019, the Corporation has \$48,585 and \$43,406, respectively, related to these equity method investments recorded in deferred charges and other assets on the consolidated balance sheets.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Although estimates are considered to be fairly stated at the time the estimates are made, actual results could differ from those estimates.

Cash Equivalents

All investments that are not limited as to use with a maturity of three months or less at the time of acquisition are reflected as cash equivalents. Cash equivalents include checking accounts, money market accounts, corporate credit card accounts, and petty cash. The carrying value of cash equivalents approximates fair value. Highly liquid debt instruments with original, short-term maturities of less than 90 days that are included as part of assets limited as to use are excluded from cash equivalents as they are commingled with longer-term investments. Amounts included in restricted cash include cash held within investments and represent funds set aside within the investment portfolio based on management's policy or contractual arrangements.

Short-Term Investments

Short-term investments include cash reinvested on a daily basis, accrued interest on investments, and money expected to be used in less than a year. Also included in short-term investments are restricted and unrestricted investment donations that are in the process of being liquidated.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

Assets Limited as to Use

Assets limited as to use include assets set aside by the Board of Directors (the Board) for future capital improvements and community health enhancement initiatives that the Board, at its discretion, may subsequently use for other purposes. In addition, assets limited as to use also include assets held by trustees under self-funded insurance agreements, investments externally designated under indenture or donor restrictions, and money expected to be used as part of BHS's community benefit.

Investments

The Corporation classifies its investments as trading. Under a trading classification, all unrestricted realized and unrealized gains and losses are included in revenue and gains in excess of expenses.

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value based on quoted market prices for those or similar investments. Dividend and interest income, realized gains and losses, and changes to fair values of investments are reported as nonoperating investment income on the consolidated statements of operations and changes in net assets. Nonoperating investment income is reported net of internal and external investment costs.

Investments in alternative investments, primarily hedge fund of funds, that invest in marketable securities and derivative products are reported using the equity method. The estimated fair values are provided by the respective fund managers and are based on historical costs, appraisals, and other estimates that require varying degrees of judgment. Management has utilized the best available information for reported values, which in some instances are valuations as of an interim date not more than 90 days before year-end. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty and may differ from the value that would have been used had a ready market for such investments existed. Resulting differences could be material. The financial statements of the hedge funds are audited annually. Equity earnings related to these alternative investments are included in nonoperating investment income. The Corporation's holding reflects net contributions to the hedge fund and an allocated share of realized and unrealized investment income and expense.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

Inventories

Inventories are stated at the lower of cost (average cost method) or market.

Unamortized Bond Issuance Costs

Costs incurred in connection with the issuance of long-term debt are deferred and amortized over the term of the related financing, which approximates the effective interest method.

Fair Value of Financial Instruments

The Corporation's carrying amount for its financial instruments, which include cash and cash equivalents, short-term investments and assets limited as to use, accounts receivable, debt, and interest rate and basis swaps, at December 31, 2020 and 2019, approximates fair value. The estimated fair value amounts have been determined by the Corporation using available market information and appropriate valuation methodologies.

Property and Equipment

Property and equipment are carried at cost, except for donated assets, which are recorded at fair value at the date of donation. Allowances for depreciation and amortization are computed primarily utilizing the straight-line method over the estimated useful lives of the assets, which range from 3 to 40 years. Depreciation expense for the years ended December 31, 2020 and 2019, was \$61,648 and \$59,608, respectively.

Lease Right of Use Assets and Liabilities

The Corporation records a lease right of use asset (that is an asset that represents the Corporation's right to use the leased asset for the lease term) for leases with a term greater than 12 months and that do not meet the criteria as a sales-type lease or a direct financing lease.

The Corporation records operating lease right of use assets at the present value of future lease payments, adding initial direct costs and prepaid lease payments, reduced by any lease incentives. Operating right of use assets are amortized using the straight-line method over the related lease term. Amortization of operating lease right of use assets is included on the accompanying consolidated statement of operations and changes in net assets in other expenses.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

The Corporation records financing lease right of use assets at the value of principal payments, adding initial direct costs and prepaid lease payments, reduced by any lease incentives. Financing right of use assets are amortized using the straight-line method over the related lease term. Amortization of financing lease right of use assets is included on the accompanying consolidated statement of operations and changes in net assets in depreciation and amortization expenses.

Asset Impairment

The Corporation considers whether indicators of impairment are present and performs the necessary tests to determine whether the carrying value of an asset is appropriate. Impairment write-downs are recognized in operating expenses at the time the impairment is identified. There were no impairments of long-lived assets in 2020 or 2019.

Deferred Charges and Other Assets

Included in deferred charges and other assets are intangible assets, goodwill, and investments in unconsolidated affiliates.

The acquisition of a business entity can result in the recording of intangible assets. Acquired definite-lived intangible assets (excluding goodwill) are amortized over the useful life of the assets. Goodwill is carried at acquisition value, less any impairment reductions.

The carrying value of goodwill amounted to approximately \$12,038 at December 31, 2020 and 2019, and is included in deferred charges and other assets on the consolidated balance sheets. Goodwill is assessed for impairment on an annual basis at the reporting unit level. If the fair value of the reporting unit is less than the carrying value, an impairment loss equal to the difference between the implied fair value of the reporting unit goodwill and the carrying value of the reporting unit goodwill is recognized. There was no impairment of goodwill in 2020 or 2019.

The Corporation accounts for its investments in less than majority owned and controlled affiliates using the equity method of accounting. Income from these investments is reflected in other revenue on the consolidated statements of operations and changes in net assets.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

Endowment Investments

Income is received directly by BHF from BHF board-designated quasi-endowment investments and quasi-endowments with restriction and is included in investment income within both net assets with and without donor restrictions. EGH receives a portion of the income from investments in endowments directly as they are released from restriction. These endowment investments have perpetual existence.

Contributions

Unconditional pledges to give cash and other assets are reported at fair value at the date the pledge is received to the extent estimated to be collectible by the Corporation.

Net Assets Without Donor Restrictions

Net assets without donor restrictions are available for use at the discretion of the Board and/or management for general operating purposes.

Net Assets With Donor Restrictions

Net assets with donor restrictions consist of assets whose use is limited by donor-imposed, time, and/or purpose restrictions.

The Corporation reports pledges, gifts of cash, and other assets as revenue with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, the net assets are reclassified as net assets without donor restriction and reported on the consolidated statements of operations and changes in net assets as net assets released from restrictions. Assets released from restrictions that are used for the purchase of property and equipment or capital purposes are reported on the consolidated statements of operations and changes in net assets as additions to net assets without restriction. Resources restricted by donors for specific operating purposes are reported in revenue without restriction, gains, and other support to the extent expended within the period.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

Some net assets have been restricted by donors to be maintained by the Corporation in perpetuity. In accordance with the restriction, a majority of the investment income and investment gains or losses from these net assets are restricted by the donor for a specific purpose. A specified portion of income earned by the net assets is released from restriction and used for operations each year and, therefore, is included on the consolidated statements of operations and changes in net assets as other revenue.

Patient Service Revenue and Patient Accounts Receivable

Patient service revenue and patient accounts receivable are reported at the amount that reflects the consideration to which BHS expects to be entitled in exchange for providing patient care. BHS has agreements with various third-party payors that provide for payments to BHS at amounts different from its established rates. Third parties include Medicare, Medicaid, managed health care plans, and other commercial plans. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. These amounts include estimated adjustments under certain reimbursement agreements with third-party payors, which are subject to audit by the applicable administering agency. These adjustments are accrued on an estimated basis and are adjusted in future periods as final settlements are determined (see Note 3). The Hospitals provide care to all patients regardless of their ability to pay. Charity care provided is excluded from patient service revenue (see Note 4).

Performance Indicator

The consolidated statements of operations and changes in net assets include a performance indicator, revenue and gains in excess of expenses. Changes in net assets without restrictions, which are excluded from revenue and gains in excess of expenses, consistent with industry practice, include contributions of long-lived assets, including assets acquired using contributions, which, by donor restrictions, were to be used for the purpose of acquiring such assets.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

Allocation of Costs

The Corporation's ability to exercise control over consolidated entities could result in the entities having a financial position or operating results that are significantly different from those that would have been obtained if the entities were autonomous. The manner of allocating certain shared and centralized costs, such as accounts payable processing, information technology support, and other Corporation-managed administration costs, is determined by the Corporation utilizing Internal Revenue Service transfer pricing guidance and is not audited. Alternate methods of accounting for these cost allocations may produce significantly different operating results for each of the consolidated entities.

Interest Rate and Basis Swaps

All interest rate and basis swaps are measured at fair value based on techniques consistent with the market approach. None of the swaps are designated as hedging instruments; therefore, the unrealized gains or losses on the fair value of the swaps are included in revenue and gains in excess of expenses on the consolidated statements of operations and changes in net assets.

