

CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION

Sharp HealthCare
Years Ended September 30, 2019 and 2018
With Report of Independent Auditors

Ernst & Young LLP



Sharp HealthCare

Consolidated Financial Statements and Supplementary Information

Years Ended September 30, 2019 and 2018

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Report of Independent Auditors

The Board of Directors
Sharp HealthCare

We have audited the accompanying consolidated financial statements of Sharp HealthCare, 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 Financial Statements

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

Auditor’s Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Sharp HealthCare at September 30, 2019 and 2018, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Adoption of Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers*

As discussed in Note 1 to the consolidated financial statements, Sharp HealthCare changed its method of revenue recognition in 2019 as a result of the adoption of the amendments to the FASB Accounting Standards Codification resulting from Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers*. Our opinion is not modified with respect to this matter.

Supplementary Information

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

Ernst + Young LLP

December 19, 2019

Sharp HealthCare

Consolidated Balance Sheets (In Thousands)

	September 30	
	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 374,987	\$ 448,311
Short-term investments	36,087	48,166
Accounts receivable, net	443,984	454,152
Estimated settlements receivable from government programs, net	–	393
Inventories	50,782	49,073
Prepaid expenses and other	55,384	58,350
Total current assets	961,224	1,058,445
Long-term investments	350,419	268,888
Assets limited as to use:		
Designated for property	2,515,079	2,253,997
Under bond indentures	43,221	108,261
Other restricted investments	67,832	64,651
Under self-insurance programs	11,256	10,594
Total assets limited as to use	2,637,388	2,437,503
Property and equipment, net	1,543,190	1,490,701
Other assets	156,218	176,369
Total assets	\$ 5,648,439	\$ 5,431,906
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 332,560	\$ 375,420
Accrued compensation and benefits	163,692	173,902
Current portion of long-term debt	17,958	17,467
Estimated settlements payable to government programs, net	2,736	–
Accrued interest	3,708	3,761
Total current liabilities	520,654	570,550
Long-term liabilities	149,960	96,632
Reserves for professional and general liabilities <i>(Note 11)</i>	9,649	12,729
Long-term debt	729,954	759,075
Total liabilities	1,410,217	1,438,986
Net assets:		
Without donor restrictions	4,152,799	3,916,899
With donor restrictions	85,423	76,021
Total net assets	4,238,222	3,992,920
Total liabilities and net assets	\$ 5,648,439	\$ 5,431,906

See accompanying notes.

Sharp HealthCare

Consolidated Statements of Operations (In Thousands)

	Year Ended September 30	
	2019	2018
Revenues:		
Patient service	\$ 2,066,201	\$ 2,058,254
Provider tax	189,841	241,217
Net patient service	2,256,042	2,299,471
Premium	1,478,138	1,401,643
Other	111,415	97,409
Total revenues	3,845,595	3,798,523
Expenses:		
Salaries and wages	1,414,918	1,366,015
Employee benefits	352,981	332,943
Medical fees	632,279	607,300
Purchased services	385,203	363,621
Supplies	459,585	439,497
Provider tax	100,809	129,940
Maintenance, utilities, and rentals	134,996	132,564
Depreciation and amortization	124,806	118,117
Business insurance	13,519	16,401
Interest	19,566	21,842
Other	50,576	54,129
Total expenses	3,689,238	3,582,369
Income from operations	156,357	216,154
Other nonoperating (loss) gain	(1,622)	11,938
Investment income	131,820	126,982
Excess of revenues over expenses	286,555	355,074
Adoption of new accounting pronouncements	–	146,378
Net assets transferred from related party	3,727	20,014
Net assets released from restrictions used for purchase of property and equipment	4,714	6,825
Pension-related changes other than net periodic pension cost	(62,241)	17,816
Other changes in net assets without donor restrictions	3,145	8,506
Increase in net assets without donor restrictions	\$ 235,900	\$ 554,613

See accompanying notes.

Sharp HealthCare

Consolidated Statements of Changes in Net Assets

(In Thousands)

	Year Ended September 30	
	2019	2018
Net assets without donor restrictions:		
Excess of revenues over expenses	\$ 286,555	\$ 355,074
Adoption of new accounting pronouncements	–	146,378
Net assets transferred from related party	3,727	20,014
Net assets released from restrictions used for purchase of property and equipment	4,714	6,825
Pension-related changes other than net periodic pension cost	(62,241)	17,816
Other changes in net assets without donor restrictions	3,145	8,506
Increase in net assets without donor restrictions	235,900	554,613
Net assets with donor restrictions:		
Contributions	18,999	27,967
Investment income	635	682
Change in net unrealized gains on investments	186	419
Net assets released from restrictions	(13,098)	(12,823)
Other changes in net assets with donor restrictions	2,680	(1,763)
Increase in net assets with donor restrictions	9,402	14,482
Increase in net assets	245,302	569,095
Net assets, beginning of year	3,992,920	3,423,825
Net assets, end of year	\$ 4,238,222	\$ 3,992,920

See accompanying notes.

Sharp HealthCare

Consolidated Statements of Cash Flows

(In Thousands)

	Year Ended September 30	
	2019	2018
Operating activities		
Increase in net assets	\$ 245,302	\$ 569,095
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Income from discontinued operations		
Net assets transferred from related party	(3,841)	(20,014)
Noncash gains	(507)	(6,297)
Depreciation of operating and nonoperating facilities	124,806	118,117
Amortization, including deferred financing costs	(911)	(576)
Change in fair value of swaps	12,553	(5,338)
Restricted contributions and investment income, net	(19,634)	(28,649)
Pension-related changes other than net periodic pension cost	62,241	(17,816)
Changes in assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	10,173	(115,213)
Inventories	(1,709)	(974)
Short-term investments	12,079	2,987
Assets limited to use and long-term investments	(281,417)	(337,003)
Prepaid expenses and other	11,876	(73,839)
Estimated settlements receivable from/payable to government programs, net	3,129	(3,138)
Increase (decrease) in:		
Accounts payable and accrued liabilities, long-term liabilities, and other liabilities	(59,589)	102,191
Accrued compensation and benefits	(10,210)	26,114
Net cash provided by operating activities	104,341	209,647
Investing activities		
Acquisition of property and equipment, net of retirements	(176,436)	(270,263)
Investments in joint ventures	(3,292)	-
Other investing activities	(126)	-
Settlement of notes receivable	-	10,072
Proceeds from sale of nonoperating property	-	12,288
Net cash used in investing activities	(179,854)	(247,903)

