Deaconess

CONSOLIDATED FINANCIAL STATEMENTS

SEPTEMBER 30, 2019 AND 2018

CPAS / ADVISORS

blue

DEACONESS HEALTH SYSTEM

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REPORT OF INDEPENDENT AUDITORS

Board of Directors
Deaconess Health System
Evansville, Indiana

We have audited the accompanying consolidated financial statements of Deaconess Health System (the System), which comprise the consolidated balance sheets as of September 30, 2019 and 2018, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the System’s preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the System'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 consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the System as of September 30, 2019 and 2018, and the results of its operations, changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Directors
Deaconess Health System
Evansville, Indiana

Change in Accounting Principles

As discussed in Note 2 to the consolidated financial statements, effective October 1, 2018, the System adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2016-14, *Presentation of Financial Statement of Not-for-Profit Entities*, FASB ASU No. 2014-09, *Revenue from Contracts with Customers* (Topic 606), and early adopted FASB ASU No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. Our opinion is not modified with respect to these matters.

Blue & Co., LLC

Indianapolis, Indiana
December 5, 2019

DEACONESS HEALTH SYSTEM

CONSOLIDATED BALANCE SHEETS
SEPTEMBER 30, 2019 AND 2018

ASSETS

	2019	2018
Current assets		
Cash and cash equivalents	$ 120,843,990	$ 83,464,245
Funds held by trustee	78,838	142,453
Patient accounts receivable, less allowance for uncollectible accounts of $21,870,000 in 2018	144,900,804	129,340,688
Inventories	8,308,038	9,928,164
Prepaid expenses and other current assets	31,008,446	47,046,775
Total current assets	305,140,116	269,922,325
Investments limited as to use		
Board designated funds	754,960,087	720,424,584
Board designated funds - Foundation	9,503,392	9,433,945
Donor restricted - Foundation	6,222,378	6,278,484
Total investments limited as to use	770,685,857	736,137,013
Property and equipment		
Land and improvements	32,211,601	28,390,617
Buildings and improvements	738,250,134	749,179,275
Furniture, fixtures and equipment	335,987,151	313,194,028
	1,106,448,886	1,090,763,920
Less allowances for depreciation	618,944,866	599,264,124
	487,504,020	491,499,796
Construction in progress	43,225,798	40,005,359
Total property and equipment, net	530,729,818	531,505,155
Other assets		
Investments in joint ventures	59,679,456	53,725,447
Goodwill and other intangibles	48,536,788	48,503,732
Other	35,844,422	21,496,930
Total other assets	144,060,666	123,726,109
Total assets	$ 1,750,616,457	$ 1,661,290,602

See accompanying notes to consolidated financial statements.

DEACONESS HEALTH SYSTEM

CONSOLIDATED BALANCE SHEETS
SEPTEMBER 30, 2019 AND 2018

LIABILITIES AND NET ASSETS

	2019	2018
Current liabilities		
Accounts payable and other accrued liabilities	$ 58,683,612	$ 61,388,318
Salaries, wages and related liabilities	67,274,653	64,635,661
Estimated third-party payor settlements	1,203,209	5,010,474
Accrued interest	1,009,455	1,037,438
Other current liabilities	81,715	97,915
Current portion of long-term debt	8,515,092	7,610,318
Total current liabilities	136,767,736	139,780,124
Long-term liabilities		
Long-term debt, less current portion	339,994,121	349,261,539
Other long-term liabilities	109,134,507	63,747,498
Total long-term liabilities	449,128,628	413,009,037
Total liabilities	585,896,364	552,789,161
Net assets		
Without donor restrictions		
Undesignated	386,712,277	367,376,675
Designated - capital improvements	754,960,087	720,424,584
Designated - held by trustee	78,838	142,453
Designated - Foundation	9,503,392	9,433,945
Non-controlling interest	7,243,121	4,845,300
Total without donor restrictions	1,158,497,715	1,102,222,957
With donor restrictions	6,222,378	6,278,484
Total net assets	1,164,720,093	1,108,501,441
Total liabilities and net assets	$ 1,750,616,457	$ 1,661,290,602

See accompanying notes to consolidated financial statements.

DEACONESS HEALTH SYSTEM

CONSOLIDATED STATEMENTS OF OPERATIONS
YEARS ENDED SEPTEMBER 30, 2019 AND 2018

	2019	2018
Revenue and other support		
Patient service revenue, net of contractual		
allowances and discounts		$ 1,009,993,525
Less provision for bad debts		11,701,814
Net patient service revenue	$ 1,104,452,592	998,291,711
Other revenue	55,818,667	60,133,947
Total revenue and other support	1,160,271,259	1,058,425,658
Expenses		
Salaries and wages	436,660,908	391,949,373
Employee benefits	108,730,381	100,947,806
Supplies	220,788,973	193,277,788
Contract services	109,079,630	100,060,064
Repairs and maintenance	34,437,457	31,173,225
Depreciation	57,056,895	51,674,057
Interest	12,124,836	10,068,248
Utilities	13,675,686	14,982,915
Other	78,704,651	71,292,784
Total expenses	1,071,259,417	965,426,260
Income from operations	89,011,842	92,999,398
Nonoperating revenues (expenses)		
Investment return	20,776,491	42,177,056
Net unrealized gain on investments	4,622,122	-0-
Reclassification of net unrealized holding loss	(4,645,143)	-0-
Contributions, gifts, and bequests	952,330	1,026,051
Grants	(1,956,023)	(4,225,103)
Total nonoperating revenues (expenses)	19,749,777	38,978,004
Excess revenues over expenses	108,761,619	131,977,402
Other changes in net assets without donor restrictions		
Net unrealized gain on investments	-0-	32,128,302
Reclassification of net unrealized holding loss	4,645,143	-0-
Benefit related changes other than net		
periodic benefit cost	(46,775,864)	27,360,575
Net assets released from restriction	718,236	3,310,235
Acquisition of non-controlling interest	-0-	(7,808,941)
Distributions to non-controlling interest	(11,074,376)	(13,861,416)
Change in net assets without donor restrictions	56,274,758	173,106,157
Net assets with donor restrictions		
Contributions, gifts and bequests	668,862	644,748
Change in beneficial interest in trusts	(36,449)	46,834
Investment return	45,850	77,963
Net unrealized gain (loss) on investments	(16,133)	21,707
Net assets released from restriction	(718,236)	(3,310,235)
Change in net assets with donor restrictions	(56,106)	(2,518,983)
Change in net assets	$ 56,218,652	$ 170,587,174

See accompanying notes to consolidated financial statements.

DEACONESS HEALTH SYSTEM

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
YEARS ENDED SEPTEMBER 30, 2019 AND 2018

	Without Donor Restrictions			
	Undesignated & Designated	Non-controlling Interest	With Donor Restrictions	Total
Net assets				
September 30, 2017	$ 915,848,997	$ 13,267,803	$ 8,797,467	$ 937,914,267
Excess revenues over expenses	118,729,548	13,247,854	-0-	131,977,402
Net unrealized gain on investments	32,128,302	-0-	21,707	32,150,009
Benefit related changes other than net periodic benefit cost	27,360,575	-0-	-0-	27,360,575
Net assets released from restriction	3,310,235	-0-	(3,310,235)	-0-
Investment return	-0-	-0-	77,963	77,963
Contributions, gifts, bequests and other changes	-0-	-0-	691,582	691,582
Acquisition of non-controlling interest	-0-	(7,808,941)	-0-	(7,808,941)
Distributions to non-controlling interest	-0-	(13,861,416)	-0-	(13,861,416)
Change in net assets	181,528,660	(8,422,503)	(2,518,983)	170,587,174
September 30, 2018	1,097,377,657	4,845,300	6,278,484	1,108,501,441
Excess revenues over expenses	95,289,422	13,472,197	-0-	108,761,619
Benefit related changes other than net periodic benefit cost	(46,775,864)	-0-	-0-	(46,775,864)
Net assets released from restriction	718,236	-0-	(718,236)	-0-
Investment return	-0-	-0-	45,850	45,850
Net unrealized loss on investments	-0-	-0-	(16,133)	(16,133)
Reclassification of net unrealized holding loss	4,645,143	-0-	-0-	4,645,143
Contributions, gifts, bequests and other changes	-0-	-0-	632,413	632,413
Distributions to non-controlling interest	-0-	(11,074,376)	-0-	(11,074,376)
Change in net assets	53,876,937	2,397,821	(56,106)	56,218,652
September 30, 2019	$ 1,151,254,594	$ 7,243,121	$ 6,222,378	$ 1,164,720,093

See accompanying notes to consolidated financial statements.