Asset Retirement Obligations

The Corporation accounts for the fair value of legal obligations associated with long-lived asset retirements by recognizing an expense and accreting a liability over the life of the asset to cover potential legal obligations at the end of the asset's useful life. The asset retirement obligation primarily relates to future asbestos remediation related to buildings on MHSB's campus, as well as ground/soil remediation associated with the removal of underground fuel tanks. The carrying value of the obligation amounted to approximately \$5,045 and \$4,897 at December 31, 2020 and 2019, respectively, and is reflected in other liabilities on the consolidated balance sheets.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

New Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases (Topic 842)*. Topic 842 requires lessees to recognize assets and liabilities for most leases. Topic 842 was subsequently amended by ASU 2018-01, *Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842*; ASU 2018-10, *Codification Improvements to Topic 842, Leases*; and ASU 2018-11, *Leases (Topic 842): Targeted Improvements*. The new standard established a right of use (ROU) asset model that requires a lessee to recognize an ROU asset and lease liability on the balance sheet for all leases with a term longer than 12 months. The new standard was effective for the Corporation on January 1, 2019, and was adopted using the modified retrospective approach.

The new standard provides a number of optional practical expedients in the transition. The Corporation has elected the “package of practical expedients,” which allows it not to reassess under the new standard its prior conclusions about lease identification, lease classification, and initial direct costs. The Corporation has not elected the use of hindsight or the practical expedient pertaining to land easements as the land easement expedient is not applicable to the Corporation. The Corporation separates lease and non-lease components for real property. For all other classes of assets, the Corporation has elected not to separate lease and non-lease components.

The new standard also provides practical expedients for ongoing accounting. The Corporation has elected the short-term lease recognition exemption for all leases that are less than 12 months. This means, for those leases that qualify, the Corporation will not recognize ROU assets or lease liabilities, and this includes not recognizing ROU assets or lease liabilities for existing short-term leases of those assets in transition (see Note 6).

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. The amendments in this update clarify the classification of eight types of transactions, including proceeds from the settlement of insurance claims and distributions received from equity method investees, on the statement of cash flows to reduce diversity in practice. BHS was required to adopt the new ASU for the year ended December 31, 2019 (and interim periods within the annual period beginning January 1, 2020), and the guidance did not have a material impact to its consolidated financial statements.

Beacon Health System, Inc. and Affiliated Corporations

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

2. Summary of Significant Accounting Policies (continued)

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. This ASU required the entity to show the changes in total cash, cash equivalents, restricted cash, and restricted cash equivalents on the statement of cash flows. The Corporation adopted this ASU in 2019 by applying a retrospective transition method, which required a restatement of its consolidated statements of cash flows for all periods presented.

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*. This ASU provides a more robust framework to determine when a transaction should be accounted for as a contribution or as an exchange transaction and provides additional guidance about how to determine whether a contribution is conditional. BHS adopted the new ASU for the fiscal year beginning on January 1, 2019, including interim periods, and this ASU did not have a material impact 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*. This ASU aligns the requirements 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. BHS is required to adopt the new ASU for the fiscal year beginning January 1, 2021, and is currently evaluating the impact this guidance will have on its consolidated financial statements.

Reclassifications

Certain reclassifications were made to the 2019 consolidated financial statements to conform with classifications made in 2020. The reclassifications had no effect on the revenue and gains in excess of expenses, the changes in net assets or on net assets previously reported.

Beacon Health System, Inc. and Affiliated Corporations

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

3. Revenue and Accounts Receivable

Patient Service Revenue

Patient service revenue is reported at the amount that reflects the consideration to which the Corporation expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others and include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, the Corporation bills the patients and third-party payors several days after the services are performed and/or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

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

Because all of its performance obligations relate to contracts with a duration of less than one year, the Corporation has elected to apply the optional exemption and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

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

Beacon Health System, Inc. and Affiliated Corporations

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

3. Revenue and Accounts Receivable (continued)

The Corporation determines the transaction price, which involves significant estimates and judgment, based on standard charges for goods and services provided, reduced by explicit and implicit price concessions, including contractual adjustments provided to third-party payors, discounts provided to uninsured and underinsured patients in accordance with the Corporation's policy and/or implicit price concessions based on the historical collection experience of patient accounts.

The Corporation determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. A summary of the payment arrangements with major third-party payors follows:

- **Medicare:** Certain inpatient acute care services are paid at prospectively determined rates per discharge based on clinical, diagnostic, and other factors. Certain services are paid based on cost-reimbursement methodologies subject to certain limits. Physician services are paid based upon established fee schedules. Outpatient services are paid using prospectively determined rates.
- **Medicaid:** Reimbursements for Medicaid services are generally paid at prospectively determined rates per discharge, per occasion of service, or per covered member.
- **Other:** Payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations provide for payment using prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Beacon Health System, Inc. and Affiliated Corporations

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

3. Revenue and Accounts Receivable (continued)

Disproportionate Share Hospital (DSH) payments by the state of Indiana (the State), if eligible, are paid according to the fiscal year of the State, which ends on June 30 of each year, and are based on the cost of uncompensated care provided by the DSH providers during their respective fiscal year ended during the State fiscal year. In 2016, MHSB qualified for the State DSH program for State fiscal years (SFYs) 2016 and 2017. In 2018, MHSB qualified for the State DSH program for SFYs 2018 and 2019. MHSB recorded patient service revenue of \$33,362 and \$7,212 for the years ended December 31, 2020 and 2019, respectively. The amounts recorded for prior state fiscal years represent changes in estimates from prior period estimates. The following is a summary by SFY:

	<u>2020</u>	<u>2019</u>
SFY 2021	\$ 6,850	\$ —
SFY 2020	10,572	3,393
SFY 2019	6,656	6,380
SFY 2018	9,284	1,454
SFY 2017	—	(4,015)
	<u>\$ 33,362</u>	<u>\$ 7,212</u>

Beacon Health System, Inc. and Affiliated Corporations

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

3. Revenue and Accounts Receivable (continued)

In April 2014, the Indiana Hospital Assessment Fee program (HAF) was approved by the Centers for Medicare & Medicaid Services (CMS) retroactively for the period July 1, 2013 to June 30, 2017. The current state budget extended HAF through June 30, 2021. Under HAF, Indiana hospitals receive additional federal Medicaid funds for the state’s health care system, administered by the Indiana Family and Social Services Administration. HAF includes both a payment to the Hospitals from the state (included in patient service revenue) and an assessment (included in supplies and other expenses) against the Hospitals, which is paid to the state the same year. BHS recognized HAF revenues and assessments as follows:

	Year Recognized		Total
	2020	2019	
Year ended December 31, 2020, HAF: Revenue	\$ 73,095	\$ –	\$ 73,095
Year ended December 31, 2020, HAF: Assessments	(38,756)	–	(38,756)
Year ended December 31, 2019, HAF: Revenue	–	68,233	68,233
Year ended December 31, 2019, HAF: Assessments	(443)	(37,874)	(38,317)
Year ended December 31, 2018, HAF: Assessments	–	(1,859)	(1,859)
	\$ 33,896	\$ 28,500	\$ 62,396

HAF revenue is included in patient service revenue and HAF assessments are included in supplies and other expenses on the consolidated statements of operations and changes in net assets.

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation, as well

Beacon Health System, Inc. and Affiliated Corporations

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

3. Revenue and Accounts Receivable (continued)

as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge the Corporation's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon the Corporation. In addition, the contracts the Corporation has with commercial payors also provide for retroactive audit and review of claims.

Settlements with third-party payors for retroactive adjustments due to 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 Corporation's historical settlement activity, 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. 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.

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. The Corporation also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. The Corporation estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to patient service revenue in the period of the change.

Estimates for DSH, settlements with third-party payors, and other contractual adjustments can differ from actual reimbursement based on the results of subsequent reviews, government regulatory changes, and cost report audits. For the years ended December 31, 2020 and 2019, patient service revenue has been increased by approximately \$15,488 and \$2,620, respectively, for changes in estimates of third-party payor settlements related to prior years. There were no other significant changes to the judgments used to determine the transaction price in prior periods.

Beacon Health System, Inc. and Affiliated Corporations

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

3. Revenue and Accounts Receivable (continued)

Management has determined that the nature, amount, timing, and uncertainty of revenue and cash flows are affected by the payors and service lines that render services to patients. Patient service revenue recognized for the years ended December 31 from major payor sources is as follows:

Payor	2020	2019
Anthem	\$ 215,725	\$ 229,753
Commercial	285,054	294,091
Medicare	280,691	293,397
Medicaid	170,526	127,632
Self-pay	33,259	40,835
Patient service revenue	\$ 985,255	\$ 985,708

The composition of patient care service revenue based on service lines the Corporation operates for the years ended December 31 is as follows:

Service lines	2020	2019
Hospitals	\$ 857,161	\$ 849,178
Medical Group	116,389	123,095
Health Ventures	2,808	4,511
Other	8,897	8,924
Patient service revenue	\$ 985,255	\$ 985,708

Patient service revenues related to the Medicare program are approximately 29% and 30% of patient service revenue for the years ended December 31, 2020 and 2019, respectively. Patient service revenues related to the Medicaid program are approximately 17% and 13% of patient service revenue for the years ended December 31, 2020 and 2019, respectively. Amounts reported under the Anthem payor contract account for approximately 22% and 23% of patient service revenue for the years ended December 31, 2020 and 2019, respectively.