Sharp HealthCare

Consolidated Statements of Cash Flows (continued)

(In Thousands)

	Year Ended September 30	
	2019	2018
	<i>(As Adjusted)</i>	
Financing activities		
Payments on long-term debt	\$ (12,709)	\$ (13,490)
Extinguishment of long-term debt	–	(118,431)
Payments under capital lease obligations	(4,737)	(4,399)
Proceeds from the issuance of long-term debt, net	–	304,397
Restricted contributions and investment income, net	19,634	28,649
Net cash provided by financing activities	2,188	196,726
Net (decrease) increase in cash and cash equivalents	(73,325)	158,470
Cash and cash equivalents and restricted cash, beginning of year ⁽¹⁾	448,866	290,396
Cash and cash equivalents and restricted cash, end of year ⁽¹⁾	\$ 375,541	\$ 448,866
Supplemental disclosures of cash flow information		
Capital lease obligations for building and equipment	\$ –	\$ (544)
Cash paid for interest	\$ 28,080	\$ 28,003
Accrued obligations for property and equipment	\$ 29,376	\$ 24,693
Net assets transferred from related party	\$ 3,841	\$ 20,014
Extinguishment of loan	\$ –	\$ (37,913)
Forgiveness of note receivable	\$ –	\$ 29,319

⁽¹⁾Cash and cash equivalents and restricted cash includes \$554, \$555 and \$558 of restricted cash on September 30, 2019, 2018, and 2017, respectively.

See accompanying notes.

Sharp HealthCare

Notes to Consolidated Financial Statements

September 30, 2019

1. Summary of Significant Accounting Policies

Organization

Sharp HealthCare (SHC) is a California nonprofit public benefit corporation with corporate offices in San Diego, California. SHC, together with its affiliated entities (collectively, Sharp), constitutes a regional integrated health care delivery system, primarily serving the residents of San Diego County. The consolidated financial statements of Sharp include following:

- SHC, including shared corporate services and Medical Foundation activities consisting of Sharp Reese-Stealy Medical Centers, SharpCare, Sharp Cardiovascular & Thoracic Center, and Sharp Kidney & Pancreas Transplant Center
- Sharp Memorial Hospital (SMH), including Stephen Birch Healthcare Center, Sharp Mary Birch Hospital for Women and Newborns, Sharp Outpatient Pavilion, Sharp Mesa Vista Hospital, and Sharp McDonald Center
- Sharp Chula Vista Medical Center (SCVMC)
- Sharp Grossmont Hospital (SGH)
- Sharp Coronado Hospital and HealthCare Center (SCHHC)
- Sharp Health Plan (SHP)
- Continuous Quality Insurance SPC (CQI SPC)
- Sharp HealthCare Foundation (SHF)
- Grossmont Hospital Foundation (GHF)

SHC, SMH, SCVMC, and SGH are collectively the Obligated Group under certain bond indentures (see Note 6).

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of Sharp's consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recently Adopted Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This ASU converged and replaced existing revenue recognition guidance, including industry-specific guidance which requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Sharp adopted ASU 2014-09 on October 1, 2018, using the full retrospective method of transition. As a result, Sharp recorded an adjustment of \$146,378,000 which is included as an increase in net assets without donor restrictions, related to the Provider Tax Program for the periods January 1, 2015, through September 30, 2017 (see further discussion of the Provider Tax Program in Note 3). The adoption of the new standard also impacted the presentation of the consolidated statement of operations, where "provision for doubtful accounts" is no longer presented as a separate line item and "patient service" revenues are presented net of estimated implicit price concession revenue deductions. The presentation of "allowance for doubtful accounts" has also been removed from the presentation in the consolidated balance sheets with the adoption of the new standard. There were no other material impacts from the adoption of the new standard.

In March 2017, the FASB issued ASU 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, which amends the guidance to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost in the financial statements. On a retrospective basis, the amendment requires an employer to separate the service cost component from the other components of net benefit cost and reflect the other components of net benefit costs to nonoperating income. Sharp adopted ASU 2017-07 on October 1, 2018, with retrospective

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

application. As a result, the consolidated statements of operations was adjusted to reflect an increase to Employee benefits with a corresponding decrease to Other nonoperating loss of \$5,138,000 and \$5,728,000 for year ended September 30, 2019 and 2018, respectively.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, which provides revised guidance concerning certain matters involving the recognition, measurement, and disclosure of financial assets and financial liabilities. Among other things, ASU 2016-01 requires equity investments, except those accounted for under the equity method of accounting or those that result in consolidation, to be measured at fair value with changes in fair value recognized in net income; simplifies the impairment assessment of equity investments not having readily determinable fair values by requiring a qualitative assessment to identify impairment so that it is similar to the qualitative assessment applied to long-lived assets, goodwill, and indefinite-lived intangibles; and eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for nonpublic entities. The revised guidance does not alter the basic framework for classifying debt instruments held as financial assets. Sharp adopted ASU 2016-01 on October 1, 2018, which did not have a material impact on the consolidated financial statements.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. Under the new guidance, the current three classes of net assets (i.e., unrestricted, temporarily restricted, and permanently restricted) have been replaced with two new classes of net assets: net assets with donor restrictions and net assets without donor restrictions. The main provisions of this update are to present on the consolidated balance sheet and on the consolidated statement of operations amounts for two classes of net assets at the end of the period, rather than for the previously required three classes. This update also requires the enhanced disclosures about self-imposed limits on the use of resources, composition of net assets with donor restrictions, disclosures about liquidity and availability of resources, amounts of expenses by both their natural classification and their functional classification, methods used to allocate costs among program and support functions, and other disclosures to improve the usefulness of information provided to donors, grantors, creditors, and other users of financial statements. Sharp adopted ASU 2016-14 on October 1, 2018, with retrospective application, and has adjusted the presentation of the consolidated financial statements accordingly. Sharp has elected to apply the practical expedient, which allows for disclosure of liquidity, availability of resources, and additional disclosure of functional expenses on a prospective basis.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the FASB Emerging Issues Task Force)*. ASU 2016-15 is intended to reduce diversity in current practice for presentation of certain cash receipts and cash payments not previously covered by the guidance. Sharp adopted ASU 2016-15 on October 1, 2018, which did not have a material impact on the consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force)*. The amendments in this update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The amendments in ASU 2016-18 do not provide a definition of restricted cash or restricted cash equivalents. Sharp adopted ASU 2016-18 on October 1, 2018. As part of adoption, Sharp also adjusted the consolidated statement of cash flows for fiscal year ended September 30, 2018, to include restricted cash.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with original maturities of three months or less. Sharp routinely invests its surplus operating funds in money market mutual funds. These funds generally invest in highly liquid U.S. government and agency obligations.