DEACONESS HEALTH SYSTEM

CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED SEPTEMBER 30, 2019 AND 2018

	2019	2018
Operating activities		
Change in net assets	$ 56,218,652	$ 170,587,174
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation	57,056,895	51,674,057
Provision for bad debts	-0-	11,701,814
Net unrealized gain on investments	(4,605,989)	(32,150,009)
Net realized gain on investments	(6,138,847)	(11,470,238)
Unrealized (gain) loss on interest rate swap	774,592	(590,529)
Loss on disposal of property and equipment	-0-	1,325,446
Amortization of debt issue costs and original issue discount/premium	(407,576)	(403,282)
Restricted contributions, gifts and bequests	(668,862)	(644,748)
Distributions to non-controlling interest	11,074,376	13,861,416
Changes in operating assets and liabilities		
Patient accounts receivable	(15,560,116)	(14,840,046)
Inventories	1,620,126	(55,451)
Prepaid expenses and other current assets	16,038,329	(7,663,590)
Investments in joint ventures and other assets	(20,334,557)	(16,940,687)
Accounts payable and other accrued liabilities	(3,511,706)	(7,051,077)
Salaries, wages and related liabilities	2,638,992	13,922,338
Estimated third-party payor settlements	(3,807,265)	12,463
Accrued interest	(27,983)	41,208
Other current liabilities	(16,200)	(383,023)
Other long-term liabilities	44,612,417	(26,511,858)
Net cash flows from operating activities	134,955,278	144,421,378
Investing activities		
Purchases of property and equipment	(55,474,558)	(124,135,576)
Proceeds from disposal of property and equipment	-0-	10,585
Net transfers (to) from trustee assets for principal, interest and construction draws	63,615	77,633,488
Purchases of board designated funds	(402,977,202)	(387,658,326)
Proceeds from sale of board designated funds	379,173,194	347,373,826
Purchase of investment in joint ventures	-0-	(2,303,307)
Purchase of assets	-0-	(30,030,388)
Net cash flows from investing activities	(79,214,951)	(119,109,698)
Financing activities		
Distributions to non-controlling interest	(11,074,376)	(13,861,416)
Restricted contributions, gifts and bequests	668,862	644,748
Payments on long-term debt	(7,955,068)	(7,384,776)
Net cash flows from financing activities	(18,360,582)	(20,601,444)
Change in cash and cash equivalents	37,379,745	4,710,236
Cash and cash equivalents		
Beginning of year	83,464,245	78,754,009
End of year	$ 120,843,990	$ 83,464,245

See accompanying notes to consolidated financial statements.

1. ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Deaconess Health System (the System) is an integrated multi-facility health system providing comprehensive health care services to southern Indiana, southeastern Illinois and western Kentucky, employing over 6,700 within the Tri-State area.

Deaconess Health System, Inc. was formed to coordinate management and strategic planning and provide operational facilities for entities within the System, the most significant of which are Deaconess Hospital, Inc. (the Hospital) and Deaconess Clinic, Inc. (the Clinic), not-for-profit corporations whose missions are to provide quality health care services with a compassionate and caring spirit to persons, families and communities of the Tri-State area.

The board of Deaconess Health System, Inc. is granted the authority to provide overall direction and control of the entities through their respective bylaws. Deaconess Health System, Inc. wholly owns the Clinic, Deaconess Care Integration, LLC, DCI Commercial ACO, LLC, OneCare, LLC, Deaconess Regional Healthcare Services Illinois, Inc., Deaconess VNA Plus, LLC, Deaconess Specialty Physicians, Inc., and Deaconess Health Kentucky, Inc. and is the sole corporate member of the Hospital.

The Clinic is comprised of Deaconess employed physicians practicing primary care and multi-specialty medicine within outpatient physician offices located throughout southern Indiana, southeastern Illinois and western Kentucky and two urgent care centers located in Evansville, Indiana. The facilities provide illness and injury care, preventative care, lab and x-ray services. The Clinic also encompasses the Deaconess Clinical Research Institute which provides drug research studies for the pharmaceutical industry.

Deaconess Care Integration, LLC is as an accountable care organization with the purpose of developing a care delivery model focused on quality metrics and reductions in cost for the Medicare population. DCI Commercial ACO, LLC is a counterpart to Deaconess Care Integration, LLC, but with a focus on the commercial populations. Its purpose is to assist commercial clients with value based coverage programs. OneCare, LLC was formed to develop a network of participating health care providers and pursue contracts, in concert with the aforementioned accountable care organizations, with provider-owned health plans, commercial payors, employers, providers, suppliers and other third parties to provide high quality, cost-effective and coordinated health care services to their enrollees.

Deaconess Regional Healthcare Services Illinois, Inc. manages activities such as pain management and other ancillary services in Illinois.

Deaconess VNA Plus, LLC provides home health and hospice care services.

Deaconess Specialty Physicians, Inc. (DSP) provides cardiology services to communities in the Tri-State area.

Deaconess Health Kentucky, Inc. (DHK) houses the operations of the System in Kentucky.

The System, located in Evansville, Indiana, is comprised of two general acute care facilities, a mental health facility and more than 40 ambulatory sites. The inpatient services have a combined capacity of 555 intensive care, pediatric, medical/surgical, orthopedic and neurosurgical beds.

During 2018, the System purchased the remaining non-controlling interest in The Heart Hospital at Deaconess Gateway, LLC, (the Heart Hospital), a 24 bed hospital providing preventative care, medical care, emergent care, diagnostic testing, cardiovascular procedures, cardiovascular surgery and cardiac rehabilitation on an outpatient and inpatient basis.

The System holds majority ownership interests in the following entities:

- Progressive Health of Indiana, LLC – 51%
- Tri-State Radiation Oncology, LLC – 51%
- Deaconess Health Plans, LLC – 95%
- Mainspring Managers, LLC – 51%
- Vascmed, LLC – 51%
- OrthoAlign, LLC – 51%
- Healthcare Resource Solutions, LLC – 95%

Progressive Health of Indiana, LLC provides physical, occupational and speech therapy services throughout southern Indiana.

Tri-State Radiation Oncology, LLC provides oncology and cancer services, including radiation therapy, pain management, counseling and rehabilitation.

Deaconess Health Plans, LLC is a preferred provider organization – managed care network formed to encourage collaboration in providing patient service and cost management.

Mainspring Managers, LLC provides neurology services to treat brain, spinal cord and nervous system injuries, diseases and disorders.

Vascmed, LLC provides services and manage the vascular service line of the Hospital.

OrthoAlign, LLC was created to manage the cost and quality of orthopedic procedures performed by the System.

Healthcare Resource Solutions, LLC provides revenue cycle and billing services.

Principles of Consolidation

The consolidated financial statements include the accounts of Deaconess Health System and its wholly owned and controlled subsidiaries. All material inter-company accounts and transactions have been eliminated in consolidation. Noncontrolling interest represents the portion of net assets that is owned by investors that are external to and not included in the consolidated financial statements.

Investments in Joint Ventures

Investments in organizations where the System's ownership percentage is equal to or less than 50% are included in investments in joint ventures on the consolidated balance sheets. Investments in joint ventures approximated $59,679,000 and $53,725,000 as of September 30, 2019 and 2018, respectively. The System's portion of income from unconsolidated organizations is reported with other operating revenue and was $20,812,000 and $20,432,000 for 2019 and 2018, respectively. A summary of the significant investments in joint ventures follows:

- The System holds a 50% ownership in the Deaconess Women's Hospital of Southern Indiana, LLC d/b/a The Women's Hospital which is a 74-bed facility dedicated to comprehensive women's care, including obstetrics, neonatal intensive care, cancer treatment and infertility and imaging services.
- The System holds a 50% ownership interest in Evansville Surgery Center Associates, LLC providing three locations of multispecialty outpatient surgery centers dedicated to the diagnosis and preoperative, intraoperative and postoperative care of patients.

- The System holds 33.3% of the membership shares in The Healthcare Group, LLC, a preferred provider organization – managed care network. The Healthcare Group, LLC encourages collaboration in providing patient service and cost management.
- The System holds a 27.5% ownership interest in Encompass Health/Deaconess, LLC, d/b/a Encompass Health Deaconess Rehabilitation Hospital, a comprehensive facility dedicated to improving, maintaining or restoring physical strength, cognition and mobility through therapeutic methods and technologies for rehabilitation.
- The System holds an ownership interest in the Tecumseh Health Reciprocal Risk Retention Group which was formed to provide liability insurance, reinsurance and risk management services to the members.
- The System holds an ownership interest in Crossroads Health Services which provides workers' compensation coverage.
- The System holds a 46% ownership interest in LoField Dialysis, LLC which was formed to provide dialysis and related services.
- The System, through DHK, holds a 33% ownership in Methodist Health located in Henderson and Morganfield, Kentucky.

Foundation

The System also encompasses a charitable Foundation supported by donations from the community. The Foundation, a department of the System, has a separate advisory board that carries out the mission of supporting medical, charitable and educational activities as designated by the donors.

Use of Estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, including estimated third-party payor settlements, defined benefit plan obligations 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 and could differ from actual results.

Cash and Cash Equivalents

Cash and cash equivalents are defined as investments in highly liquid debt instruments with an original maturity of three months or less, excluding amounts whose use is limited by arrangements under trust agreements, board designation or by donors. The System maintains its cash in accounts, which at times may exceed federally insured limits. The System has not experienced any losses in such accounts and believes that it is not exposed to any significant credit risk on cash and cash equivalents. Additional cash flows information for 2019 and 2018 is as follows:

	2019	2018
Supplemental cash flows information		
Cash paid for interest, net of capitalized interest	$ 12,036,000	$ 9,902,000
Property and equipment in liabilities	$ 807,000	$ 1,358,000

Capitalized interest expense, net of interest income was $-0- and approximately $6,099,000 for 2019 and 2018, respectively.