Beacon Health System, Inc. and Affiliated Corporations

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

3. Revenue and Accounts Receivable (continued)

Credit is granted without collateral to patients, most of whom are local residents and are insured under third-party arrangements. Major components of patient accounts receivable include approximately 20% from Medicare, approximately 11% from Medicaid, and approximately 20% from Anthem at December 31, 2020, and approximately 22% from Medicare, approximately 7% from Medicaid, and approximately 21% from Anthem at December 31, 2019.

The Corporation has elected the practical expedient and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Corporation'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 services will be one year or less. However, the Corporation 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.

The Corporation has applied the practical expedient and all incremental customer contract acquisition costs are expensed as they are incurred as the amortization period of the asset that the Corporation, otherwise, would have recognized is one year or less in duration.

Other Revenue

Other revenues consist of revenues associated with retail services, such as pharmacy and cafeteria, ancillary services and strategic initiatives with entities with less than majority ownership or noncontrolling interests (Joint Ventures) by the Corporation, health and fitness membership, and leased space rental agreements with third parties. Revenues associated with pharmacy services are estimated as prescriptions are filled and collected by patients. Retail sales are recorded at the time of service. Revenues associated with Joint Ventures are recognized on the equity method. Health and fitness revenue is recognized over the membership period and leased space rental revenue is recognized over the term of the lease.

Beacon Health System, Inc. and Affiliated Corporations

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

3. Revenue and Accounts Receivable (continued)

The composition of other revenue for the years ended December 31 is as follows:

Service lines	2020	2019
Retail service revenue	\$ 13,727	\$ 13,294
Joint Venture revenue	(115)	4,056
Grant revenue*	32,926	4,400
Health and fitness revenue	4,218	5,936
Rental revenue	2,988	3,240
Other revenue	21,249	15,421
	\$ 74,993	\$ 46,347

* Grant revenue includes Federal CARES Act funding of approximately \$29,486 and \$0 for the years ended December 31, 2020 and 2019, respectively.

As of December 31, 2020, the Corporation received \$29,486 in grant payments from the U.S. Department of Health and Human Services from the Provider Relief Fund established under the Coronavirus Aid, Relief and Economic Security Act (CARES Act), which has been recognized as revenue and included in other operating revenue within the consolidated statement of operations and changes in net assets. Payments from the Provider Relief Fund are intended to cover patient care lost revenues and qualified expenses, net of other reimbursed sources, attributed to COVID-19 and are not required to be repaid provided the recipient attests to and complies with the terms and conditions of the grant funds. The recognition of this support falls under the grant accounting guidance of accounting principles generally accepted in the United States. This guidance requires all significant terms and conditions to have been met for recognition to occur. Management of the Corporation will continue to monitor compliance with the terms and conditions of the CARES Act grant funds and the impact of the pandemic on the Corporation's consolidated revenues and expenses.

In addition, the Corporation received approximately \$77,288 from the CMS as an advance payment for Medicare services during 2020. The funds are provided through the expansion of the Medicare Accelerated and Advance Payment Program to ensure providers and suppliers have the resources needed to combat the COVID-19 pandemic. The advances will be recouped by withholding future Medicare fee-for-service payments for claims until such time as the full

Beacon Health System, Inc. and Affiliated Corporations

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

3. Revenue and Accounts Receivable (continued)

accelerated payment has been recouped, unless the Corporation elects to repay the advances prior to full recoupment. Recoupments are scheduled to begin in April 2021. Subsequent to the 29-month recoupment period, any unpaid remaining balance is subject to an interest charge of 4% per annum. Accelerated and advance payments of approximately \$52,000 and \$25,288 are included in due to third-party payors and other liabilities, respectively, within the consolidated balance sheet. The CARES Act also permits employers to defer the employer portion of social security taxes. Employers are required to remit one-half of the amount deferred by December 31, 2021, and the remaining half by December 31, 2022. Through December 31, 2020, the Corporation has deferred approximately \$14,284 of these taxes; half of this liability is included in accrued salaries and benefits and the other half is included in other noncurrent liabilities within the consolidated balance sheet.

4. Charity Care

Patients who meet the Corporation's criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue.

Charity care represents unreimbursed costs for services rendered at a reduced fee, or no fee, due to the inability of the patient to pay for services. The amount of the charity care provided was approximately \$2,804 and \$5,714 for the years ended December 31, 2020 and 2019, respectively, at estimated cost. The Corporation utilized a cost to charge ratio methodology for the cost analysis. The only reimbursement for financial assistance care received by the Corporation is determined through a settlement process in the Hospitals' annual Medicare cost report filing. Financial assistance care reimbursement was approximately \$566 and \$1,022 for the years ended December 31, 2020 and 2019, respectively.

5. Retirement Plans

The Corporation maintains a defined contribution employee retirement and savings plan for all employees who have attained 21 years of age and have completed 12 months of continuous service. The Corporation's contributions are based on 100% of the employee's contributions, up to 4% of the employee's salary. Both employee and corporation contributions are subject to certain limitations. The benefit plan expense for the years ended December 31, 2020 and 2019, was approximately \$12,863 and \$13,891, respectively.

Beacon Health System, Inc. and Affiliated Corporations

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

6. Lease Obligations

The Corporation has leases for certain office space and equipment. The lease term begins at the lease commencement date and is determined on that date based on the noncancelable term of the lease. The Corporation's operating lease terms range from seven to ten years, with the obligations ending in February 2029. The lease agreements contain variable lease payments and the Corporation does not intend to extend the lease agreements. The Corporation's financing lease terms are five years, ending in May 2023 and October 2023. The lease agreement has a standard lease payment, with a purchase option at the end of the agreement.

The Corporation is using a discount rate of 3.2% for operating leases, which represents the Corporation's incremental borrowing rate. The total operating lease payments that will be incurred over the life of the operating leases are \$5,764 as of December 31, 2020. In July 2019, one of the operating leases was terminated. The results of the lease termination were that \$4,728 was written off for the operating ROU, \$4,742 was written off for the operating lease liability, and \$646 was taken as a loss on the lease termination.

The Corporation is using a discount rate of 2.269% for financing leases, which is the rate embedded in the lease agreements. The total financing lease payments that will be incurred over the life of the leases are \$2,977, of which \$2,809 is amortization and \$168 is interest.

Beacon Health System, Inc. and Affiliated Corporations

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

6. Lease Obligations (continued)

The current portion of the operating and financing ROU is included in other current assets and the long-term portion of the operating and financing ROU is included in deferred charges and other assets. The current portion of the operating and financing lease liability is included in other current liabilities and the long-term portion of the operating and financing ROU is included in other long-term liabilities. The table below sets forth a summary of the Corporation's ROU assets and lease liabilities at December 31:

	2020	2019
Current portion of operating ROU	\$ 681	\$ 647
Long-term portion of operating ROU	3,150	3,844
Total operating ROU assets	\$ 3,831	\$ 4,491
Current portion of operating lease liability	\$ 668	\$ 647
Long-term portion of operating lease liability	3,189	3,857
Total operating lease liability	\$ 3,857	\$ 4,504
Current portion of financing ROU	\$ 605	\$ 498
Long-term portion of financing ROU	1,531	1,755
Total financing ROU assets	\$ 2,136	\$ 2,253
Current portion of financing lease liability	\$ 595	\$ 478
Long-term portion of financing lease liability	1,570	1,782
Total financing lease liability	\$ 2,165	\$ 2,260

Beacon Health System, Inc. and Affiliated Corporations

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

6. Lease Obligations (continued)

At December 31, 2020, the minimum future lease payments under these leases are as follows:

	Operating	Financing	Total
2021	\$ 782	\$ 641	\$ 1,423
2022	782	641	1,423
2023	794	572	1,366
2024	809	409	1,218
2025	826	—	826
Thereafter	207	—	207
	<u>\$ 4,200</u>	<u>\$ 2,263</u>	<u>\$ 6,463</u>

Operating lease expense for the years ended December 31, 2020 and 2019, was approximately \$795 and \$1,081, respectively, which is included in supplies and other expenses.

Amortization expense for financing leases at December 31, 2020 and 2019, was \$543 and \$130, respectively, which is included in depreciation and amortization expense. Interest expense for financing leases at December 31, 2020 and 2019, was \$56 and \$15, respectively, and is included in interest expense.