Net Patient Accounts Receivable

Net patient accounts receivable and net patient service revenue have been adjusted to the estimated amounts expected to be received based on contractual rates for services rendered, inclusive of the estimated price concession.

Inventories

Inventories, consisting principally of supplies, are stated at the lower of cost or market value.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Short-Term Investments

Short-term investments include corporate and government obligation securities, which are included in professionally managed portfolios, and are measured at fair value in the consolidated balance sheets. The maturities of these securities do not exceed one year. Investment income or loss (including unrealized and realized gains and losses) is included in the consolidated statements of operations.

Long-Term Investments

Long-term investments, which are included in professionally managed portfolios, are measured at fair value in the consolidated balance sheets. The maturities of these securities are in excess of one year or are investments in equities that are not expected to be liquidated over the next year. Investment income or loss (including unrealized and realized gains and losses) is included in the consolidated statements of operations.

Assets Limited as to Use

Assets limited as to use invested in debt and equity securities with readily determined fair values are measured at fair value in the consolidated balance sheets. Investment income or loss (including unrealized and realized gains and losses) is included in the consolidated statements of operations unless the income or loss is restricted by donor or law.

Alternative investments represent ownership interests in a private equity limited partnership. The limited partnership has a general manager with full discretionary authority over investment decisions. The private equity limited partnership invests in companies operating in segments within the health care sector. Alternative investments are accounted for using the net asset value (NAV) expedient, which is determined using investment valuations provided by the general partner, and approximates fair value. Alternative investments generally are not marketable and have underlying investments that may not have quoted market values. The estimated value of such investments is subject to uncertainty and could have differed had a ready market existed. The overall risk is the investment and capital call commitments as discussed in Note 2.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Assets limited as to use primarily include assets set aside by Sharp's Board of Directors (the Board) for future capital improvements, over which the Board retains control and may at its discretion subsequently designate for other purposes, and amounts held by trustees under indenture agreements. Assets limited as to use consist of the following:

Designated for property – Cash resources not required for operations have been designated as funded depreciation to be used for future capital improvements. This designation may be changed and such funds used for other purposes. At September 30, 2019 and 2018, \$37,866,000 and \$25,896,000, respectively, of such assets are pledged as collateral for notes payable and other liabilities.

Under bond indentures – In accordance with the terms of Sharp's various bond indentures, certain bond proceeds and principal and interest payments have been deposited with a trustee and are limited as to use in accordance with the related indentures.

Other restricted investments – Certain cash and investments are limited as to use for future community benefit and for other purposes.

Under self-insurance programs – Certain cash and investments are restricted under Sharp's professional liability self-insurance program.

Derivative Instruments

Sharp recognizes all derivatives in its consolidated balance sheets at fair value, with changes in fair value recorded in the consolidated statements of operations (see Note 6).

Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset from 3 to 40 years and is computed using the straight-line method. Property and equipment under capital lease obligations are amortized on the straight-line method over the lease term or the estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the consolidated statements of operations.

Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Gifts of long-lived assets such as land, buildings, or equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Unamortized Financing Costs

Costs incurred in obtaining long-term financing are amortized over the terms of the related obligations using the effective interest method.

Net Assets

Net assets, revenues, gains, and losses are classified on the existence or absence of donor or grantor imposed restrictions. Net assets and changes therein are classified and reported as follows:

Net assets without donor restrictions – Net assets available for use in general operations and not subject to donor restrictions. Board-designated funds to be used in the future for specific projects are included in net assets without donor restrictions.

Net assets with donor restrictions – Net assets whose use by Sharp has been limited by donor imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as to a specific time period or purpose. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for the resource was restricted has been fulfilled, or both.

Impairment or Disposal of Long-Lived Assets

Sharp reviews long-lived assets for impairments when events or changes in business conditions indicate that their carrying values may not be recoverable. Sharp considers assets to be impaired and writes them down to fair value if expected undiscounted cash flows are less than the carrying amounts. No impairments were recorded in 2019 or 2018.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Income From Operations

Sharp's primary purpose is to provide diversified health care services to the community served by its affiliates. Only those activities directly associated with the furtherance of this purpose are considered operating activities and classified as operating revenues and expenses. Items excluded from income from operations consist of investment income, gains and losses on disposition of property and equipment, changes in the fair value of interest rate swaps, and net income from SHF and GHF.

Excess of Revenues Over Expenses

The accompanying consolidated statements of operations include excess of revenues over expenses (not-for-profit performance indicator) and other changes in net assets without donor restrictions. Changes in net assets without donor restrictions that are excluded from excess of revenues over expenses, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services, long-lived assets acquired using contributions that by donor restriction were to be used for the purposes of acquiring such assets, and pension-related changes other than net periodic pension cost.

Net Patient Service Revenues

Sharp has agreements with third-party payors that provide for payments to Sharp at amounts different from its established rates. Sharp's patient service revenues are reported at the amount that reflects the consideration to which Sharp expects to be paid for providing patient care based on the terms of the contractual agreement with the payor, Sharp's historical settlement activity and other information. These amounts are due from patients and third-party payors, including health insurers and government programs. Patients who meet Sharp'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. Generally, Sharp bills the patients and third-party payors after services are performed.

Patient service revenues are recognized as performance obligations are satisfied. Inpatient services are performance obligations satisfied over time and revenue is recognized based on actual charges incurred in the reporting period. Unsatisfied or partially unsatisfied performance obligations relate to inpatient acute care services not completed by the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

generally occurs within days or weeks of the end of the reporting period. Outpatient services are performance obligations satisfied at a point in time and revenue is recognized when goods or services are provided, and Sharp does not believe it is required to provide additional goods or services.

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

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 patient service revenues when information becomes available. The impact of revenue arising from a change in the estimate of transaction price concessions for performance obligations satisfied in prior years was not material in fiscal years ended September 30, 2019 and 2018.

Premium Revenues

Sharp has agreements with various employers and health maintenance organizations to provide medical services to subscribing participants. Under these agreements, Sharp receives monthly capitation payments based on the number of participants who have selected Sharp, regardless of services actually performed by Sharp.

Other Revenues

Other revenue includes unrestricted donations, retail pharmacy gross revenue, management services, parking, and others. Revenue is recognized when obligations under the terms of the contract are satisfied. Revenues from these services are measured at the amount of consideration Sharp expects to receive for those services.