Patient Accounts Receivable

Patient accounts receivable are recorded at net realizable value based on certain assumptions determined by each payor. For third-party payors including Medicare, Medicaid, and commercial and managed care, the net realizable value is based on the estimated contractual reimbursement percentage, which is based on current contract prices or historical paid claims data by payor. For self pay accounts receivable, which includes patients who are uninsured and the patient responsibility portion for patients with insurance, the net realizable value is determined using estimates of historical collection experience without regard to aging category. These estimates are adjusted for estimated conversions of patient responsibility portions, expected recoveries and any anticipated changes in trends.

Patient accounts receivable can be impacted by the effectiveness of the System's collection efforts. Additionally, significant changes in payor mix, business office operations, economic conditions or trends in federal and state governmental healthcare coverage could affect the net realizable value of accounts receivable. The System also continually reviews the net realizable value of accounts receivable by monitoring historical cash collections as a percentage of trailing net operating revenues, as well as by analyzing current period net revenue and admissions by payor classification, aged accounts receivable by payor, days revenue outstanding, the composition of self pay receivables between pure self pay patients and the patient responsibility portion of third-party insured receivables and the impact of recent acquisitions and dispositions.

Final settlements for some payors and programs are subject to adjustment based on administrative review and audit by third parties. As a result of these final settlements, the System has recorded amounts due to third-party.

Net Patient Service Revenue

Patient service revenue is recorded at the amount that reflects the consideration to which the System expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others, and includes variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, the System bills the patients and third-party payors several days after the services are performed 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 System. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. The System 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 System receiving inpatient acute care services or patients receiving services in our outpatient centers or in their homes. The System measures the performance obligation from admission as an inpatient or the commencement of an outpatient service, to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge or completion of the outpatient services. The method of reimbursement for the System is primarily fee for service. The timing of revenue and recognition for healthcare services is transferred over time.

Because all of its performance obligations relate to contracts with a duration of less than one year, the System has elected to apply the optional exemption provided in the Financial Accounting Standards Board (the FASB) Accounting Standards Codification (ASC) 606-10-50-14a 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 previously 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 System determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with the System's policy, and implicit price concessions provided to uninsured patients. The System determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. The System determines its estimate of implicit price concessions based on its historical collection experience with this class of patients.

Charity Care, Community Benefit and Assistance to the Uninsured

The System provides care to patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain established policies of the System. Essentially, these policies define charity services as those services for which no payment or reduced payment based upon a graduated scale, is anticipated, based on the Federal Poverty Income Guidelines, published by the Department of Health and Human Services and where incurred charges are considered significant when compared to the income of the patient. Because collection of amounts determined to qualify as charity care is not pursued, such amounts are not reported as revenue.

The System's charity care policy reflects the current economic conditions and other factors unique to the System's customer base. Charity care provided during 2019 and 2018, measured at established rates, was approximately $69,592,000 and $57,119,000, respectively. In addition, other programs and services for the benefit of the community are provided. The costs of these programs are included in operating expenses. The System receives reimbursements from certain governmental payors to assist in the funding of charity care.

Of the System's total expenses reported, an estimated $23,933,000 and $19,586,000 arose from providing services to charity patients during 2019 and 2018, respectively. The estimated costs of providing patient assistance services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the System's total expenses to gross patient service revenue. The System did modify its financial assistance policy during 2019 and 2018. The System has a policy for uninsured patients with discounted rates similar to contractual payors. Uninsured self pay discounts were an estimated $31,111,000 and $24,458,000 in 2019 and 2018, respectively.

Inventories

Inventories (principally pharmaceuticals and medical supplies) are stated at the lower of cost (first in, first out) or net realizable value.

Investments Limited as to Use

These investments are recorded at fair value in the consolidated balance sheets. The 2019 investment return includes interest, dividends, realized gains and losses, and unrealized gains and losses on investments as part of excess revenues over expenses. In 2018, unrealized gains and losses on other-than-trading securities were excluded from excess revenues over expenses unless the unrealized loss on investment security was considered other-than-temporary.

Investments consist of short-term investments (principally cash equivalents), US Government and government agency obligations, marketable debt securities (corporate bonds and fixed income mutual funds), marketable equity securities (common and preferred corporate stock), equity mutual funds, private equity funds, and mortgage backed securities. Fair values for investments are based on quoted market prices. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Investments limited as to use include assets held by trustees under indenture agreements, amounts set aside by the Board of Directors for future capital improvements, retirement of debt over which the Board retains control and may at its discretion subsequently designate for other purposes and amounts designated by for the Foundation and donor restrictions. Amounts required to meet current liabilities of the System have been classified as current assets.

Private equity investments consist of limited partnerships investing in common stock of small and medium capitalization companies and mutual funds. Investments in those limited partnerships are reported at fair value as determined by the individual manager of each partnership. Although the manager uses its best judgment in estimating the fair value of the investments in the investment funds, there are inherent limitations in any estimation technique. Therefore, the values reported are not necessarily indicative of the amount that the investments funds could realize in a current transaction.

These estimated values may differ significantly from the values that would have been used had a ready market for the investments in the investment funds existed and the difference could be material. Private equity investments totaled approximately $113,887,000 and $105,978,000 (14.8% and 14.4% of investment portfolio) as of September 30, 2019 and 2018, respectively.

A decline in the market value of any other-than-trading security below cost that is deemed to be other-than-temporary results in a reduction in carrying amount to fair value. The impairment is charged to excess revenues over expenses and a new cost basis for the security is established. During 2018, the System continually reviewed the investment portfolio and evaluated whether declines in the fair value of debt securities should be considered other-than-temporary. In 2018, the System did not record other-than-temporary declines in the fair value of its investments. Effective October 1, 2018, the System reclassified its debt securities to trading securities. As a result, a reclassification of unrealized holding gain/loss of approximately $4,645,000 was made from other changes in net assets without donor restrictions to nonoperating revenues (expenses).

Investment securities are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of the System's investments could occur in the near term and that such changes could materially affect the amounts reflected in the consolidated financial statements. A critical factor in this evaluation is the length of time and extent to which the market value of the individual security has been less than cost. Other factors considered include recommendations of investment advisors and conditions specific to the issuer or industry in which the issuer operates.

Property and Equipment and Depreciation

Property and equipment are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable assets, ranging from 3 to 40 years, using the straight-line method. Equipment under capital leases are amortized on the straight-line method over the lease term or the estimated useful life of the equipment, if shorter.

Debt Issue Costs

Costs incurred in connection with the issuance of debt are amortized over the term of the related debt using the bonds outstanding method. Estimated annual amortization is approximately $125,000.

Business Combinations and Goodwill and Other Intangibles

The System accounts for a business combination using the acquisition method of accounting, and accordingly, the net assets of the acquired entity are recorded at their estimated fair values at the date of acquisition. Goodwill represents the excess of the purchase price over the fair value of net assets, including amounts assigned to identifiable intangible assets, if any. Goodwill is tested for impairment on an annual basis, or whenever an event occurs or circumstances indicate the carrying value of the goodwill may be impaired. The System performed the required annual impairment test for goodwill as of September 30, 2019 and 2018 using the income approach of calculating the present value of the future cash flows. The System determined no impairment of goodwill existed as of September 30, 2019 and 2018. As of September 30, 2019 and 2018, the System recorded goodwill and other intangibles of approximately $48,537,000 and $48,504,000, respectively, related to the acquisition of majority owned entities. Included in these totals are other intangibles, net of accumulated amortization of approximately $300,000 as of September 30, 2019 and 2018 related primarily to non-compete and similar agreements. Annual amortization is estimated at $30,000 over the remaining amortization periods.

During 2018, the System paid approximately $30,030,000 to purchase the assets of several healthcare entities including the acquisition of the non-controlling interest of the Heart Hospital. The System recorded goodwill and other intangibles of approximately $23,038,000 related to the purchases. The following is a summary of the assets purchased and liabilities assumed during 2018:

Assets		
Cash	$	688,000
Patient accounts receivable		3,767,000
Other current assets		990,000
Equipment		2,885,000
Goodwill and other assets		2,617,000
Total assets	$	10,947,000
Liabilities		
Accounts payable and other	$	3,146,000
Long-term debt		809,000
Total liabilites	$	3,955,000

Medical Malpractice

The System participates in the Indiana Medical Malpractice Act, IC 34-18 (the Act), which provides a maximum recovery of $1,650,000 for an occurrence of malpractice until June 30, 2019, and $1,800,000 thereafter. The Act requires the System to maintain medical malpractice liability insurance in the amount of at least $400,000 per occurrence ($8,000,000 in the annual aggregate) until June 30, 2019. Effective July 1, 2019, the Act requires the System to maintain medical malpractice liability insurance in the amount of at least $500,000 per occurrence ($10,000,000 in the annual aggregate). The Act also requires the System to pay a surcharge to the State Patient's Compensation Fund (the Fund). The Fund is used to pay medical malpractice claims in excess of per occurrence and the annual aggregate amounts as noted above, under certain terms and conditions. The Fund is on a claims-made basis and as long as this coverage is continuous or replaced with equivalent insurance, claims based on occurrences during its term but reported subsequently will be insured.