Beacon Health System, Inc. and Affiliated Corporations

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

7. Long-Term Debt

Long-term debt consists of the following at December 31:

	<u>2020</u>	<u>2019</u>
Tax-exempt bonds issued on behalf of BHS by the Indiana Finance Authority:		
BHS Revenue Bonds, Series 2018, bearing interest at a variable rate of 0.73% at December 31, 2020, due in varying annual installments on December 15 of each year through 2043, with a mandatory tender date of December 15, 2028	\$ 32,500	\$ 33,750
BHS Revenue Refunding Bonds, Series 2017A, bearing interest at variable rates with a floating fixed interest rate swap of 0.59% at December 31, 2020, due in varying annual installments on August 15 of each year through 2033, with a mandatory tender date of September 8, 2022	36,535	36,780
BHS Revenue Refunding Bonds, Series 2017B, bearing interest at a variable rate of 0.59% at December 31, 2020, due annually on May 1 of each year through 2033	37,000	38,120
BHS Revenue Bonds, Series 2013A, bearing interest at fixed rates between 3.50% and 5.00%, due in varying annual installments on August 15 of each year through 2034	74,320	79,750
BHS Revenue Note, Series 2013B, bearing interest at a fixed rate of 1.17% at December 31, 2020, due in monthly installments through 2020	—	371
Tax-exempt bonds issued on behalf of BHS by the Hospital Authority of St. Joseph County:		
BHS Revenue Bonds, Series 2016, bearing interest at a fixed rate of 1.39%, due in varying annual installments through 2046	48,005	48,800
BHS Revenue Bonds, Series 2013C, bearing interest at fixed rates between 3.75% and 5.00%, due in varying annual installments on August 15 of each year through 2044	46,130	46,130
Loans and Line of Credit issued on behalf of Community Hospital of Bremen by Lake City Bank:		
Loan payable to Lake City Bank dated August 4, 2004, semiannual payments of principal and interest at a variable rate (3.50% as of December 31, 2020), due January 1, 2025, secured by real property	1,918	2,267

Beacon Health System, Inc. and Affiliated Corporations

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

7. Long-Term Debt (continued)

	<u>2020</u>	<u>2019</u>
Loan on behalf of Community Hospital of Bremen by United States Department of Agriculture:		
Loan payable to United States Department of Agriculture dated April 25, 2005, semiannual payments of principal and interest, interest at a fixed rate of 4.25% due April 15, 2045, secured by real property	\$ 9,676	\$ 9,897
Mortgage – bearing interest at variable rates of 1.93% and 3.25% at December 31, 2020 and 2019, respectively, London Interbank Offered Rate (LIBOR) plus 1.50% due to varying annual installments on the last day of every month through 2020	–	108
Other obligations	120	181
	286,204	296,154
Bond issuance costs	(1,657)	(1,770)
Unamortized premium	11,008	11,843
	295,555	306,227
Less current portion	10,751	9,889
	\$ 284,804	\$ 296,338

In December 2018, the Indiana Finance Authority, on behalf of BHS, issued revenue bonds Series 2018 (2018 Bonds) in the principal amount of \$35,000. The 2018 Bonds are private placement bonds, bearing interest at a variable monthly interest rate. Proceeds from the bonds were utilized to fund existing and future capital projects.

In September 2017, the Indiana Finance Authority, on behalf of BHS, issued revenue refunding bonds Series 2017A (2017A) in the principal amount of \$37,240. The 2017A Bonds are private placement bonds, bearing interest at a variable monthly interest rate. The proceeds from 2017A were utilized to refund the MHSB Revenue Bonds, Series 2008A.

In September 2017, the Indiana Finance Authority, on behalf of BHS, issued revenue refunding bonds Series 2017B (2017B) in the principal amount of \$40,210. The 2017B Bonds are private placement bonds, bearing interest at a variable monthly interest rate. The proceeds from 2017B were utilized to refund the EGH Revenue Bonds, Series 2008.

Beacon Health System, Inc. and Affiliated Corporations

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

7. Long-Term Debt (continued)

In August 2016, the Hospital Authority of St. Joseph County issued Hospital Revenue Bonds, Series 2016 (Series 2016 Bonds), on behalf of the Obligated Group. The Series 2016 Bonds are \$50,000 private placement bonds bearing interest at a fixed rate of 1.39%, due in varying annual installments through 2046. Proceeds from the bonds were utilized to fund existing and future capital projects.

In May 2013, the Indiana Finance Authority, on behalf of BHS, issued revenue refunding bonds Series 2013A (2013A) in the principal amount of \$116,705. The interest rate for 2013A is a fixed rate varying between 2.00% and 5.00%. The proceeds from 2013A were utilized to refund the MHSB Revenue Bonds, Series 2008B; MHSB Revenue Bonds, Series 1998A; and EGH Revenue Bonds, Series 1998.

In May 2013, the Indiana Finance Authority, on behalf of BHS, issued a revenue note Series 2013B (2013B) in the principal amount of \$7,492. The interest rate for 2013B is a fixed rate of 1.17%. Proceeds from the bond were utilized for the purchase of a helicopter.

In May 2013, the Hospital Authority of St. Joseph County, on behalf of BHS, issued revenue bonds Series 2013C (2013C) in the principal amount of \$46,130. The interest rate for 2013C is a fixed rate varying between 3.75% and 5.00%. The proceeds from 2013C were utilized to refund the MHSB Revenue Bonds, Series 2007. The remaining proceeds are set aside in externally designated investments for future projects.

The Corporation is the Obligated Group Agent for the Obligated Group under the Master Trust Indentures. The Obligated Group includes the Corporation, MHSB, EGH, and BMG. MHF and BHV constitute designated affiliates under the terms of the Master Trust Indentures. The bonds are secured by pledged revenues of the Obligated Group and contain various covenants, including achievement of specified financial ratios and limitations on additional debt.

The loan agreements require maintenance of certain debt service coverage ratios, limit additional borrowings, and require compliance with various other restrictive covenants. The Corporation was in compliance with all covenants during 2020 and 2019.

In June 2018, BHS became the sole corporate member of CHB. CHB's long-term debt instruments at December 31, 2019, included a loan from Lake City Bank and a loan from the United States Department of Agriculture (USDA).

Beacon Health System, Inc. and Affiliated Corporations

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

7. Long-Term Debt (continued)

CHB's loan with Lake City Bank, dated August 4, 2004, bears interest at a variable rate equal to the prime rate, minus 0.50%, adjusted annually with a floor of 3.50% and a ceiling of 8.50%. CHB's outstanding loan with Lake City Bank is secured by virtually all assets of CHB.

CHB obtained a direct construction loan, dated April 25, 2005, from the USDA in the amount of \$12,000. The loan bears interest at a fixed of 4.25% to be repaid over 40 years. The loan is secured by the real property.

Interest capitalized for the years ended December 31, 2020 and 2019, was approximately \$938 and \$1,197, respectively.

Maturities of long-term debt and other obligations for each of the next five years are as follows:

2021	\$	10,754
2022		11,149
2023		11,315
2024		11,740
2025		12,376

8. Line of Credit

The Corporation has a \$2,000 revolving line of credit with 1st Source Bank. The line of credit was renewed and extended through May 31, 2021. Of the \$2,000 revolving line of credit, \$50 for the years ended December 31, 2020 and 2019, was segregated for the beneficiary of a self-insurance trust. Conversely, \$1,950 was available to be drawn upon at December 31, 2020 and 2019. No draws were taken by the Corporation in either 2020 or 2019. The interest rate on the line of credit is the prime rate minus 0.5%. No amounts were outstanding on the line of credit as of December 31, 2020 or 2019.

Beacon Health System, Inc. and Affiliated Corporations

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

9. Interest Rate and Basis Swaps

MHSB has various derivative instruments related to long-term debt obligations to manage the exposure on interest rates and MHSB's interest expense. Through the use of derivative financial instruments, MHSB is exposed to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contracts. When the fair value of the derivative contract is positive, the counterparty owes MHSB, which creates credit risk to MHSB. When the fair value of the derivative contract is negative, MHSB owes the counterparty, and there is no credit risk to MHSB at that point in time. MHSB minimizes the credit risk in derivative instruments by entering into transactions that require the counterparty to post collateral for the benefit of the fair value of the derivative contract. Market risk is the adverse effect on the value of the financial instrument that results from a change in interest rates. The management of market risk associated with interest rate changes is defined in MHSB's Swap Management Policy (the Policy). The Policy includes continuous monitoring of market conditions, emergent opportunities, and risks. Swap management is meant to be long term in nature, and any modifications to the program are reviewed for the long-term costs and benefits.

Management also mitigates risk through periodic reviews of its derivative position in the context of its total blended cost of capital.

In May 2019, MHSB terminated one Morgan Stanley swap with a notional amount of \$81,000. MHSB realized a net gain of \$723, which is included in nonoperating income on the consolidated statement of operations and changes in net assets.

The derivative instruments require adherence to collateral posting thresholds. For the years ended December 31, 2020 and 2019, the mark-to-market valuation on the swap portfolio was below the required collateral posting threshold of \$30,000 with PNC Bank, \$25,000 with Morgan Stanley, \$25,000 with Wells Fargo, and \$25,000 with Deutsche Bank.