Health Care Service Costs

Sharp contracts with certain health care providers for the provision of medical services to eligible members. These services include primary care and specialty physician services, inpatient and outpatient facility services, pharmacy, and other medical services. Providers are paid on capitated, per diem, and structured fee-for-service bases.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Health care service costs (included in medical fees and purchased services on the accompanying consolidated statements of operations) are accrued in the period in which the services are provided to enrollees, based in part on estimates, including estimates of medical services provided but not yet reported to Sharp.

Charity Care

Sharp's policy is to accept all patients regardless of their ability to pay. In assessing a patient's ability to pay, Sharp utilizes financial eligibility requirements or criteria. Sharp provides charity care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Charity care is not reported as revenue because Sharp does not pursue collection of amounts determined to qualify as charity care.

Charity care costs are calculated using a ratio of cost to gross charge methodology by department. Direct revenues and costs of each department were included in the calculation, in addition to an allocation of overhead costs.

The cost of charity care is summarized as follows:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Charity care, at cost	\$ 23,865	\$ 25,005

Contributions

Unconditional promises to give cash and other assets to Sharp are reported at fair value at the date the promise is received. Conditional promises to give and indications or intentions to give are reported at fair value at the date the gift becomes unconditional. The gifts are reported as support with 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 with restrictions are reclassified as net assets without restrictions and reported on the consolidated statements of operations as other operating revenues.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions and included in other nonoperating (loss) gain in the consolidated statements of operations.

Contributions Received by Related Parties

Sharp recognizes an interest in the net assets of related-party fundraising organizations when Sharp is the sole beneficiary and has the ability to influence or control the financial and operating decisions of such organizations. For the years ended September 30, 2019 and 2018, Sharp held an interest in the net assets of Coronado Hospital Foundation (CHF), a philanthropic organization dedicated to supporting the programs and services of SCHHC. Sharp's interest in the total net assets of CHF totaled \$11,680,000 and \$7,496,000 as of September 30, 2019 and 2018, respectively, and is included in other assets on the accompanying consolidated balance sheets. Changes in Sharp's interest in the net assets without donor restrictions of CHF are included on the consolidated statements of operations as a component of the total change in net assets without donor restrictions separate from excess revenues over expenses, and totaled \$1,504,000 and \$1,914,000 for the years ended September 30, 2019 and 2018, respectively. Changes in Sharp's interest in CHF's net assets that are subject to donor restrictions are included on the consolidated statements of changes in net assets as a component of other changes in net assets with donor restrictions, and totaled \$2,680,000 and \$(1,763,000) for the years ended September 30, 2019 and 2018, respectively.

Income Taxes

The principal operations of Sharp are exempt from taxation pursuant to Section 501(c)(3) of the Internal Revenue Code and related California provisions.

Sharp recognizes tax benefits from any uncertain tax positions only if it is more likely than not the tax position will be sustained, based solely on its technical merits, with the taxing authority having full knowledge of all relevant information. Sharp records a liability for unrecognized tax benefits from uncertain tax positions as discrete tax adjustments in the first interim period that the more-likely-than-not threshold is not met. Sharp recognizes deferred tax assets and liabilities for temporary differences between the financial reporting basis and the tax basis of its assets and liabilities along with net operating loss and tax credit carryovers only for tax positions that meet the more-likely-than-not recognition criteria. At September 30, 2019 and 2018, no such assets or liabilities were recorded.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Accounting Standards Issued But Not Yet Adopted

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which amends the guidance relating to the definition of a lease, recognition of lease assets and lease liabilities on the balance sheet, and the disclosure of key information about leasing arrangements. Under the new standard, all lessees must recognize a right-of-use asset and liability on the balance sheet for all leases with terms in excess of 12 months. Operating leases were previously not recognized on the balance sheet. Consistent with current guidance, a lessee's recognition, measurement, and presentation of expenses and cash flows arising from a lease will continue to depend primarily on its classification. The ASU will be effective for Sharp on October 1, 2019, and Sharp has elected the optional transition method to apply the standard as of the effective date and therefore, will not apply the standard to the comparative periods presented in the consolidated financial statements. Sharp intends to elect certain practical expedients and will carry forward historical conclusions related to (1) contracts that contain leases, (2) existing lease and easement classification, and (3) initial direct costs. Sharp will not elect the hindsight practical expedient, which permits the use of hindsight when determining lease term and impairment of right-of-use assets. Further, Sharp will elect a short-term lease exception policy, permitting Sharp to not apply the recognition requirements of this standard to short-term leases (i.e., leases with terms of 12 months or less) and an accounting policy to account for lease and non-lease components as a single component for certain classes of assets. Upon adoption, Sharp expects to increase lease assets and lease liabilities which will have a material impact on the consolidated balance sheets and does not expect the transition adjustment will have a material impact on the consolidated statements of operations, consolidated statements of cash flows or related disclosures.

In March 2017, the FASB issued ASU 2017-06, *Plan Accounting: Defined Benefit Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting (a consensus of the FASB Emerging Issues Task Force)*, which enhances the disclosure and financial statement presentation requirements for an employee benefit plan's interest in a master trust and aligns such requirements across all employee benefit plans. The adoption of ASU 2017-06 is required for Sharp on October 1, 2019, and management is currently evaluating the effect of this guidance, if any, on its consolidated financial statements.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which assists not-for-profit and other entities in (1) evaluating whether transactions should be accounted for as contributions (i.e., nonreciprocal transactions) within the scope of FASB ASC Topic 958, *Not-for-Profit Entities*, or as exchange (i.e., reciprocal) transactions subject to other guidance (e.g., FASB ASC 606, *Revenue from Contracts with Customers*), and (2) distinguishing between conditional and unconditional contributions. The adoption of ASU 2018-08 is required for Sharp on October 1, 2019, for transactions in which Sharp serves as a resource recipient and on October 1, 2020, for transactions in which Sharp serves as a resource provider. Management is currently evaluating the effect of this guidance, if any, on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15, *Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract*, which requires an entity (customer) in a hosting arrangement that is a service contract to capitalize certain costs incurred during the application development stage depending on the nature of the costs. Costs incurred during the preliminary project and post implementation stages are expensed as the activities are performed. Costs capitalized pursuant to this guidance are to be amortized over the term of the hosting arrangement in the same line item in the statement of operations where the non-capital hosting fees are expensed. The capitalized implementation costs are required to be presented in the statement of cash flows in the same manner as fees associated with the hosting element (operating activities), and in the balance sheet in the same line item that a prepayment of fees associated with the hosting element would be presented. Sharp plans to early adopt ASU 2018-15 on October 1, 2019, as permitted by the guidance. Management is currently evaluating the effect of this guidance, if any, on its consolidated financial statements.