The System is a member of a Vermont insurance company, Tecumseh Health Reciprocal Risk Retention Group (THRRRG), as a means to comply with the System's required portion of the insurance coverage pursuant to the Act, as well as its general liability insurance and excess coverage. Membership in THRRRG includes 14 hospitals as of September 30, 2019. Coverage through THRRRG provides protection from liability in an amount not to exceed $250,000 per incident and aggregate liability protection not to exceed $7,500,000 per year. In addition, the System maintains a commercial umbrella/excess liability policy with a limit of $15,000,000 each occurrence, $15,000,000 aggregate per member and $30,000,000 total policy aggregate.

Other Long-Term Liabilities

Other long-term liabilities include obligations related to the unfunded status of defined benefit plans, other employee benefit programs and derivative liabilities related to an interest rate swap.

Performance Indicator

The consolidated statements of operations includes a performance indicator, excess revenues over expenses. Transactions deemed by management to be ongoing, major, or central to the provision of healthcare services are reported as revenue, support, and expenses. Transactions incidental to the provision of patient care services are reported as nonoperating revenues (expenses). Changes in net assets without donor restrictions, which are excluded from the performance indicator, consistent with industry practice for 2019, include pension related changes other than net periodic pension cost and contributions of long-lived assets (including assets acquired using contributions, which, by donor restriction, were to be used for the purposes of acquiring such assets). Additionally in 2018, unrealized gains and losses on all other than trading securities were excluded from the performance indicator.

Income Taxes

Deaconess Health System, Inc., the Hospital, the Clinic, DSP and DHK are not-for-profit corporations as described in Section 501(c)(3) of the Internal Revenue Code and are generally exempt from income taxes. However, they are required to file Federal Form 990 – Return of Organization Exempt from Income Tax, which is an informational return only.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the System and recognize a tax liability if the System has taken an uncertain position that more likely than not would not be sustained upon examination by various Federal and state taxing authorities. Management has analyzed the tax positions taken by the System and has concluded that as of September 30, 2019 and 2018, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying consolidated financial statements. The System is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

The remaining consolidated subsidiaries are organized as limited liability companies, whereby net taxable income is taxed directly to the members of the limited liability companies. Thus, the consolidated financial statements do not include any provision for Federal or state income taxes related to these entities.

These entities have filed their Federal and state income tax returns for periods through their most recent fiscal year ends (primarily December 31, 2018). These income tax returns are generally open to examination by the relevant taxing authorities for a period of three years from the later of the date the return was filed or its due date (including approved extensions).

Contribution Revenues and In-Kind Donations

Unconditional promises to give cash and other assets to the System are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as support with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets are released from restriction. Donor-restricted contributions whose restrictions are met within the same year as received are included in nonoperating revenues (expenses) in the accompanying consolidated financial statements. In-kind donations are recorded as revenue and expense in the accompanying consolidated financial statements. These donations consist mainly of medical supplies and services which are recorded at their estimated fair values.

Net Assets

Net assets without donor restrictions are comprised of net assets that are undesignated, board designated and held by non-controlling interest. The following net assets without donor restrictions were board designated as of September 30, 2019 and 2018:

	2019	2018
Board designated		
Capital improvements	$ 754,960,087	$ 720,424,584
Held by trustee for debt service	78,838	142,453
Foundation	9,503,392	9,433,945
	$ 764,542,317	$ 730,000,982

Net assets with donor restrictions include those assets whose use by the System has been limited primarily for capital projects or a specified time period or purpose. Also included are net assets contributed with donor restrictions requiring they be held in perpetuity with income used to support the System's activities. The following is a summary of net assets with donor restrictions as of September 30, 2019 and 2018:

	2019	2018
Patient medical care	$ 1,342,205	$ 1,282,212
Education and scholarship	775,666	739,776
Capital projects	810,089	749,791
Beneficial interest in trusts	1,173,972	1,210,421
To be held in perpetuity	692,080	692,080
Other System support	1,428,366	1,604,204
	$ 6,222,378	$ 6,278,484

Net assets were released from restriction during 2019 and 2018 for the following purposes:

	2019	2018
Patient medical care	$ 210,451	$ 969,936
Education and scholarship	121,420	559,608
Capital projects	123,064	567,183
Other System support	263,301	1,213,508
	$ 718,236	$ 3,310,235

Advertising Costs

Advertising costs are expensed as incurred. Total expense for 2019 and 2018 was approximately $1,238,000 and $1,638,000, respectively.

Reclassification

Certain 2018 amounts in the consolidated financial statements have been reclassified to conform to the 2019 presentation. The reclassifications have no effect on previously reported net assets or change in net assets.

Going Concern Evaluation

The System evaluates whether there are conditions or events that raise substantial doubt about the System's ability to continue as a going concern for a period of one year from the date the consolidated financial statements are issued.

Subsequent Events

The System evaluates events or transactions occurring subsequent to the consolidated balance sheet date for recognition and disclosure in the accompanying consolidated financial statements through the date the consolidated financial statements are issued which is December 5, 2019.

2. CHANGE IN ACCOUNTING PRINCIPLES

ASU 2016-14 - Effective October 1, 2018, the System adopted the Financial Accounting Standards Board's (the FASB) Accounting Standards Update (ASU) No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities* (ASU 2016-14). ASU 2016-14 simplifies and improves how a not-for-profit organization classifies its net assets, as well as information it presents in the financial statements and notes about its liquidity, financial performance and cash flows. The System has adjusted the presentation of its 2019 consolidated financial statements herein and retrospectively adjusted the presentation of its 2018 consolidated financial statements. In addition to changes in terminology used to describe categories of net assets throughout the consolidated financial statements, new disclosures were added regarding liquidity and the availability of resources (Note 11) and disclosures related to the functional allocation of expenses were expanded (Note 12). The impact of the adoption of ASU No. 2016-14 on the Systems' net assets is as follows:

Consolidated balance sheet	Previously Reported 9/30/2018	Adjustment	Currently Reported 9/30/2018
Net assets			
Unrestricted	$ 1,102,222,957	$ (1,102,222,957)	$ -0-
Temporarily restricted	4,375,983	(4,375,983)	-0-
Permanently restricted	1,902,501	(1,902,501)	-0-
Without donor restrictions	-0-	1,102,222,957	1,102,222,957
With donor restrictions	-0-	6,278,484	6,278,484
Total net assets	$ 1,108,501,441	$ -0-	$ 1,108,501,441
Consolidated statements of operations			
Change in net assets			
Unrestricted	$ 173,106,157	$ (173,106,157)	$ -0-
Temporarily restricted	(2,565,817)	2,565,817	-0-
Permanently restricted	46,834	(46,834)	-0-
Without donor restrictions	-0-	173,106,157	173,106,157
With donor restrictions	-0-	(2,518,983)	(2,518,983)
	$ 170,587,174	$ -0-	$ 170,587,174

There was no significant impact to the consolidated statement of cash flows as a result of adopting this ASU.

ASU 2014-09 and Topic 606 - On October 1, 2018, the System adopted the new revenue recognition accounting standard issued by the FASB and codified in the FASB ASC as topic 606 (ASC 606). The revenue recognition standard in ASC 606 outlines a single comprehensive model for recognizing revenue as performance obligations, defined in a contract with a customer as goods or services transferred to the customer in exchange for consideration, are satisfied. The standard also requires expanded disclosures (Note 5) regarding the System's revenue recognition policies and significant judgments employed in the determination of revenue.

The System applied the modified retrospective approach to all contracts when adopting ASC 606. As a result, upon the System's adoption of ASC 606 the majority of what was previously classified as the provision for bad debts in the consolidated statements of operations is now reflected as implicit price concessions (as defined by ASC 606) and therefore, included as a reduction to net patient service revenue in 2019. For changes in credit issues not assessed at the date of service, the System prospectively recognizes those amounts in operating expenses on the consolidated statements of operations, if any. For periods prior to the adoption of ASC 606, the provision for bad debts was presented consistent with the previous revenue recognition standards that required such provision to be presented separately as a component of net patient service revenue.

Additionally, upon adoption of ASC 606, the allowance for uncollectible accounts of approximately $21,870,000 as of October 1, 2018 was reclassified as a component of net patient accounts receivable. Other than these changes, the adoption of ASC 606 did not have a material impact on the 2019 consolidated financial statements, and the System does not expect it to have a material impact on its results of operations on a prospective basis. As part of the adoption of ASC 606, the System elected two of the available practical expedients provided for in the standard. First, the System does not adjust the transaction price for any financing components as those were deemed insignificant. Additionally, the System expenses all incremental customer contract acquisition costs as incurred, because such costs are not material and would be amortized over a period less than one year.

Net Patient Service Revenues under ASC 606:

Upon adoption of ASC 606, net patient service revenues are recorded at the transaction price estimated by the System to reflect the total consideration due from patients and third-party payors in exchange for providing goods and services in patient care. These services are considered to be a single performance obligation and have a duration of less than one year. Revenues are recorded as these goods and services are provided. The transaction price, which involves significant estimates, is determined based on the System's standard charges for the goods and services provided, with a reduction recorded for price concessions related to third-party contractual arrangements as well as patient discounts and other patient price concessions. During the year ended September 30, 2019, the impact of changes to the inputs used to determine the transaction prices was considered immaterial to the current period.