Beacon Health System, Inc. and Affiliated Corporations

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

9. Interest Rate and Basis Swaps (continued)

The following is a summary of the outstanding fixed payor rate swaps as of December 31, 2020:

Origination Date	Notional Amounts	MHSB Receives	MHSB Pays	Maturity Date
March 2006	\$ 36,535	61.90% of 30-day LIBOR plus 0.31%	3.5150%	August 2033
March 2003	6,750	65.00% of 30-day LIBOR plus 0.45%	3.8100	August 2034

The following is a summary of the outstanding fixed payor rate swaps as of December 31, 2019:

Origination Date	Notional Amounts	MHSB Receives	MHSB Pays	Maturity Date
March 2006	\$ 36,780	61.90% of 30-day LIBOR plus 0.31%	3.5150%	August 2033
March 2003	7,050	65.00% of 30-day LIBOR plus 0.45%	3.8100	August 2034

The following is a summary of the outstanding basis rate swaps as of December 31, 2020:

Origination Date	Notional Amounts	MHSB Receives	MHSB Pays	Maturity Date
January 2007	\$ 42,000	74.600% of 1M LIBOR	SIFMA tax-exempt index + 0.0715%	January 2041
March 2001	140,000	75.125% of 3M LIBOR	SIFMA tax-exempt index	March 2031
July 2009	63,000	74.600% of 1M LIBOR	SIFMA tax-exempt index + 0.1700%	January 2041

Beacon Health System, Inc. and Affiliated Corporations

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

9. Interest Rate and Basis Swaps (continued)

The following is a summary of the outstanding basis rate swaps as of December 31, 2020:

Origination Date	Notional Amounts	MHSB Receives	MHSB Pays	Maturity Date
January 2007	\$ 42,000	74.600% of 1M LIBOR	SIFMA tax-exempt index + 0.0715%	January 2041
March 2001	140,000	75.125% of 3M LIBOR	SIFMA tax-exempt index	March 2031
July 2009	63,000	74.600% of 1M LIBOR	SIFMA tax-exempt index + 0.1700%	January 2041

Net interest paid or received under the above swap agreements is included in interest expense. The net differential for MHSB as a result of the swap agreements amounted to payments of approximately \$1,467 for the year ended December 31, 2020, which is reflected as an increase in interest expense, and receipts of approximately \$7 for the year ended December 31, 2019, which is reflected as a decrease in interest expense. The swap agreements do not qualify for hedge accounting; therefore, the change in the fair value of the swap agreements is recorded as an unrealized nonoperating (loss) gain of approximately \$(3,741) and \$353 for the years ended December 31, 2020 and 2019, respectively.

The fair value of derivative instruments at December 31 is as follows:

	Balance Sheet Location	2020	2019
Derivatives not designated as hedging instruments:			
Interest rate contracts	Interest rate and basis swap receivable	\$ —	\$ 323
	Interest rate and basis swaps payable	(18,302)	(14,884)
		<u>\$ (18,302)</u>	<u>\$ (14,561)</u>

Beacon Health System, Inc. and Affiliated Corporations

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

10. Liquidity and Availability of Resources

As of December 31 financial assets and liquidity resources available within one year for general expenditure, such as operating expenses, scheduled principal payments on debt, and capital expenditures not financed with debt, were as follows:

	<u>2020</u>	<u>2019</u>
Cash and cash equivalents	\$ 115,392	\$ 67,962
Short-term investments	56,231	13,201
Internally designated investments	812,663	755,371
Restricted cash	5,408	5,034
Externally designated investments – insurance trust	2,952	2,854
Board-designated endowment	30,090	27,947
Endowment investments	9,421	8,712
Total financial assets	<u>1,032,157</u>	881,081
Less amounts unavailable for general expenditure due to:		
Restricted bond funds	(670)	(7,029)
Restricted by donors with purpose restrictions	(14,957)	(13,847)
Restricted by donors in perpetuity	(400)	(475)
Restricted for insurance trust	(2,952)	(2,854)
Board designated	(30,090)	(27,947)
Add liquidity resources:		
Unused line of credit	<u>1,950</u>	1,950
Total financial assets available for general expenditure within one year	<u>\$ 985,038</u>	<u>\$ 830,879</u>

BHS has various investments to maintain and strengthen its financial well-being and liquidity. The management of investments is defined by the Corporation's investment policy and is under the direction of an investment committee consisting of external advisors and BHS employees with the knowledge and understanding to undertake the monitoring of market conditions, emergent opportunities, and risks to help maximize the financial strength of the investments while considering the liquidity needs of BHS.

Beacon Health System, Inc. and Affiliated Corporations

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

11. Investments

Total investment return for the years ended December 31 is summarized as follows:

	<u>2020</u>	<u>2019</u>
Investment return:		
Net unrealized gains on investments	\$ 43,848	\$ 32,707
Net realized gains on investments	9,158	42,443
Net equity earnings on alternative investments	11,986	16,760
	<u>\$ 64,992</u>	<u>\$ 91,910</u>
Reported as:		
Investment income, net (nonoperating)	\$ 64,225	\$ 90,848
Investment income (net assets with donor restrictions)	767	1,062
	<u>\$ 64,992</u>	<u>\$ 91,910</u>

The Corporation's investments are exposed to various kinds and levels of risk. Equity mutual funds expose the Corporation to market risk, performance risk, and liquidity risk. Market risk is the risk associated with major movements of the equity markets. Performance risk is the risk associated with a corporation's operating performance. Fixed-income securities expose the Corporation to interest rate risk, credit risk, and liquidity risk. As interest rates change, the value of many fixed-income securities is affected, including those with fixed interest rates. Credit risk is the risk that the obligor of the security will not fulfill its obligations. Liquidity risk is affected by the willingness of market participants to buy and sell given securities. Liquidity risk tends to be higher for equities related to small capitalization companies. Due to the volatility of the capital markets, there is a reasonable possibility of changes in fair value, resulting in additional gains and losses in the near term.

Beacon Health System, Inc. and Affiliated Corporations

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

12. Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable, and accounts payable and accrued expenses are reasonable estimates of their fair values due to the short-term nature of these financial instruments.

Accounting Standards Codification (ASC) 820-10-50-2, *Fair Value Measurement – Overall – Disclosure*, establishes a three-level valuation hierarchy. The valuation hierarchy is 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 an active market and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instruments.
- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Beacon Health System, Inc. and Affiliated Corporations

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

12. Fair Value of Financial Instruments (continued)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The following tables present the financial instruments carried as of December 31, by caption, on the consolidated balance sheets by the valuation hierarchy defined above for those instruments carried at fair value, as well as the alternative investments that are reported on the equity method of accounting. Deferred compensation investments are included in other assets on the consolidated balance sheets.

	2020					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
Assets						
Short-term investments ^(a)	\$ 56,231	\$ —	\$ —	\$ 56,231	\$ —	\$ 56,231
Internally designated investments:						
Blended fund	255,935	—	—	255,935	—	255,935
Total mutual funds	255,935	—	—	255,935	—	255,935
Common stock ^(a)	61,990	—	—	61,990	—	61,990
Alternatives:						
Hedge funds	—	—	—	—	27,376	27,376
Emerging markets	—	—	—	—	100,744	100,744
Master limited partnership	—	—	—	—	26,091	26,091
Private equity	—	—	—	—	87,948	87,948
Real estate investment trust	—	—	—	—	36,277	36,277
International	—	—	—	—	1,610	1,610
Commingled funds	—	—	—	—	120,859	120,859
Other	—	—	—	—	180	180
Long/short equity	—	—	—	—	19,431	19,431
Relative value	—	—	—	—	38,533	38,533
Tactical trading	—	—	—	—	35,689	35,689
Total alternatives	—	—	—	—	494,738	494,738
Total internally designated investments	317,925	—	—	317,925	494,738	812,663

Beacon Health System, Inc. and Affiliated Corporations

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

12. Fair Value of Financial Instruments (continued)

	2020					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
Assets (continued)						
Restricted cash ^(a)	\$ 5,408	\$ –	\$ –	\$ 5,408	\$ –	\$ 5,408
Externally designated investment – insurance trust:						
Fixed income ^(a)	2,952	–	–	2,952	–	2,952
Board-designated endowment:						
Mutual funds: ^(a)						
Equities	1,477	–	–	1,477	–	1,477
Blended fund	17,110	–	–	17,110	–	17,110
Fixed income ^{(a), (b)}	439	105	–	544	–	544
Alternatives	–	–	–	–	10,959	10,959
Total board-designated endowment	19,026	105	–	19,131	10,959	30,090
Endowment:						
Mutual funds: ^(a)						
Fixed income	–	–	–	–	–	–
Blended fund	5,743	–	–	5,743	–	5,743
Alternatives	–	–	–	–	3,678	3,678
Total endowment	5,743	–	–	5,743	3,678	9,421
Swap ^(c)	–	–	–	–	–	–
Total	\$ 407,285	\$ 105	\$ –	\$ 407,390	\$ 509,375	\$ 916,765
Liabilities						
Swaps ^(c)	\$ –	\$ –	\$ (18,302)	\$ (18,302)	\$ –	\$ (18,302)
Total	\$ –	\$ –	\$ (18,302)	\$ (18,302)	\$ –	\$ (18,302)

Beacon Health System, Inc. and Affiliated Corporations

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

12. Fair Value of Financial Instruments (continued)

	2019					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
Assets						
Short-term investments ^(a)	\$ 13,201	\$ —	\$ —	\$ 13,201	\$ —	\$ 13,201
Internally designated investments:						
Blended fund	251,780	—	—	251,780	—	251,780
Total mutual funds	251,780	—	—	251,780	—	251,780
Common stock ^(a)	71,493	—	—	71,493	—	71,493
Alternatives:						
International equity	—	—	—	—	30	30
Master limited partnership	—	—	—	—	36,562	36,562
Private equity	—	—	—	—	66,406	66,406
Real estate investment trust	—	—	—	—	35,652	35,652
International	—	—	—	—	14,036	14,036
Commingled funds	—	—	—	—	205,283	205,283
Other	—	—	—	—	36,042	36,042
Long/short hedge	—	—	—	—	12,177	12,177
Global	—	—	—	—	5,490	5,490
Multi-strategy	—	—	—	—	20,420	20,420
Total alternatives	—	—	—	—	432,098	432,098
Total internally designated investments	323,373	—	—	323,373	432,098	755,371