2. Fair Value Measurements

Sharp accounts for certain assets at fair value. A fair value hierarchy for valuation inputs has been established to prioritize the valuation inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels, which is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

- Level 1 – Pricing is based on observable inputs such as quoted prices for identical assets in active markets. Financial assets in Level 1 include U.S. Treasury securities and listed equities.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

- Level 2 – Pricing inputs are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Financial assets and liabilities in this category generally include corporate bonds, U.S. government agency securities, commercial paper, supranational bonds, negotiable certificates of deposit, fixed-income funds, mortgage-backed securities, interest rate swaps, and commingled plan trust funds.
- Level 3 – Pricing inputs are generally unobservable and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities. The fair values are therefore determined using factors that involve considerable judgment and interpretations, including, but not limited to, private and public comparables, third-party appraisals, discounted cash flow models, and fund manager estimates. Sharp does not hold any financial assets that would be included in this category.

Assets and liabilities measured at fair value are based on one or more of three valuation techniques as identified below. The valuation techniques are as follows:

- a) Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. This technique was utilized for all Level 1 investments.
- b) Cost approach: Amount that would be required to replace the service capacity of an asset (replacement cost). This technique was utilized for all Level 2 investments except for swaps.
- c) Income approach: Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques, option-pricing, and excess earnings model). This technique was utilized for swaps.

Sharp's investments in partnerships, limited liability companies, and similarly structured entities amounting to approximately \$13,983,000 and \$14,717,000 as of September 30, 2019 and 2018, respectively, are accounted for using the equity method of accounting, which is not a fair value measurement, and are included in other assets on the consolidated balance sheets.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

Only assets and liabilities measured at fair value on a recurring basis are shown in the three-tier fair value hierarchy.

	Total		Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)		NAV Practical Expedient
<i>(In Thousands)</i>							
September 30, 2019							
Short-term investments:							
U.S. treasury obligations	\$ 14,758	\$	14,758	\$	–	\$	–
Corporate bonds	8,981		–		8,981		–
U.S. government agencies	5,238		–		5,238		–
Commercial paper	5,909		–		5,909		–
Negotiable certificates of deposit	1,050		–		1,050		–
Interest receivable	151		–		151		–
	\$ 36,087	\$	14,758	\$	21,329	\$	–
Long-term investments:							
Equities	\$ 43,489	\$	43,489	\$	–	\$	–
U.S. treasury obligations	80,786		80,786		–		–
Corporate bonds	124,897		–		124,897		–
U.S. government agencies	48,161		–		48,161		–
Mortgage-backed securities and collateralized mortgage obligations	14,613		–		14,613		–
Asset-backed securities	23,973		–		23,973		–
Supranational	13,010		–		13,010		–
Interest receivable	1,490		–		1,490		–
	\$ 350,419	\$	124,275	\$	226,144	\$	–

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	NAV Practical Expedient
<i>(In Thousands)</i>				
September 30, 2019				
Assets limited as to use:				
Designated for property:				
Cash and cash equivalents	\$ 18,011	\$ 18,011	\$ —	\$ —
Equities	1,324,367	1,324,367	—	—
U.S. treasury obligations	461,623	461,623	—	—
Corporate bonds	440,736	—	440,736	—
U.S. government agencies	81,421	—	81,421	—
Mortgage-backed securities and collateralized mortgage obligations	68,358	—	68,358	—
Commercial paper	17,759	—	17,759	—
Asset-backed securities	68,372	—	68,372	—
Supranational	27,465	—	27,465	—
Private equity	1,474	—	—	1,474
Interest receivable	5,493	—	5,493	—
	\$ 2,515,079	\$ 1,804,001	\$ 709,604	\$ 1,474
Under bond indentures:				
Cash and cash equivalents	\$ 1,260	\$ 1,260	\$ —	\$ —
U.S. treasury obligations	27,944	27,944	—	—
Corporate bonds	3,552	—	3,552	—
U.S. government agencies	3,001	—	3,001	—
Commercial paper	5,045	—	5,045	—
Asset-backed securities	1,024	—	1,024	—
Supranational	1,249	—	1,249	—
Interest receivable	146	—	146	—
	\$ 43,221	\$ 29,204	\$ 14,017	\$ —

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	NAV Practical Expedient
<i>(In Thousands)</i>				
September 30, 2019				
Assets limited as to use (continued):				
Other restricted investments:				
Cash and cash equivalents	\$ 1,592	\$ 1,592	\$ —	\$ —
Equities	35,053	35,053	—	—
U.S. treasury obligations	14,170	14,170	—	—
Fixed income funds	1,178	1,148	30	—
Corporate bonds	9,968	—	9,968	—
U.S. government agencies	2,168	—	2,168	—
Mortgage-backed securities and collateralized mortgage obligations	1,606	—	1,606	—
Commercial paper	263	—	263	—
Asset-backed securities	1,106	—	1,106	—
Supranational	603	—	603	—
Interest receivable	125	—	125	—
	\$ 67,832	\$ 51,963	\$ 15,869	\$ —

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	NAV Practical Expedient
Total				
<i>(In Thousands)</i>				
September 30, 2019				
Assets limited as to use (continued):				
Under self-insurance programs:				
Cash and cash equivalents	\$ 44	\$ 44	\$ —	\$ —
Equities	2,164	2,164	—	—
U.S. treasury obligations	2,869	2,869	—	—
Corporate bonds	3,773	—	3,773	—
U.S. government agencies	917	—	917	—
Mortgage-backed securities and collateralized mortgage obligations	627	—	627	—
Commercial paper	134	—	134	—
Asset-backed securities	459	—	459	—
Supranational	226	—	226	—
Interest receivable	43	—	43	—
	\$ 11,256	\$ 5,077	\$ 6,179	\$ —
 Net swap payables	 \$ 4,788	 \$ —	 \$ 4,788	 \$ —
	\$ 4,788	\$ —	\$ 4,788	\$ —

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

The following table provides the composition of certain investment assets as of September 30, 2018. Only assets and liabilities measured at fair value on a recurring basis are shown in the three-tier fair value hierarchy.