<u>ASU 2016-01</u> - On October 1, 2018, the System early adopted FASB ASU No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* (ASU 2016-01) which affects all entities that hold financial assets or owe financial liabilities. The guidance in ASU 2016-01 supersedes the guidance to classify equity securities with readily determinable fair values into different categories (that is, trading or available-for-sale) and requires equity securities (including other ownership interests, such as partnerships, unincorporated joint ventures, and limited liability companies) to be measured at fair value with changes in the fair value recognized through the excess revenues over expenses. An entity's equity investments that are accounted for under the equity method of accounting or result in consolidation of an investee are not included within the scope of this guidance. The amendments allow equity investments that do not have readily determinable fair values to be remeasured at fair value either upon the occurrence of an observable price change or upon identification of an impairment. The amendments also require enhanced disclosures about those investments. This ASU does not have a material effect on the System's consolidated financial position, results of operations, or disclosures in the notes to the consolidated financial statements. The primary impact on the System is that changes in the fair value of equity investments will be recognized within the performance indicator, excess revenues over expenses, rather than below the performance indicator where it was previously presented.

3. INVESTMENTS

Investments at fair value consisted of the following as of September 30:

	2019	2018
Board designated funds		
Cash	$ 5,092,110	$ 8,699,128
Common stocks	179,817,965	176,444,248
Mutual funds	239,499,793	231,782,242
US Government and government agency obligations	39,986,238	48,441,062
Corporate bonds	110,795,812	100,291,208
Mortgage backed securities	65,880,701	48,788,248
Private equity	113,887,468	105,978,448
	754,960,087	720,424,584
Funds held by trustee		
Money market mutual funds	78,838	142,453
Less current portion	(78,838)	(142,453)
	-0-	-0-
Board designated - Foundation and donor restricted - Foundation		
Cash	63,564	92,397
Common stocks	1,158,897	1,243,419
Mutual funds	11,640,232	12,175,414
US Government and government agency obligations	67,435	74,940
Accrued interest and other	2,795,642	2,126,259
	15,725,770	15,712,429
Investments limited as to use, net	$ 770,685,857	$ 736,137,013

Investments reported as current assets are those that the System has made available for use in operations within the next twelve months. Investments limited as to use that are required for obligations classified as current liabilities are also reported in current assets. A detail of investment return for both net assets with and without donor restrictions for 2019 and 2018 is as follows:

	2019	2018
Interest and dividends and other	$ 15,458,086	$ 30,194,252
Net realized gain	6,138,847	11,470,238
Unrealized gain (loss) on interest rate swap	(774,592)	590,529
Investment return, net	$ 20,822,341	$ 42,255,019

The unrealized gain on investments in 2019 for net assets without donor restrictions was approximately $4,622,000 and is reported under nonoperating revenues (expenses) in the consolidated statement of operations. The unrealized loss on investments for net assets with donor restrictions was $16,000 in 2019 and is included in changes in net assets with donor restrictions on the consolidated statement of operations.

The unrealized gain on investments for 2018 was approximately $32,150,000 for both net assets with and without restrictions. The amounts were reported in either other changes in net assets without donor restrictions or changes in net assets with donor restrictions in 2018 prior to the adoption of FASB ASU No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*.

Effective October 1, 2018, the System reclassified its debt securities to trading securities. As a result, a reclassification of net unrealized holding loss of approximately $4,645,000 was made from other changes in net assets without donor restrictions to nonoperating revenues (expenses).

See Note "Derivative Financial Instruments – Interest Rate Swaps" for additional information on unrealized gain or loss on interest rate swap.

4. FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1) and the lowest priority to unobservable inputs (level 3). The three levels of the fair value hierarchy are described as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the System has the ability to access.
- Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.
- Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used as of September 30, 2019 and 2018:

- *Common stocks*: Valued based on the closing price reported on the active market on which the individual securities are traded.
- *Mutual funds*: Valued based on quoted net asset value (NAV) of the shares held by the System at year-end. The NAV is based on the value of the underlying assets owned by the fund, minus its liabilities and then divided by the number of shares outstanding. The NAV is quoted in an active market.
- *Money market mutual funds*: Valued based at the subscription and redemption activity at a $1 stable NAV. However, on a daily basis the funds are valued at their daily NAV calculated using the amortized cost of securities.
- *US Government and government agency obligations*: Valued based on the closing price reported on the active market on which the securities are traded.
- *Corporate bonds and mortgage backed securities*: Valued using pricing models maximizing the use of observable inputs for similar securities.

- *Private equity investments*: Valued at the NAV of units of the fund. The NAV, as provided by the investment manager, is used as a practical expedient to estimate fair value. The private equity investments consist of investments in a variety of domestic and foreign equity and debt securities, managed accounts and other investment vehicles that employ diversified styles and strategies. The NAV is based on the fair value of the underlying investments held by the fund less its liabilities. Due to the nature of the investments held by the fund, changes in market conditions and the economic environment may significantly impact the NAV of the fund and, consequently, the fair value of the System's interests in the funds. Although a secondary market exists for these investments, it is not active and individual transactions are typically not observable. When transactions do occur in this limited secondary market, they may occur at discounts to the reported NAV. It is therefore reasonably possible that if the System were to sell these investments in the secondary market, a buyer may require a discount to the reported NAV, and the discount could be significant.
- *Derivative (Interest rate swap agreement)*: Valued using pricing models that are derived principally from observable market data based on discounted cash flows and interest rate yield curves at quoted intervals for the full term of the swap. See the Note disclosure "Derivatives Financial Instruments – Interest Rate Swaps" for additional information related to derivatives.

Assets and liabilities measured at fair value on a recurring basis as of September 30, 2019 and 2018 are as follows:

	September 30, 2019			
	Total	Level 1	Level 2	Level 3
Assets				
Investments limited as to use				
Money market mutual funds	$ 78,838	$ -0-	$ 78,838	$ -0-
Common stocks				
Consumer	36,578,130	36,578,130	-0-	-0-
Financial services	22,692,716	22,692,716	-0-	-0-
Industrial and materials	27,563,555	27,563,555	-0-	-0-
Technology	34,017,302	34,017,302	-0-	-0-
Healthcare	19,743,869	19,743,869	-0-	-0-
Other	40,381,290	40,381,290	-0-	-0-
Total common stocks	180,976,862	180,976,862	-0-	-0-
Mutual funds				
Large growth	31,055,758	31,055,758	-0-	-0-
Large value	29,604,968	29,604,968	-0-	-0-
Large blend	190,361,326	190,361,326	-0-	-0-
Other	117,973	117,973	-0-	-0-
Total mutual funds	251,140,025	251,140,025	-0-	-0-
US Government and government agency obligations	40,053,673	40,053,673	-0-	-0-
Corporate bonds				
Consumer	28,559,153	-0-	28,559,153	-0-
Financial services	31,697,760	-0-	31,697,760	-0-
Industrial and materials	34,305,876	-0-	34,305,876	-0-
International	6,883,211	-0-	6,883,211	-0-
Other	9,349,812	-0-	9,349,812	-0-
Total corporate bonds	110,795,812	-0-	110,795,812	-0-
Mortgage backed securities	65,880,701	-0-	65,880,701	-0-
	648,925,911	$ 472,170,560	$ 176,755,351	$ -0-
Cash	5,155,674			
Private equity (a)	113,887,468			
Accrued interest and other	2,795,642			
	$ 770,764,695			
Liabilities				
Derivative	$ 691,550	$ -0-	$ 691,550	$ -0-

	September 30, 2018			
	Total	Level 1	Level 2	Level 3
Assets				
Investments limited as to use				
Money market mutual funds	$ 142,453	$ -0-	$ 142,453	$ -0-
Common stocks				
Consumer	34,304,987	34,304,987	-0-	-0-
Financial services	24,324,758	24,324,758	-0-	-0-
Industrial and materials	31,825,144	31,825,144	-0-	-0-
Technology	33,835,806	33,835,806	-0-	-0-
Healthcare	16,994,820	16,994,820	-0-	-0-
Other	36,402,152	36,402,152	-0-	-0-
Total common stocks	177,687,667	177,687,667	-0-	-0-
Mutual funds				
Large growth	30,819,451	30,819,451	-0-	-0-
Large value	31,304,359	31,304,359	-0-	-0-
Large blend	181,715,431	181,715,431	-0-	-0-
Other	118,415	118,415	-0-	-0-
Total mutual funds	243,957,656	243,957,656	-0-	-0-
US Government and government agency obligations	48,516,002	48,516,002	-0-	-0-
Corporate bonds				
Consumer	21,896,900	-0-	21,896,900	-0-
Financial services	28,713,361	-0-	28,713,361	-0-
Industrial and materials	31,579,744	-0-	31,579,744	-0-
International	6,796,691	-0-	6,796,691	-0-
Other	11,304,512	-0-	11,304,512	-0-
Total corporate bonds	100,291,208	-0-	100,291,208	-0-
Mortgage backed securities	48,788,248	-0-	48,788,248	-0-
	619,383,234	$ 470,161,325	$ 149,221,909	$ -0-
Cash	8,791,525			
Private equity (a)	105,978,448			
Accrued interest and other	2,126,259			
	$ 736,279,466			
Derivative	$ 83,042	$ -0-	$ 83,042	$ -0-

(a) In accordance with Subtopic 820-10, certain investments that were measured at NAV per share or its equivalent have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the line items presented at fair value in the consolidated balance sheets.