Beacon Health System, Inc. and Affiliated Corporations

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

12. Fair Value of Financial Instruments (continued)

	2019					
	Level 1	Level 2	Level 3	Fair Value	Equity Method	Carrying Value
Assets (continued)						
Restricted cash ^(a)	\$ 5,034	\$ —	\$ —	\$ 5,034	\$ —	\$ 5,034
Externally designated investment – insurance trust:						
Fixed income ^(a)	2,854	—	—	2,854	—	2,854
Board-designated endowment:						
Mutual funds: ^(a)						
Equities	1,356	—	—	1,356	—	1,356
Blended fund	15,462	—	—	15,462	—	15,462
Fixed income ^{(a), (b)}	453	—	—	453	—	453
Equities ^(a)	1,628	—	—	1,628	—	1,628
Alternatives	—	—	—	—	9,048	9,048
Total board-designated endowment	18,899	—	—	18,899	9,048	27,947
Endowment:						
Mutual funds: ^(a)						
Blended fund	5,154	—	—	5,154	—	5,154
Equities ^(a)	542	—	—	542	—	542
Alternatives	—	—	—	—	3,016	3,016
Total endowment	5,696	—	—	5,696	3,016	8,712
Swap ^(c)	—	—	323	323	—	323
Total	\$ 368,957	\$ —	\$ 323	\$ 369,280	\$ 444,162	\$ 813,442
Liabilities						
Swaps ^(c)	\$ —	\$ —	\$ (14,884)	\$ (14,884)	\$ —	\$ (14,884)
Total	\$ —	\$ —	\$ (14,884)	\$ (14,884)	\$ —	\$ (14,884)

(a) Pricing for mutual funds, short-term investments, equities, and government obligations is based on the open market and is valued on a daily basis.

(b) Pricing is based on the fair value of the securities and is valued on a monthly basis. Information used to value this account is provided by International Data Corp. (IDC). In the event that a security is not actively traded in the open market, the characteristics are matched to a comparable issue from the IDC data to appropriately value the holding.

Beacon Health System, Inc. and Affiliated Corporations

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

12. Fair Value of Financial Instruments (continued)

- (c) Pricing is based on discounted cash flows to reflect a credit spread adjustment to the LIBOR discount curve in order to reflect “nonperformance” risk. The credit spread adjustment is derived from how other comparable entities’ bonds price and trade in the market. As the credit spread adjustment is a significant component of the swap valuation and is an unobservable input, the swaps have been classified as Level 3.

The following table sets forth a summary of changes in the fair value of the Corporation’s Level 3 swaps for the years ended December 31:

	<u>2020</u>	<u>2019</u>
Balance, beginning of year	\$ (14,561)	\$ (14,051)
Unrealized (losses) gains, net	(3,741)	353
Realized gains, net	–	723
Sales of swaps	–	(1,586)
Balance, end of year	<u>\$ (18,302)</u>	<u>\$ (14,561)</u>

For the year ended December 31, 2020, the Corporation recorded approximately \$3,741 in nonoperating losses, which relates to losses of \$4,318 due to the change in the swaps’ value and gains of \$577 to reflect the fair value of the uncollateralized portion of the swap balance. For the year ended December 31, 2019, the Corporation recorded approximately \$353 in non-operating gains, which relates to losses of \$483 due to the change in the swaps’ value and gains of \$28 to reflect the fair value of the uncollateralized portion of the swap balance.

Beacon Health System, Inc. and Affiliated Corporations

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

13. Functional Expenses

The Corporation provides general health care services to residents within its geographic location. Expenses related to this and general and administrative functions for the years ended December 31 are as follows:

	2020			2019		
	Health Care Services	Administrative Functions	Total	Health Care Services	Administrative Functions	Total
Salaries and wages	\$ 416,564	\$ 42,645	\$ 459,209	\$ 413,288	\$ 36,695	\$ 449,983
Employee benefits	81,684	13,292	94,976	95,182	13,155	108,337
Supplies and other	259,571	12,600	272,171	259,042	5,680	264,722
Professional fees and purchased services	86,739	32,102	118,841	84,958	31,003	115,961
Depreciation and amortization	54,754	7,700	62,454	54,969	5,043	60,012
Interest	7,660	156	7,816	7,502	314	7,816
Total	\$ 906,972	\$ 108,495	\$1,015,467	\$ 914,941	\$ 91,890	\$1,006,831

14. Commitments

BMG is a guarantor for a portion of a loan of an unconsolidated joint venture, Valparaiso Medical Development, LLC, in which BMG records an equity interest. The portion of debt guaranteed by BMG is a maximum of \$6,560 and \$4,316 at December 31, 2020 and 2019, respectively. No amounts have been paid or accrued pursuant to this guarantee as of December 31, 2020 or 2019. The loan is collateralized by the assets, including the facility and land, held by Valparaiso Medical Development, LLC.

The Corporation has total commitments to invest \$184,300 in certain hedge funds and alternative investments. During the years ended December 31, 2020 and 2019, the Corporation invested approximately \$16,404 and \$32,266, respectively. The Corporation had a remaining unfunded commitment of approximately \$48,655 at December 31, 2020.

Beacon Health System, Inc. and Affiliated Corporations

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

15. Professional Liability Insurance

The Corporation is involved in lawsuits and various governmental investigations, audits, reviews, and administrative proceedings arising in the ordinary course of business. Additionally, the Corporation may be subject to additional claims alleging professional liability for medical malpractice. The Corporation has a claims-made policy that covers all entities and has a \$25,000 deductible per claim. Historically, MHSB and EGH have obtained separate professional liability insurance coverage under claims-made policies. The claims-made policy covers all years other than years that were self-funded. MHSB was self-funded for its professional and general liability coverage for the period of December 1, 2003 to November 30, 2009. EGH was self-funded for its professional and general liability coverage for the period of March 1, 2010 to April 1, 2012. The Indiana Medical Malpractice Act has provided recovery up to \$1,250, per occurrence, with the first \$250 covered by the respective entity, for claims prior to July 1, 2017. For the period of July 1, 2017 to June 30, 2019, the coverage limit was \$1,650, per occurrence, with the first \$400 covered by the respective entity. Effective July 1, 2019, the coverage limit was increased to \$1,800, per occurrence, with the first \$500 covered by the respective entity. MHSB maintains a trust fund for its self-insurance program, which it will continue to maintain until all claims have been settled. The fair value of the trust fund at December 31, 2020 and 2019, was approximately \$2,952 and \$2,854, respectively. The amount of malpractice and general liability claims, including a component for incurred but not reported claims, was approximately \$4,927 and \$5,000, gross of an insurance recoverable at December 31, 2020 and 2019, respectively, which is included in pension and other liabilities. The interest rate used to discount these claims was 3% at December 31, 2020 and 2019. In addition, at December 31, 2020 and 2019, the Corporation recognized a recoverable insurance asset of approximately \$4,287, which is included in deferred charges and other assets.

16. Income Taxes

The Corporation and its related affiliates, except for BHV, have been determined to qualify as exempt from federal income tax under Section 501(a) as organizations described in Section 501(c)(3) of the Code.

Most of the income received by the Corporation and its related affiliates, except for BHV, is exempt from taxation, as the income is related to the mission of the organization. Accordingly, there is no material provision for income tax for these entities. However, some of the income received by exempt entities is subject to taxation as unrelated business income. The Corporation and its subsidiaries file federal and various state income tax returns in the United States.

Beacon Health System, Inc. and Affiliated Corporations

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

16. Income Taxes (continued)

ASC 740, *Income Taxes*, requires that realization of an uncertain income tax position is more likely than not (i.e., greater than 50% likelihood of receiving a benefit) before it is recognized in the financial statements as the amount most likely to be realized assuming a review by tax authorities having all relevant information and applying current conventions. This interpretation also clarifies the financial statement classification of tax-related penalties and interest and sets forth new disclosures regarding unrecognized tax benefits. No amount was recorded for the years ended December 31, 2020 or 2019.

17. Net Assets Without Donor Restrictions

Net assets without donor restrictions are comprised of the following at December 31:

	<u>2020</u>	<u>2019</u>
Undesignated	\$ 1,520,051	\$ 1,415,501
Board-designated endowment	30,090	27,947
	<u>\$ 1,550,141</u>	<u>\$ 1,443,448</u>

Board-Designated Endowment – The Board has designated a portion of net assets without donor restrictions as a board-designated endowment for the purpose of funding the Foundation’s operational expenses.