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	NAV Practical Expedient
<i>(In Thousands)</i>				
September 30, 2018				
Short-term investments:				
U.S. treasury obligations	\$ 7,071	\$ 7,071	\$ —	\$ —
Corporate bonds	24,612	—	24,612	—
U.S. government agencies	5,473	—	5,473	—
Commercial paper	3,158	—	3,158	—
Negotiable certificates of deposit	2,045	—	2,045	—
Asset-backed securities	72	—	72	—
Supranational	5,498	—	5,498	—
Interest receivable	237	—	237	—
	<u>\$ 48,166</u>	<u>\$ 7,071</u>	<u>\$ 41,095</u>	<u>\$ —</u>
Long-term investments:				
Equities	\$ 30,526	\$ 30,526	\$ —	\$ —
U.S. treasury obligations	63,505	63,505	—	—
Corporate bonds	94,177	—	94,177	—
U.S. government agencies	34,285	—	34,285	—
Mortgage-backed securities and collateralized mortgage obligations	7,828	—	7,828	—
Asset-backed securities	24,851	—	24,851	—
Supranational	12,609	—	12,609	—
Interest receivable	1,107	—	1,107	—
	<u>\$ 268,888</u>	<u>\$ 94,031</u>	<u>\$ 174,857</u>	<u>\$ —</u>

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	NAV Practical Expedient
<i>(In Thousands)</i>				
September 30, 2018				
Assets limited as to use:				
Designated for property:				
Cash and cash equivalents	\$ 15,712	\$ 15,712	\$ —	\$ —
Equities	1,244,704	1,244,704	—	—
U.S. treasury obligations	408,707	408,707	—	—
Corporate bonds	357,583	—	357,583	—
U.S. government agencies	74,092	—	74,092	—
Mortgage-backed securities and collateralized mortgage obligations	54,621	—	54,621	—
Commercial paper	17,262	—	17,262	—
Asset-backed securities	49,697	—	49,697	—
Supranational	26,588	—	26,588	—
Private equity	398	—	—	398
Interest receivable	4,633	—	4,633	—
	<u>\$ 2,253,997</u>	<u>\$ 1,669,123</u>	<u>\$ 584,476</u>	<u>\$ 398</u>
Under bond indentures:				
Cash and cash equivalents	\$ 3,340	\$ 3,340	\$ —	\$ —
U.S. treasury obligations	37,949	37,949	—	—
Corporate bonds	42,674	—	42,674	—
U.S. government agencies	5,284	—	5,284	—
Commercial paper	1,492	—	1,492	—
Asset-backed securities	10,338	—	10,338	—
Supranational	6,790	—	6,790	—
Interest receivable	394	—	394	—
	<u>\$ 108,261</u>	<u>\$ 41,289</u>	<u>\$ 66,972</u>	<u>\$ —</u>

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	NAV Practical Expedient
<i>(In Thousands)</i>				
September 30, 2018				
Assets limited as to use (continued):				
Other restricted investments:				
Cash and cash equivalents	\$ 3,442	\$ 3,442	\$ —	\$ —
Equities	33,686	33,686	—	—
U.S. treasury obligations	12,093	—	12,093	—
Fixed income funds	1,164	1,069	95	—
Corporate bonds	8,417	—	8,417	—
U.S. government agencies	2,346	—	2,346	—
Mortgage-backed securities	1,431	—	1,431	—
Commercial paper	357	—	357	—
Asset-backed securities	902	—	902	—
Supranational	702	—	702	—
Interest receivable	111	—	111	—
	\$ 64,651	\$ 38,197	\$ 26,454	\$ —
Under self-insurance programs:				
Cash and cash equivalents	\$ 44	\$ 44	\$ —	\$ —
Equities	2,134	2,134	—	—
U.S. treasury obligations	2,962	2,962	—	—
Corporate bonds	3,236	—	3,236	—
U.S. government agencies	895	—	895	—
Mortgage-backed securities	518	—	518	—
Commercial paper	159	—	159	—
Asset-backed securities	387	—	387	—
Supranational	219	—	219	—
Interest receivable	40	—	40	—
	\$ 10,594	\$ 5,140	\$ 5,454	\$ —
Net swap receivables	\$ 7,766	\$ —	\$ 7,766	\$ —
	\$ 7,766	\$ —	\$ 7,766	\$ —

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

2. Fair Value Measurements (continued)

The nature and risk of investments for which fair value is determined using a calculated NAV is that there is no provision for redemption of funds during the term of the fund. Distribution from the fund will be received at the end of the charter term, which is estimated to be over the next 11 years. The unfunded commitments were \$3,319,000 and \$4,602,000 at September 30, 2019 and 2018, respectively.

Liquidity Management

As part of its liquidity management, Sharp's strategy is to structure its financial assets to be available to satisfy general operating expenses, current liabilities, and other obligations as they come due. Sharp invests cash in excess of daily requirements in short-term investments and has a line of credit, as discussed in Note 6 to help manage unanticipated liquidity needs. Additionally, board designated funds may be utilized if necessary.

Sharp's financial assets available for general operating expenses within one year of September 30, 2019, are as follows:

Cash and cash equivalents	\$ 374,987
Short-term investments	36,087
Accounts receivable, net	443,984
	<u>\$ 855,058</u>

3. Net Patient Service Revenues

Patient Service Revenues

Sharp has agreements with third-party payors that provide for payments to Sharp at amounts different from its established rates. Payment arrangements are as follows:

Medicare: Inpatient acute care services and outpatient services provided to Medicare program beneficiaries are paid at prospectively determined rates per diagnosis. Sharp is paid for cost-reimbursable items at a tentative rate. Physician services are paid based upon established fee schedules. Amounts received from the Medicare programs for hospital services are subject to audit and final settlement by a Medicare Administrative Contractor after submission of annual hospital cost reports. Sharp's Medicare cost reports have been audited generally through

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

3. Net Patient Service Revenues (continued)

September 30, 2015. The estimated net settlement payables are \$3,885,000 and \$1,397,000 and adjustments pertaining to prior-year cost reports resulted in additional revenue of \$1,206,000 and \$7,261,000 at September 30, 2019 and 2018, respectively.

Medi-Cal: Inpatient and outpatient services provided to Medi-Cal program beneficiaries are paid either under contracted rates or cost-reimbursable items at a tentative rate. Services are generally paid at prospectively determined rates per discharge, per occasion of service, or per covered member. Amounts received from Medi-Cal programs are subject to audit and final settlement by the California Department of Health Care Services after submission of annual cost reports. Sharp's Medi-Cal cost reports have been audited generally through September 30, 2017. The estimated net settlement payables and adjustments pertaining to prior-year cost reports were immaterial in 2019 and 2018.