The following tables summarize the private equity investments measured at fair value based on NAV per share as of September 30, 2019 and 2018:

	Fair Value		Unfunded	Redemption	Redemption
Investment	2019	2018	Commitments	Frequency	Notice Period
Private equity	$ 39,786,047	$ 40,935,596	None	Monthly	45 days
Private equity	74,101,421	65,042,852	None	Daily	Daily
	$ 113,887,468	$ 105,978,448			

The System's policy is to recognize transfers between levels as of the end of the reporting period. There were no transfers during 2019 and 2018.

Realized gain and loss are reported in the consolidated statements of operations as a component of investment return. Net realized gains of approximately $6,139,000 and $11,470,000 were recorded during 2019 and 2018, respectively. Differences between market value and cost of investments are classified as unrealized gains or losses. The unrealized gain or loss is included in earnings for the period attributable to the change in unrealized gain or loss relating to assets held as of September 30, 2019 and 2018 and is reported in the consolidated statements of operations as net unrealized gain or loss on investments. During 2019, the System recognized an unrealized gain of $4,606,000 which was included in both nonoperating revenues (expenses) and changes in net assets with donor restrictions. During 2018, the System recognized an unrealized gain of $32,150,000 which was included in both other changes in net assets without and with donor restrictions prior to the implementation of ASU 2016-01 in 2019.

The System holds investments which are exposed to various risks such as interest rate, market, and credit. Due to the level of risk associated with these securities and the level of uncertainty related to changes in the value, it is at least reasonably possible that changes in the various risk factors will occur in the near term that could materially affect the amounts reported in the accompanying consolidated financial statements.

5. NET PATIENT SERVICE REVENUE, RELATED RECEIVABLES AND ESTIMATED SETTLEMENTS

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Recently, government activity has increased with respect to investigation and/or allegations concerning possible violations of fraud and abuse statutes and/or regulations by health care providers. Laws and regulations concerning government programs, including Medicare and Medicaid, are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Final determination of compliance with such laws and regulations is subject to future government review and interpretation. Violations may result in significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. The System believes that it is in compliance with all applicable laws and regulations.

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 System'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. Adjustments arising from a change in the transaction price increased net patient service revenue by approximately $163,000 and $1,261,000 in 2019 and 2018, respectively. As of September 30, 2019, Medicare and Medicaid reports have been audited and final settled with the fiscal intermediary through September 30, 2015.

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. The System also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. The System estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to net patient service revenue in the period of the change. For 2019 and 2018, adjustments were recognized due to changes in the System’s estimates of implicit price concessions, discounts, and contractual adjustments for performance obligations satisfied in prior years were not significant. Subsequent changes that are significant and determined to be the result of an adverse change in the patient's ability to pay, determined on a portfolio basis, are recorded as bad debt expense.

Consistent with the System's mission, care is provided to patients regardless of their ability to pay. Therefore, the System has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts the System expects to collect based on its collection history with those patients.

Patients who meet the System'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.

The System has determined that the nature, amount, timing, and uncertainty of revenue and cash flows are affected by the following factors: payors, geography, service lines, method of reimbursement, and timing of when revenue is recognized. The following tables provide details of these factors.

The composition of net patient service revenue by payor and by service line for 2019 and 2018 is as follows:

	2019	2018
Payor type		
Medicare	$ 397,602,933	$ 350,400,390
Medicaid	119,280,880	107,815,505
Commercial and managed care	584,255,421	537,080,941
Self pay and other	3,313,358	2,994,875
	$ 1,104,452,592	$ 998,291,711
Service line		
Hospital - inpatient	$ 426,318,701	$ 341,415,765
Hospital - outpatient	446,198,847	373,361,100
Physician services	231,935,044	283,514,846
	$ 1,104,452,592	$ 998,291,711

A summary of net patient service revenue, including information on service lines, for 2019 and 2018 follows:

	2019	2018
Patient service revenue	$ 3,114,993,478	$ 2,815,577,773
Adjustments		
Charity care	69,591,682	57,119,440
Uninsured self pay discounts	31,111,273	24,458,111
Contractual adjustments	1,886,399,446	1,724,006,697
Total adjustments	1,987,102,401	1,805,584,248
Net patient service revenue	1,127,891,077	1,009,993,525
Less implied price concessions	23,438,485	-0-
Less provision for bad debts	-0-	11,701,814
Net patient service revenue net of provision for bad debts	$ 1,104,452,592	$ 998,291,711

The following is mix of patient accounts receivable and patient service revenue as of September 30, 2019 and 2018 and for the years then ended:

	Receivable		Revenue	
	2019	2018	2019	2018
Medicare	32%	26%	36%	35%
Medicaid	5%	6%	11%	11%
Commercial and managed care	58%	63%	52%	53%
Self pay and other	5%	5%	1%	1%
	100%	100%	100%	100%

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

Medicare

Inpatient acute care services, outpatient services and physician services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic and other factors. Certain outpatient services and defined medical education costs related to Medicare beneficiaries are paid based on cost reimbursement methodologies. The System's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization. Inpatient non-acute care services are generally reimbursed based upon cost reimbursement methodologies.

Medicaid and Hospital Assessment Fee and Healthy Indiana Plan Programs

Medicaid services are paid at prospectively determined rates per day or per discharge for inpatients or per occasion of service for outpatients. To the extent that services to Medicare and Medicaid program beneficiaries are reimbursed based on cost reimbursement methodologies, final settlement is determined after submission of annual cost reports and audits thereof by the fiscal intermediary.

The System participates in the State of Indiana’s Hospital Assessment Fee (HAF) Program. The purpose of the HAF Program is to fund the State share of enhanced Medicaid payments and Medicaid Disproportionate Share payments for Indiana hospitals. Previously, the State share was funded by governmental entities through intergovernmental transfers. The Medicaid enhanced payments relate to both fee for service and managed care claims. The Medicaid enhanced payments are designed to follow the patients and result in increased Medicaid rates. The hospitals also started funding the Healthy Indiana Plan (HIP), the State’s Medicaid expansion program. The payments related to the HIP Program mirror the Medicaid payments under the HAF Program but the funding includes physician, state administration, and certain non-hospital expenditures. During 2019 and 2018, the System recognized HAF and HIP program expense of approximately $37,504,000 and $29,112,000, respectively, which resulted in Medicaid rate increases. HAF and HIP program expense is included in other expenses on the consolidated statements of operations while the Medicaid rate increases are recorded in net patient service revenue.

The System also entered into payment agreements with certain other commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term.

6. LONG-TERM DEBT

The following is a summary of long-term debt as of September 30, 2019 and 2018:

	2019	2018
Hospital Revenue Bonds, Series 2011A Term bonds, payable through March 2029 in amounts ranging from $770,000 to $1,630,000 with interest; fixed rates ranging from 2.50% to 6.00%	$ 12,930,000	$ 13,935,000
Hospital Revenue Bonds, Series 2012B Term bonds, payable through January 2022 in amounts ranging from $880,000 to $1,755,000 with interest; fixed rate 2.30%	4,930,000	6,350,000
Hospital Revenue Bonds, Series 2012C Term bonds, payable through January 2019 in amounts ranging from $1,100,000 to $1,625,000 with interest; fixed rate 2.28%	-0-	1,625,000
Hospital Revenue Bonds, Series 2013A Term bonds, payable through March 2035 in amounts ranging from $470,000 to $8,070,000 with interest; fixed rates ranging from 3.00% to 5.00%	64,615,000	65,085,000
Hospital Revenue Bonds, Series 2013B Term bonds, payable through March 2029 in amounts ranging from $1,000,000 to $1,735,000 with interest; variable based on 70% of BBA LIBOR rate, 1.971% as of September 30, 2019	14,810,000	16,015,000
Hospital Revenue Bonds, Series 2013C Term bonds, payable through March 2036 in amounts ranging from $250,000 to $2,840,000 with interest: variable based on 67% of BBA LIBOR rate plus 90 basis points, 2.299% as of September 30, 2019	39,180,000	39,430,000
Refunding Revenue Bonds, Series 2015A Term bonds, payable from March 2017 through March 2039 in amounts ranging from $140,000 to $20,255,000 with interest; fixed rates ranging from 3.00% to 5.00%	47,770,000	47,910,000
Series 2016 Term Loan Agreement payable from January 2019 through January 2025 in amounts ranging from $500,000 through $2,100,000 with final payment of $39,900,000 due in August 2026, fixed interest at 2.5%	52,500,000	53,000,000
Hospital Revenue Bonds, Series 2016A Serial bonds, payable through March 2039 in amounts ranging from $405,000 to $1,920,000 with interest; fixed rates ranging from 3.00% to 5.00%	18,970,000	18,970,000
Term bonds, payable on March 1, 2044 in amounts ranging from $9,760,000 to $45,000,000 with interest; fixed rates ranging from 3.125% to 5.000%	85,860,000	85,860,000
Other	469,077	1,809,145
	342,034,077	349,989,145
Current portion	(8,515,092)	(7,610,318)
Original issue premiums (discounts), net	7,790,201	8,314,252
Debt issue costs	(1,315,065)	(1,431,540)
Long-term debt, net of current portion	$ 339,994,121	$ 349,261,539

In 2013, the System, the Indiana Finance Authority (the Authority) and Fifth Third Bank entered into Bond Purchase Contracts (the Contracts) whereby Fifth Third purchased from the Authority all of the Series 2012B, 2012C and 2013B bonds in a private placement. The Series 2013C bonds were purchased from the Authority by Bank of America in a private placement.