18. Net Assets With Donor Restrictions

Net assets with donor restrictions are available for the following purposes at December 31:

	<u>2020</u>	<u>2019</u>
Net assets currently available for:		
Children’s services	\$ 2,534	\$ 2,480
Education	2,346	2,626
Patient care	8,698	7,702
System priorities	953	705
Community impact	426	334
Quasi-endowments	400	475
	<u>\$ 15,357</u>	<u>\$ 14,322</u>

Beacon Health System, Inc. and Affiliated Corporations

Notes to Consolidated Financial Statements (continued)

(Dollars in Thousands)

18. Net Assets With Donor Restrictions (continued)

The various purposes of the above donor restricted amounts are as follows:

Children's services – Programs and services for pediatric patients throughout the Corporation

Education – Formal and continuing education

Patient care – Specific patient care services lines (i.e., cancer, cardiac, and trauma)

System priorities – Specific system initiatives as determined throughout the Corporation requiring formal approval and funding

Community impact – Initiatives that focus on preventive care and education throughout the community

Quasi-endowments – Designated to be held in perpetuity, income generated to be used for indigent care and/or area of greatest need

19. Subsequent Events

The Corporation evaluated events and transactions occurring subsequent to December 31, 2020 through March 4, 2021, the date of issuance of the accompanying consolidated financial statements. During this period, there were no subsequent events requiring recognition or disclosure in the consolidated financial statements.

Supplementary Information

Report of Independent Auditors on Supplementary Information

The Board of Directors
Beacon Health System, Inc. and Affiliated Corporations

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The following financial information is presented for purposes of additional analysis and is 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

March 4, 2021

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet
(In Thousands)

December 31, 2020

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Assets									
Current assets:									
Cash and cash equivalents	\$ 115,392	\$ –	\$ 25,189	\$ 2,768	\$ 171	\$ 1,101	\$ 16,038	\$ 65,559	\$ 4,566
Short-term investments	56,231	–	12	–	1,288	–	–	54,931	–
Patient accounts receivable	219,756	(3,663)	122,775	29,250	–	201	64,919	1,945	4,329
Due from third-party payors	37,690	–	35,323	1,243	–	–	1,019	–	105
Other receivables	10,865	–	825	4,314	213	198	359	4,955	1
Other current assets	1,287	–	388	–	–	681	–	218	–
Inventories	30,629	–	17,679	–	–	120	8,534	4,012	284
Prepaid expenses	15,517	–	1,896	654	–	–	923	12,001	43
Due from affiliates	–	(15,204)	945	1,803	–	–	2,954	9,502	–
Total current assets	487,367	(18,867)	205,032	40,032	1,672	2,301	94,746	153,123	9,328
Assets limited as to use:									
Internally designated investments	812,663	–	–	–	–	–	–	812,663	–
Restricted cash	5,408	–	–	–	4,154	–	–	–	1,254
Externally designated investments – insurance trust	2,952	–	2,921	21	–	10	–	–	–
Board-designated endowment	30,090	–	–	–	30,090	–	–	–	–
Endowment and temporarily restricted investments	9,421	–	–	–	1,528	–	7,893	–	–
	860,534	–	2,921	21	35,772	10	7,893	812,663	1,254
Property and equipment:									
Land	53,920	–	21,868	4,015	–	–	3,846	23,412	779
Buildings and improvements	894,527	–	527,881	53,686	94	1,458	266,242	35,626	9,540
Furniture and equipment	575,924	–	315,321	36,471	164	2,689	134,003	83,780	3,496
Construction-in-progress	11,336	–	2,097	4,742	–	–	1,921	2,562	14
	1,535,707	–	867,167	98,914	258	4,147	406,012	145,380	13,829
Less allowances for depreciation and amortization	854,141	–	514,073	52,587	187	3,486	229,792	51,239	2,777
	681,566	–	353,094	46,327	71	661	176,220	94,141	11,052
Deferred charges and other assets	75,603	(12,367)	5,748	16,453	213	10,176	3,692	49,929	1,759
Interest in net assets of recipient organization	–	(7,464)	7,464	–	–	–	–	–	–
Total assets	\$ 2,105,070	\$ (38,698)	\$ 574,259	\$ 102,833	\$ 37,728	\$ 13,148	\$ 282,551	\$ 1,109,856	\$ 23,393

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet (continued)
(In Thousands)

December 31, 2020

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Liabilities and net assets									
Current liabilities:									
Accounts payable	\$ 69,891	\$ –	\$ 26,155	\$ 15,375	\$ 2	\$ 63	\$ 19,031	\$ 8,368	\$ 897
Accrued salaries and benefits	51,466	–	21,531	10,206	–	–	10,186	9,543	–
Accrued expenses	625	(3,663)	2,049	120	–	–	1,048	979	92
Other current liabilities	1,263	–	379	–	–	668	–	216	–
Due to third-party payors	53,069	–	29,298	(5)	–	–	21,609	–	2,167
Due to affiliates	–	(15,204)	–	–	–	8,590	–	1,193	5,421
Current maturities of long-term debt	10,751	–	4,099	–	–	–	3,078	2,995	579
Total current liabilities	187,065	(18,867)	83,511	25,696	2	9,321	54,952	23,294	9,156
Noncurrent liabilities:									
Long-term debt, less current maturities	284,804	–	134,802	123	–	–	61,723	77,141	11,015
Other liabilities	49,401	–	27,422	1,462	–	3,200	12,182	3,642	1,493
Interest rate and basis swaps	18,302	–	18,302	–	–	–	–	–	–
Total liabilities	539,572	(18,867)	264,037	27,281	2	12,521	128,857	104,077	21,664
Net assets:									
Without donor restrictions	1,550,141	(12,367)	302,758	75,552	30,262	627	145,801	1,005,779	1,729
With donor restrictions	15,357	(7,464)	7,464	–	7,464	–	7,893	–	–
Total net assets	1,565,498	(19,831)	310,222	75,552	37,726	627	153,694	1,005,779	1,729
Total liabilities and net assets	\$ 2,105,070	\$ (38,698)	\$ 574,259	\$ 102,833	\$ 37,728	\$ 13,148	\$ 282,551	\$ 1,109,856	\$ 23,393

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet
(In Thousands)

December 31, 2019

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Assets									
Current assets:									
Cash and cash equivalents	\$ 67,962	\$ –	\$ 11,977	\$ 3,665	\$ 26	\$ 604	\$ 11,553	\$ 38,792	\$ 1,345
Short-term investments	13,201	–	12	–	1,219	–	–	11,970	–
Patient accounts receivable	180,883	(3,931)	107,471	20,704	–	448	52,105	1,088	2,998
Due from third-party payors	18,626	–	15,747	1,401	–	–	1,217	–	261
Other receivables	7,490	–	3,339	1,280	292	197	484	1,898	–
Other current assets	1,146	–	499	–	–	647	–	–	–
Inventories	24,908	–	17,209	–	–	136	7,304	–	259
Prepaid expenses	19,365	–	2,015	492	–	–	1,267	15,543	48
Due from affiliates	–	(10,398)	770	405	–	–	–	9,223	–
Total current assets	333,581	(14,329)	159,039	27,947	1,537	2,032	73,930	78,514	4,911
Assets limited as to use:									
Internally designated investments	755,371	–	–	–	–	–	–	755,371	–
Restricted cash	5,034	–	–	–	3,780	–	–	–	1,254
Externally designated investments – insurance trust	2,854	–	2,824	20	–	10	–	–	–
Board-designated endowment	27,947	–	–	–	27,947	–	–	–	–
Endowment and temporarily restricted investments	8,712	–	–	–	1,368	–	7,344	–	–
	799,918	–	2,824	20	33,095	10	7,344	755,371	1,254
Property and equipment:									
Land	51,925	–	21,501	4,015	–	–	3,846	21,784	779
Buildings and improvements	856,141	–	529,157	51,650	94	1,431	257,633	7,034	9,142
Furniture and equipment	529,342	–	309,525	35,612	163	2,697	123,834	54,854	2,657
Construction-in-progress	48,801	–	4,688	2,520	–	23	10,385	31,135	50
	1,486,209	–	864,871	93,797	257	4,151	395,698	114,807	12,628
Less allowances for depreciation and amortization	794,488	–	489,637	47,565	168	3,359	212,357	39,840	1,562
	691,721	–	375,234	46,232	89	792	183,341	74,967	11,066
Deferred charges and other assets	71,600	(12,367)	6,294	16,284	315	10,871	3,692	44,752	1,759
Interest in net assets of recipient organization	–	(6,978)	6,978	–	–	–	–	–	–
Interest rate swap	323	–	323	–	–	–	–	–	–
Total assets	\$ 1,897,143	\$ (33,674)	\$ 550,692	\$ 90,483	\$ 35,036	\$ 13,705	\$ 268,307	\$ 953,604	\$ 18,990

Beacon Health System, Inc. and Affiliated Corporations

Details of Consolidated Balance Sheet (continued)
(In Thousands)