Commercial: Inpatient and outpatient services provided to patients covered under commercial insurance policies are paid using a variety of payment methodologies based on contractual agreements. The transaction price for commercial payors is reduced by explicit contractual adjustments, and implicit price concessions based on collection history with this portfolio of patients.

Other: Inpatient and outpatient services provided to patients not covered by third-party payors are paid based on Sharp's policies and the patient's ability to pay. Sharp reduces the transaction price by implicit price concessions to uninsured patients and patients with uninsured balances, such as copays and deductibles. The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts Sharp expects to collect based on its collection history with this portfolio of patients. Subsequent changes to the estimates are considered variable consideration and are included in patient service revenue when information becomes available.

As part of its patient service revenue analysis, Sharp examines the fluctuations in payor and entity type as each factor represents a varying degree of uncertainty regarding the nature, timing and extent of payments.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

3. Net Patient Service Revenues (continued)

The composition of patient service revenues by payor is as follows:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Medicare	\$ 585,147	\$ 589,664
Medi-Cal	416,797	414,347
Commercial	1,051,490	1,041,299
Other	12,767	12,944
	<u>\$ 2,066,201</u>	<u>\$ 2,058,254</u>

The composition of patient service revenues by entity type is as follows:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Hospital	\$ 1,813,876	\$ 1,822,199
Medical Foundation	196,484	180,757
Other	62,099	77,063
Eliminations	(6,258)	(21,765)
	<u>\$ 2,066,201</u>	<u>\$ 2,058,254</u>

Provider Tax Revenue

California legislation established a program (the Program) that imposes a fee (provider tax expense) on certain general acute care hospitals in order to make supplemental and grant payments (provider tax revenues) to hospitals serving the Medi-Cal population. Some of these payments will be made directly by the state, while others will be made by the Medi-Cal managed care plans, which will receive increased rates from the state. Outside of this legislation, the California Hospital Association has created a private program, operated by the California Health Foundation and Trust (CHFT), which was established to alleviate disparities potentially resulting from the implementation of the Program. Private hospitals that are profitable under the program contribute pledge amounts (Pledge Fee) to CHFT. These funds are used to provide grants to hospitals that may not be profitable under the Program.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

3. Net Patient Service Revenues (continued)

The Program is generally established for a 30-month period. The most recent program, a 30-month program, beginning January 1, 2017, expired on June 30, 2019. The Program activity is included on the consolidated statements of operations and consolidated balance sheets as of and for the 12 months ended September 30:

	2019	2018
	<i>(In Thousands)</i>	
Provider tax revenue	\$ 189,841	\$ 241,217
Provider tax expense	(100,809)	(129,940)
Income from operations from provider tax	\$ 89,032	\$ 111,277
Accounts receivable, net	\$ 116,068	\$ 138,347
Other assets	68,033	88,263
Accounts payable and accrued liabilities	34,578	45,330
Long-term liabilities	9,510	15,180

Prior to the adoption of ASC 606, Sharp recognized revenues as components of the program were approved by the Center for Medicare and Medicaid Services (CMS). Upon adoption of ASC 606, Sharp recognizes revenue over the period to which the program relates as long as collection is probable and estimable. Collection is deemed probable and estimable once the model has been published and the tax waiver, which establishes the program, has been approved by CMS. The following is a summary of the impact of adoption on the consolidated statement of operations and consolidated balance sheet as of and for the 12 months ended September 30, 2018:

	As Adjusted	Previously Reported
	<i>(In Thousands)</i>	
Provider tax revenue	\$ 241,217	\$ 248,520
Provider tax expense	(129,940)	(161,066)
Income from operations from provider tax	\$ 111,277	\$ 87,454

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

3. Net Patient Service Revenues (continued)

	As Adjusted	Previously Reported
	<i>(In Thousands)</i>	
Accounts receivable, net	\$ 454,152	\$ 380,297
Prepaid expenses and other	58,350	100,255
Other assets	176,369	88,106
Accounts payable and accrued liabilities	375,420	440,588
Long-term liabilities	96,632	81,452

On September 30, 2019, the California Department of Health Care Services (DHCS) submitted paperwork to CMS requesting approval a tax waiver necessary to create a sixth program. The new program will span 30 months, covering the period July 1, 2019 to December 31, 2021. Approval of the tax waiver is anticipated in fiscal year 2020.

Premium Revenues

As part of its premium revenue analysis, Sharp examines the fluctuations by entity type as this represents a varying degree of uncertainty regarding the nature, timing and extent of payments.

Sharp's premium revenue is reported at an amount that reflects the consideration to which Sharp expects to be paid.

The composition of premium revenues based on Sharp's entity type is as follows:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Hospital	\$ 599,219	\$ 574,016
Medical Foundation	476,582	453,563
Insurance	786,117	725,274
Eliminations	(383,780)	(351,210)
	\$ 1,478,138	\$ 1,401,643

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

4. Investment Income

Investment income for cash equivalents, short-term investments, long-term investments and assets limited as to use is composed of the following:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Interest income	\$ 74,165	\$ 60,975
Unrealized gains, net	50,635	47,049
Realized gains, net	7,020	18,958
	\$ 131,820	\$ 126,982

5. Property and Equipment

Property and equipment, net consist of the following:

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Land and improvements	\$ 112,627	\$ 112,167
Buildings and improvements	1,740,976	1,682,923
Equipment and furniture	535,662	506,216
Software cost	147,250	143,418
Construction-in-progress	359,366	278,890
	2,895,881	2,723,614
Less accumulated depreciation and amortization	(1,352,691)	(1,232,913)
	\$ 1,543,190	\$ 1,490,701

Depreciation and amortization expense for the years ended September 30, 2019 and 2018, amounted to approximately \$124,806,000 and \$118,117,000, respectively. Included in these amounts is amortization for buildings and equipment under capital lease obligations. Sharp has approximately \$71,685,000 and \$80,720,000 at September 30, 2019 and 2018, respectively, of buildings and equipment under capital lease, at cost. Accumulated depreciation for buildings and equipment under capital lease was \$34,595,000 and \$30,050,000 at September 30, 2019 and 2018,

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

5. Property and Equipment (continued)

respectively. Sharp recorded depreciation expense of \$4,565,000 in fiscal years 2019 and 2018 relating to buildings and equipment under capital lease. Sharp has outstanding commitments to complete construction-in-progress totaling approximately \$79,687,000 at September 30, 2019.