Under the terms of the Contracts, Fifth Third and Bank of America agreed to hold the Series 2012B and 2012C bonds through the stated bond maturity dates. The Contracts for the Series 2013B and 2013C bonds are through 2023. At the end of the Contract periods for the Series 2013B and 2013C bonds, these bonds could be remarketed to the original holders or to new investors at interest rate options as provided in the bond documents. If the Series 2013B and 2013C bonds cannot be remarketed at the end of the Contract periods, the System would be subject to payment of the remaining principal.

The System entered into an interest rate swap agreement with Fifth Third on the Series 2013B bonds. See the Note disclosure "Derivatives Financial Instruments – Interest Rate Swaps" for additional information.

All of the revenue bonds are secured by a security interest in the System's revenue. The System covenants that it will not permit any lien or security interest on the System facility other than certain permitted encumbrances. In addition, the various agreements require maintenance of certain debt service income ratios, limit additional borrowings, and require compliance with various other restrictive covenants. As of September 30, 2019 and 2018, the System believed it was in compliance with the restrictive covenants.

As of September 30, 2019, the System did not have any significant commitments outstanding related to property and equipment.

Aggregate maturities of long-term debt are as follows:

Year Ending September 30,	
2020	$ 8,515,092
2021	8,948,985
2022	8,805,000
2023	9,440,000
2024	9,785,000
Thereafter	296,540,000
	$ 342,034,077

7. DERIVATIVE FINANCIAL INSTRUMENTS – INTEREST RATE SWAPS

Objectives and Strategies for Using Derivatives

The System makes limited use of derivative financial instruments for the purpose of managing interest rate risk. In particular, forward interest rate swaps (which are designated as cash flow hedges) are used to manage the risk associated with interest rates on variable-rate borrowings and to lower its overall borrowing costs.

As of September 30, 2019 and 2018, the System had outstanding an interest rate swap agreement with Fifth Third, having a notional amount of $14,810,000 and $16,015,000, respectively. The agreement effectively changes the System's interest rate exposure on its Series 2013B bonds through March 2029 to a fixed 2.78%. The interest rate swap agreement matures at the time the related long-term debt matures. The System is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreement. However, the System does not anticipate nonperformance by the counterparties.

The derivative is not designated as a hedging instrument, and is marked-to-market on the consolidated balance sheet at fair value. The related gains and losses are included in excess revenues over expenses, the performance indicator, for the reporting period. Cash flows from interest rate swap contracts are classified as an operating activity on the consolidated statement of cash flows.

The asset derivatives are reported in the consolidated balance sheets as other assets. The liability derivatives are reported as derivative liabilities in the other long-term liabilities. As of September 30, 2019 and 2018, the fair values of derivatives recorded in the consolidated balance sheets are as follows:

	2019	2018
Other long-term liabilities		
Derivative asset (liability)	$ (691,550)	$ 83,042

During 2019 and 2018, the amount of gain or loss recognized in the consolidated statements of operations and reported as a component of investment income under nonoperating revenues (expenses) is as follows:

	2019	2018
Nonoperating revenues (expenses)		
Investment return		
Unrealized gain (loss) on derivative	$ (774,592)	$ 590,529

8. DEFINED BENEFIT PENSION PLAN

The System offers a noncontributory defined benefit pension plan covering eligible employees. Benefits are based on each participant's years of service and compensation. Contributions to the plan are based on actuarially determined amounts sufficient to meet the benefits to be paid to plan participants. The defined benefit pension plan is closed to new participants. Participants should refer to the plan documents for more complete information.

The following tables set forth the funded status of the benefit plan and amounts recognized in the consolidated financial statements as of September 30, 2019 and 2018 and for the years then ended.

	2019	2018
Change in benefit obligation		
Benefit obligation, beginning of year	$ 277,497,199	$ 299,201,948
Service cost	5,827,597	6,770,049
Interest cost	10,908,400	9,882,572
Benefits paid	(24,353,796)	(17,636,092)
Actuarial (gain) loss	41,790,607	(20,721,278)
Benefit obligation, end of year	$ 311,670,007	$ 277,497,199

	2019	2018
Changes in plan assets		
Fair value of plan assets, beginning of year	$ 221,432,645	$ 215,900,410
Actual return on plan assets	6,003,801	15,164,327
Employer contributions	8,004,000	8,004,000
Benefits paid	(24,353,796)	(17,636,092)
Fair value of plan assets, end of year	$ 211,086,650	$ 221,432,645
Funded status		
Funded status of the plan, end of year	$ (100,583,357)	$ (56,064,554)
Amounts recognized in the consolidated balance sheets consist of		
Other long-term liabilities	$ (100,583,357)	$ (56,064,554)
Amounts not yet reflected in net periodic benefit cost and included in other changes in unrestricted net assets		
Prior service (cost) credit	$ -0-	$ -0-
Accumulated gain (loss)	(109,711,490)	(62,935,626)
Other changes in unrestricted net assets	(109,711,490)	(62,935,626)
Cumulative employer contributions in excess (deficit) of net periodic benefit cost	9,128,133	6,871,072
Net amount recognized in the consolidated balance sheets	$ (100,583,357)	$ (56,064,554)

Other pension disclosures for 2019 and 2018 include:

	2019	2018
Components of net periodic benefit cost		
Service cost	$ 5,827,597	$ 6,770,049
Interest cost	10,908,400	9,882,572
Expected return on plan assets	(14,764,370)	(14,927,576)
Amortization of prior year service cost	-0-	-0-
Amortization of (gain) loss	3,775,312	6,402,546
Net periodic benefit cost	$ 5,746,939	$ 8,127,591
Other changes in unrestricted net assets		
Net (gain) loss arising during year	$ 50,551,176	$ (20,958,029)
Amortization of prior service cost	-0-	-0-
Amortization of gain (loss)	(3,775,312)	(6,402,546)
Total other changes in unrestricted net assets	$ 46,775,864	$ (27,360,575)
Estimated amounts that will be amortized from other changes in unrestricted net assets over the next fiscal year		
Amortization of prior service (cost) credit	$ -0-	$ -0-
Amortization of gain (loss)	$ (8,546,734)	$ (3,775,312)

	2019	2018
Weighted-average actuarial assumptions to determine benefit obligations of September 30		
Discount rate	3.13%	4.22%
Rate of compensation increase	3.50%	3.50%
Measurement date	9/30/19	9/30/18
Weighted-average actuarial assumptions to determine net periodic benefit cost as of September 30		
Discount rate	4.22%	3.79%
Expected long-term rate of return	6.75%	7.00%
Rate of compensation increase	3.50%	3.50%
Additional year end information		
Projected benefit obligation	$ 311,670,007	$ 277,497,199
Accumulated benefit obligation	$ 294,096,427	$ 261,326,781
Fair value of plan assets	$ 211,086,650	$ 221,432,645

The following is a schedule by year of expected benefit payments for the years after September 30, 2019:

Year Ending September 30,	
2020	$ 10,014,256
2021	10,957,669
2022	11,814,834
2023	12,637,081
2024	13,365,716
2025-2029	78,842,858
	$ 137,632,414

Determination of net periodic pension cost for the years ended September 30, 2019 and 2018 is based on assumptions and census data as of January 1, 2019 and 2018, respectively.

The principal long-term determinant of a portfolio's investment return is its asset allocation. The pension benefits plan allocation includes growth assets (60%) and fixed income (40%). In addition, active management strategies have added value relative to passive benchmark returns. The expected long-term rate of return assumption is based on the mix of assets in the plan, the long-term earnings expected to be associated with each asset class, and the additional return expected through active management. This assumption is periodically benchmarked against peer plans.

The amortization of any prior service cost is determined using a straight-line amortization of the cost over the average remaining service period of employees expected to receive benefits under the pension benefits plan.

The pension benefits plan's weighted-average, asset allocations as of September 30, 2019 and 2018, by asset category, are as follows:

	2019	2018
Equity		
Mutual funds	31%	39%
Common/collective trusts	9%	11%
Common stocks	13%	11%
Total equity	53%	61%
Fixed income		
Mutual funds	0%	10%
Bonds	26%	11%
Common/collective trusts	13%	10%
Total fixed income	39%	31%
Cash equivalents	3%	1%
Private equity	5%	7%
	100%	100%

The allocation strategy for the pension benefits plan currently comprises approximately 50% to 70% growth investments (target of 60%) and 30% to 50% fixed-income investments (target of 40%). Within the growth investment classification, the plan asset strategy encompasses equity and equity-like instruments that are expected to represent approximately 60% of the System's plan asset portfolio of both public and private market investments. The largest component of these equity and equity-like instruments is public equity securities that are well diversified and invested in U.S. and international companies.

Fair value of mutual funds and marketable equity securities are based on the quoted prices in active markets. Common/collective trusts are valued at the NAV on a private market that is not active. However, the underlying investments are traded on an active market. The fair value of the private equity funds is valued at the percentage ownership of the NAV as reported to the plan by the individual managers.