December 31, 2019

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Liabilities and net assets									
Current liabilities:									
Accounts payable	\$ 55,291	\$ –	\$ 20,236	\$ 9,812	\$ –	\$ 638	\$ 12,491	\$ 11,693	\$ 421
Accrued salaries and benefits	39,169	(3,931)	19,037	8,490	–	465	9,484	5,574	50
Accrued expenses	4,294	–	2,103	–	–	–	868	1,211	112
Other current liabilities	1,125	–	478	–	–	647	–	–	–
Due to third-party payors	498	–	302	–	–	–	176	–	20
Due to affiliates	–	(10,398)	–	–	257	6,202	4	713	3,222
Current maturities of long-term debt	9,889	–	4,373	–	–	–	2,901	2,045	570
Total current liabilities	110,266	(14,329)	46,529	18,302	257	7,952	25,924	21,236	4,395
Noncurrent liabilities:									
Long-term debt, less current maturities	296,338	–	139,396	181	–	–	65,056	80,111	11,594
Other liabilities	17,885	–	9,891	23	–	3,869	1,753	2,349	–
Interest rate and basis swaps	14,884	–	14,884	–	–	–	–	–	–
Total liabilities	439,373	(14,329)	210,700	18,506	257	11,821	92,733	103,696	15,989
Net assets:									
Without donor restrictions	1,443,448	(12,367)	333,014	71,977	27,801	1,884	168,230	849,908	3,001
With donor restrictions	14,322	(6,978)	6,978	–	6,978	–	7,344	–	–
Total net assets	1,457,770	(19,345)	339,992	71,977	34,779	1,884	175,574	849,908	3,001
Total liabilities and net assets	\$ 1,897,143	\$ (33,674)	\$ 550,692	\$ 90,483	\$ 35,036	\$ 13,705	\$ 268,307	\$ 953,604	\$ 18,990

Beacon Health System, Inc. and Affiliated Corporations

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

Year Ended December 31, 2020

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Unrestricted revenue, gains, and other support									
Patient service revenue	\$ 985,255	\$ –	\$ 555,056	\$ 116,389	\$ –	\$ 2,808	\$ 282,515	\$ 8,897	\$ 19,590
Other revenue	74,993	(8,820)	30,192	17,943	1,348	2,136	18,996	12,745	453
Net assets released from restrictions used for operations	929	–	417	121	108	–	112	171	–
	<u>1,061,177</u>	<u>(8,820)</u>	<u>585,665</u>	<u>134,453</u>	<u>1,456</u>	<u>4,944</u>	<u>301,623</u>	<u>21,813</u>	<u>20,043</u>
Expenses									
Salaries and wages	459,209	–	162,678	147,577	653	2,702	90,582	46,499	8,518
Employee benefits	94,976	–	35,628	23,324	232	616	19,155	14,276	1,745
Supplies and other	272,171	(1,457)	143,594	27,338	635	1,713	80,569	15,002	4,777
Management fees	–	–	47,151	14,427	155	720	25,567	(90,009)	1,989
Professional fees and purchased services	118,841	(7,363)	42,775	11,371	44	305	28,980	40,100	2,629
Depreciation and amortization	62,454	–	30,198	5,511	19	146	17,493	7,872	1,215
Interest	7,816	–	6,078	–	–	–	1,101	156	481
	<u>1,015,467</u>	<u>(8,820)</u>	<u>468,102</u>	<u>229,548</u>	<u>1,738</u>	<u>6,202</u>	<u>263,447</u>	<u>33,896</u>	<u>21,354</u>
Income (loss) from operations	45,710	–	117,563	(95,095)	(282)	(1,258)	38,176	(12,083)	(1,311)
Nonoperating income (expenses)									
Investment income, net	64,225	–	418	55	2,074	1	(68)	61,706	39
Unrealized loss on swap transactions, net	(3,741)	–	(3,741)	–	–	–	–	–	–
Revenue and gains in excess of (less than) expenses	<u>106,194</u>	<u>–</u>	<u>114,240</u>	<u>(95,040)</u>	<u>1,792</u>	<u>(1,257)</u>	<u>38,108</u>	<u>49,623</u>	<u>(1,272)</u>

Beacon Health System, Inc. and Affiliated Corporations

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

Year Ended December 31, 2020

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Net assets without donor restrictions									
Revenue and gains in excess of (less than) expenses	\$ 106,194	\$ -	\$ 114,240	\$ (95,040)	\$ 1,792	\$ (1,257)	\$ 38,108	\$ 49,623	\$ (1,272)
Net assets released from restrictions used for capital purposes	424	-	424	-	-	-	-	-	-
Net assets released from restriction by donor	75	-	-	-	75	-	-	-	-
Other	-	-	(144,920)	98,615	594	-	(60,537)	106,248	-
Increase (decrease) in net assets without donor restrictions	106,693	-	(30,256)	3,575	2,461	(1,257)	(22,429)	155,871	(1,272)
Net assets with donor restrictions									
Purpose-restricted contributions	1,696	-	-	-	1,696	-	-	-	-
Investment income	767	-	-	-	218	-	549	-	-
Reclass of contribution restriction by donor	(75)	-	-	-	(75)	-	-	-	-
Net assets released from restrictions used for operating and capital purposes	(1,353)	-	-	-	(1,353)	-	-	-	-
Change in interest in recipient organization	-	(561)	561	-	-	-	-	-	-
Increase (decrease) in net assets with donor restrictions	1,035	(561)	561	-	486	-	549	-	-
Increase (decrease) in net assets	107,728	(561)	(29,695)	3,575	2,947	(1,257)	(21,880)	155,871	(1,272)
Net assets at beginning of year	1,457,770	(19,345)	339,992	71,977	34,779	1,884	175,574	849,908	3,001
Net assets at end of year	\$ 1,565,498	\$ (19,906)	\$ 310,297	\$ 75,552	\$ 37,726	\$ 627	\$ 153,694	\$ 1,005,779	\$ 1,729

Beacon Health System, Inc. and Affiliated Corporations

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

Year Ended December 31, 2019

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Unrestricted revenue, gains, and other support									
Patient service revenue	\$ 985,708	\$ –	\$ 539,841	\$ 123,095	\$ –	\$ 4,511	\$ 290,629	\$ 8,924	\$ 18,708
Other revenue	46,347	(6,212)	24,973	9,414	1,142	2,618	8,336	5,614	462
Net assets released from restrictions used for operations	926	–	587	29	115	–	61	134	–
	1,032,981	(6,212)	565,401	132,538	1,257	7,129	299,026	14,672	19,170
Expenses									
Salaries and wages	449,983	–	165,239	143,227	685	3,913	88,107	40,437	8,375
Employee benefits	108,337	–	41,741	25,723	160	1,139	23,102	14,515	1,957
Supplies and other	264,722	(6,212)	144,257	22,921	373	3,397	82,472	13,380	4,134
Management fees	–	–	41,724	13,583	218	918	22,855	(81,127)	1,829
Professional fees and purchased services	115,961	–	43,124	10,003	69	385	28,533	31,727	2,120
Depreciation and amortization	60,012	–	30,323	5,544	12	235	17,626	5,207	1,065
Interest	7,816	–	5,186	1	–	–	1,791	314	524
	1,006,831	(6,212)	471,594	221,002	1,517	9,987	264,486	24,453	20,004
Income (loss) from operations	26,150	–	93,807	(88,464)	(260)	(2,858)	34,540	(9,781)	(834)
Nonoperating income (expenses)									
Investment income, net	90,848	–	181	71	2,952	6	22	87,572	44
Unrealized gains on swap transactions, net	353	–	353	–	–	–	–	–	–
Realized gain on swap termination	723	–	723	–	–	–	–	–	–
Loss on lease termination	(692)	–	–	–	–	(692)	–	–	–
Revenue and gains in excess of (less than) expenses	117,382	–	95,064	(88,393)	2,692	(3,544)	34,562	77,791	(790)

Beacon Health System, Inc. and Affiliated Corporations

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

Year Ended December 31, 2019

	Consolidated	Eliminations	Memorial Hospital of South Bend, Inc.	Beacon Medical Group, Inc.	Beacon Health Foundation, Inc.	Beacon Health Ventures, Inc.	Elkhart General Hospital, Inc.	Beacon Health System, Inc.	Community Hospital of Bremen, Inc.
Net assets without donor restrictions									
Revenue and gains in excess of (less than) expenses	\$ 117,382	\$ –	\$ 95,064	\$ (88,393)	\$ 2,692	\$ (3,544)	\$ 34,562	\$ 77,791	\$ (790)
Net assets released from restrictions used for									
capital purposes	815	–	734	–	–	–	81	–	–
Other	–	–	(75,158)	84,869	–	–	(27,581)	17,870	–
Contribution of net assets of Community Hospital of Bremen	–	–	–	–	12	–	–	–	(12)
Increase (decrease) in net assets without donor restrictions	118,197	–	20,640	(3,524)	2,704	(3,544)	7,062	95,661	(802)
Net assets with donor restrictions									
Purpose-restricted contributions	2,588	–	–	–	2,588	–	–	–	–
Investment income	1,062	–	–	–	298	–	764	–	–
Net assets released from restrictions									
used for operating and capital purposes	(1,741)	–	–	–	(1,741)	–	–	–	–
Change in interest in recipient organization	–	(1,220)	1,220	–	–	–	–	–	–
Increase (decrease) in net assets with donor restrictions	1,909	(1,220)	1,220	–	1,145	–	764	–	–
Increase (decrease) in net assets	120,106	(1,220)	21,860	(3,524)	3,849	(3,544)	7,826	95,661	(802)
Net assets at beginning of year	1,337,664	(18,125)	318,132	75,501	30,930	5,428	167,748	754,247	3,803
Net assets at end of year	\$ 1,457,770	\$ (19,345)	\$ 339,992	\$ 71,977	\$ 34,779	\$ 1,884	\$ 175,574	\$ 849,908	\$ 3,001

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