The following is an analysis of fair value of the major classes of pension benefits plan assets of September 30, 2019 and 2018:

	2019	2018
Level 1		
Mutual funds		
Intermediate bond	$ -0-	$ 23,303,890
Large blend and value	53,902,396	62,198,253
Foreign	12,407,504	23,573,003
Total mutual funds	66,309,900	109,075,146
Common stocks		
Financial services	4,368,329	5,742,758
Industrial and materials	3,662,349	8,493,611
Other	18,390,740	10,107,019
Total common stocks	26,421,418	24,343,388
Total Level 1	92,731,318	133,418,534
Level 2		
Fixed income bonds		
Domestic	52,471,874	21,571,895
High yield	653,621	683,263
Foreign	1,843,041	1,349,341
Total Level 2	54,968,536	23,604,499
Cash equivalents	7,117,858	1,630,428
Common/collective trusts - not classified	44,853,420	47,578,245
Private equity - not classified	11,415,518	15,200,939
	$ 211,086,650	$ 221,432,645

See the Note disclosure “Fair Value Measurements” for additional information.

The System expects to contribute in excess of the required funding amounts to its pension benefits plan in 2020 of approximately $8,000,000.

The System also offers a 401k plan to eligible employees where the System makes base contributions to eligible employees based on years of service in addition to matching contributions (ranging from 25% to 60% of employee deferral up to 6% of eligible earnings) based on the eligible employees’ contribution to the 401k plan. Total expense for the System’s contributions for eligible employees for 2019 and 2018 was approximately $11,448,000 and $14,731,000, respectively.

9. RELATED PARTY TRANSACTIONS

The System is a joint-owner of The Women’s Hospital. The System owns the building in which The Women’s Hospital is located and leases the space to The Women’s Hospital currently at approximately $230,000 per month with an option to increase that amount annually through 2031. The System provides ancillary services (lab, radiology) for The Women’s Hospital. Ancillary services provided were approximately $3,511,000 and $2,931,000 in 2019 and 2018, respectively.

The System is a joint owner of Evansville Surgery Center Associates, LLC (Surgery Center). The System recorded contract service expense related to the Surgery Center of approximately $31,886,000 and $28,393,000 in 2019 and 2018, respectively. As of September 30, 2019 and 2018, the System had a liability to the Surgery Center of approximately $4,217,000 and $3,797,000, respectively.

The System is a joint-owner of Encompass Health Deaconess Rehabilitation Hospital. The System provides ancillary services (lab, radiology) to Encompass Health Deaconess Rehabilitation Hospital. Ancillary services provided were approximately $815,000 and $366,000 in 2019 and 2018, respectively.

Related party transactions between the System and other joint ventures in 2019 and 2018 were not significant to the System's overall consolidated financial statements.

10. COMMITMENTS AND CONTINGENCIES

Operating leases

The System leases various equipment and facilities under operating leases expiring at various dates through 2027. Total lease expense for 2019 and 2018 was approximately $17,543,000 and $14,406,000, respectively.

The following are the minimum lease payments for the years after September 30, 2019:

Year Ending September 30,	
2020	$ 17,783,049
2021	16,910,046
2022	13,348,852
2023	12,560,461
2024	5,365,730
Thereafter	4,862,859
	$ 70,830,997

Litigation

The System is involved in litigation and regulatory matters arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the System's future financial position, results from operations or cash flows.

Health Insurance

The System's employee health care insurance is provided through a combination of insured, self-insured and purchased re-insurance coverage from a commercial carrier. The System maintains an estimated liability for the amount of claims incurred but not reported. Substantially all employees are covered for major medical benefits. The self-insured health coverage carries a stop-loss maximum of $450,000 per case with no aggregate limit.

11. LIQUIDITY AND AVAILABILITY OF RESOURCES

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the 2019 consolidated balance sheet date approximate $265,745,000 and are comprised of $120,844,000 in cash and cash equivalents and $144,901,000 of patient accounts receivable. None of the financial assets are subject to donor or other contractual restrictions that make them unavailable for general expenditure within one year of the consolidated balance sheet date. Patient accounts receivable are subject to implied time restrictions, but are expected to be collected within one year.

As a part of the System's liquidity management, it has a policy to structure financial assets to be available as its general expenditures, liabilities and other obligations come due. In addition, the System periodically invests excess cash in investments. The System has board designated investments of approximately $764,463,000 as of September 30, 2019. Although the System does not intend to spend from these board designated funds (other than amounts appropriated for general expenditure), these amounts could be made available, if necessary.

12. FUNCTIONAL EXPENSES

The System provides health care services to patients in the community and the surrounding areas. Healthcare services and other certain related expenses approximated 89.3% and 88.5% of total expenses in 2019 and 2018, respectively. General and administrative expenses approximated 10.7% and 11.5% in 2019 and 2018, respectively. Fundraising expenses were not significant in 2019 and 2018. Expenses related to providing these services for 2019 and 2018 are as follows:

	2019		
	Healthcare Services	General & Administrative	Total
Expenses			
Salaries and wages	$ 394,577,959	$ 42,082,949	$ 436,660,908
Employee benefits	92,898,278	15,832,103	108,730,381
Supplies	218,889,431	1,899,542	220,788,973
Contract services	100,424,176	8,655,454	109,079,630
Repairs and maintenance	24,578,589	9,858,868	34,437,457
Depreciation	38,846,678	18,210,217	57,056,895
Interest	7,143,312	4,981,524	12,124,836
Utilities	8,429,898	5,245,788	13,675,686
Other	70,524,590	8,180,061	78,704,651
Total expenses	$ 956,312,911	$ 114,946,506	$ 1,071,259,417

	2018		
	Healthcare Services	General & Administrative	Total
Expenses			
Salaries and wages	$ 352,739,331	$ 39,210,042	$ 391,949,373
Employee benefits	85,988,110	14,959,696	100,947,806
Supplies	191,481,590	1,796,198	193,277,788
Contract services	89,115,289	10,944,775	100,060,064
Repairs and maintenance	22,022,581	9,150,644	31,173,225
Depreciation	35,744,847	15,929,210	51,674,057
Interest	5,831,270	4,236,978	10,068,248
Utilities	9,163,298	5,819,617	14,982,915
Other	62,698,581	8,594,203	71,292,784
Total expenses	$ 854,784,897	$ 110,641,363	$ 965,426,260

Certain costs such as salaries and wages and employee benefits have been allocated among healthcare services and general and administrative categories based on actual direct expenditures incurred by departments, locations, and cost centers, and cost allocations based upon time spent by the System's personnel. Other expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include repairs and maintenance, depreciation, and interest, which are allocated based on statistics such as square footage. Although the methods used were appropriate, alternative methods may provide different results.

13. RECENTLY ISSUED ACCOUNTING STANDARDS

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842).* This new standard, which the System is not required to adopt until its year ending September 30, 2020, is intended to improve financial reporting about leasing transactions by requiring entities that lease assets to recognize on their balance sheet the assets and liabilities for the rights and obligations created by those leases, and to provide additional disclosures regarding the leases. Leases with terms (as defined in the ASU) of twelve months or less are not required to be reflected on an entity's balance sheet.

In June 2018, the FASB issued ASU 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The amendments in this ASU clarify and improve current guidance about whether a transfer of assets (or the reduction, settlement, or cancellation of liabilities) is a contribution or an exchange transaction. The amendments clarify how an entity determines whether a resource provider is participating in an exchange transaction by evaluating whether the resource provider is receiving commensurate value in return for the resources transferred. Additionally, the amendments in this ASU require that an entity determine whether a contribution is conditional on the basis of whether an agreement includes a barrier that must be overcome and either a right of return of assets transferred or a right of release of a promisor's obligation to transfer assets. Finally, ASU 2018-08 amends the "simultaneous release accounting policy" to allow a not-for-profit entity to recognize a restricted contribution directly in net assets without donor restrictions if the restriction is met in the same period that revenue is recognized. The System will be required to adopt this new standard in the year ending September 30, 2020.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash (Topic 230) – Restricted Cash*. This new standard intends to eliminate diversity in practice by requiring the statement of cash flows to present the change in the total cash and cash equivalents, which will include restricted cash and cash equivalents. The Hospital will be required to adopt this new standard in the year ending September 30, 2020.

In May 2019, the FASB issued ASU 2019-06, *Intangibles—Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topic 958), Extending the Private Company Accounting Alternatives on Goodwill and Certain Identifiable Intangible Assets to Not-for-Profit Entities*. The accounting alternatives in this ASU, if elected, will reduce for preparers the cost and complexity associated with the subsequent accounting for goodwill and the accounting for certain items that currently are considered to be identifiable intangible assets for not-for-profit entities. A not-for-profit entity that elects the accounting alternative should amortize goodwill on a straight-line basis over a period not to exceed ten years, test for impairment upon a triggering event, and have the option to elect to test for impairment at the entity level. This ASU also provides not-for-profit entities with an alternative to subsume into goodwill and amortize customer-related intangible assets that are not capable of being sold or licensed independently from the other assets of a business and all noncompetition agreements acquired. This ASU is effective upon issuance and not-for-profit entities electing to adopt these alternatives do not have to demonstrate preferability.

The System is presently evaluating the effects that these ASUs will have on its future financial consolidated statements, including related disclosures.