On May 29, 1991, Sharp leased the Grossmont Hospital (the Hospital) existing campus land, buildings, and equipment from the Grossmont Healthcare District (the District). The lease provided for an original 30-year term ending May 29, 2021, at \$1 per year. In 2014, the lease was extended for an additional 30-year term ending on May 29, 2051. The buildings, improvements, and equipment acquired by the Hospital since the inception of the lease will revert to the District at the end of the lease term.

The Hospital and the District initiated, in 2006, a project for the construction of three shelled floors in the Emergency and Critical Care Center, central plant upgrades, infrastructure improvements, and facility renovations (the Project). The Project is being funded using the proceeds of general obligation (GO) bonds. In July 2007 and February 2011, \$85,500,000 and \$136,860,000, respectively, in GO bonds were issued by the District. In May 2015, \$24,500,000 in GO bonds were issued by the District, which was the third and final series of GO bonds. Sharp considers the District to be a related party based upon these relationships between Sharp and the District.

The Hospital is not required to make any payments to the District with respect to the contribution to the Project of assets constructed using the GO bond proceeds. Therefore, the GO bonds have not been included in the consolidated financial statements as a liability of Sharp. The portion of the Project funded with the GO bonds is being recognized as a transfer of net assets from the District as the Project is completed. In fiscal 2019 and 2018, the Hospital recorded \$3,841,000 and \$20,014,000, respectively, of construction-in-progress and a related transfer of net assets for the portion of the Project completed during the year with proceeds of the GO bonds.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt

Long-term debt consists of the following:

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Series 2017B and Series C Variable Rate Revenue Bonds (Series 2017B and C Bonds). Principal is due in annual amounts ranging from \$1,455,000 in 2022 to \$10,380,000 in 2052. The borrowing amount is net of unamortized debt issuance costs of \$985,000 at September 30, 2019. Interest is payable monthly at a variable rate (1.52% at September 30, 2019).	\$ 148,090	\$ 148,045
Series 2017A Revenue Bonds (Series 2017A Bonds) collateralized by revenues of the Obligated Group. Principal due in annual amounts ranging from \$1,640,000 in 2031 to \$34,030,000 in 2047. Interest payable semiannually at rates ranging from 3.00% to 5.00%. The borrowing amount is net of the unamortized original issue premium of \$15,004,000 and unamortized debt issuance costs of \$1,313,000 at September 30, 2019. The bonds include issuer call features totaling \$141,840,000 in 2028.	155,531	156,068
Series 2014A Revenue Bonds (Series 2014A Bonds) collateralized by revenues of the Obligated Group. Principal due in annual amounts ranging from \$4,105,000 in 2020 to \$32,300,000 in 2043. Interest payable semiannually at rates ranging from 4.50% to 5.00%. The borrowing amount is net of the unamortized original issue premium of \$5,143,000 and unamortized debt issuance costs of \$1,410,000 at September 30, 2019. The bonds include issuer call features totaling \$140,120,000 in 2023.	155,523	158,112
Series 2009C and Series D Variable Rate Revenue Bonds (Series 2009C and D Bonds). Principal is due in annual amounts ranging from \$145,000 in 2022 to \$11,805,000 in 2035. Interest is payable monthly at a variable rate (1.27% at September 30, 2019).	99,880	99,880

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt (continued)

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
<p>Series 2011A Revenue Bonds (Series 2011A Bonds) collateralized by revenues of the Obligated Group. Principal due in annual amounts ranging from \$245,000 in 2020 to \$8,180,000 in 2030. Interest payable semiannually at rates ranging from 4.63% to 6.00%. The borrowing amount is net of the unamortized original issue premium of \$180,000 and unamortized debt issuance costs of \$491,000 at September 30, 2019. The bonds include issuer call features totaling \$54,490,000 in 2021.</p>	\$ 54,424	\$ 54,542
<p>Series 2012A Revenue Bonds (Series 2012A Bonds) collateralized by revenues of the Obligated Group. Principal due in annual amounts ranging from \$3,490,000 in 2020 to \$5,055,000 in 2028. Interest payable semiannually at rates ranging from 4.00% to 5.00%. The borrowing amount is net of the unamortized original issue premium of \$1,969,000 and unamortized debt issuance costs of \$300,000 at September 30, 2019. The bonds include issuer call features totaling \$30,735,000 in 2023.</p>	39,524	44,956
<p>Series 2009A Variable Rate Revenue Bonds (Series 2009A Bonds). Principal due in annual amounts ranging from \$4,215,000 in 2020 to \$5,360,000 in 2024. The borrowing amount is net of the unamortized debt issuance costs of \$159,000 at September 30, 2019. Interest is payable monthly at a variable rate (1.27% at September 30, 2019).</p>	21,466	25,501
<p>Series 2010A Variable Rate Revenue Bonds (Series 2010A Bonds) collateralized by revenues of the Obligated Group. Principal due in quarterly amounts ranging from \$250,000 to \$450,000 through 2035. The borrowing amount is net of the unamortized debt issuance costs of \$177,000 at September 30, 2019. Interest payable quarterly at a variable rate (1.74% at September 30, 2019).</p>	22,013	22,974

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt (continued)

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Reverse Repurchase Agreement collateralized by U.S. Treasury securities. Principal due in April 2021. Interest payable quarterly at a variable rate (2.99% at September 30, 2019).	\$ 15,500	\$ 15,500
Capital lease obligations at imputed rates of interest ranging from 2.09% to 7.27%, collateralized by leased building or equipment.	35,961	50,964
Total	747,912	776,542
Less current portion	(17,958)	(17,467)
	\$ 729,954	\$ 759,075

On November 28, 2017, Sharp deposited \$12.1 million into an escrow fund to legally defease \$11.0 million of outstanding fixed rate Series 2009B bonds (2009B bonds). The escrow funds were irrevocably designated for retirement of the 2009B bonds on August 1, 2019, which was the earliest date covered by the existing 2009B redemption option. As a result of the defeasance, a \$1.3 million loss on extinguishment of debt was recorded in fiscal year 2018 and is included in other nonoperating gain in the accompanying consolidated statements of operations for the year ended September 30, 2018, which represents advance interest payments through July 2019 and the write-off of the unamortized cost of issuance and bond discount of the defeased portion of the 2009B bonds.

In December 2017, Sharp issued Series 2017A bonds in the amount of \$141.8 million, Series 2017B bonds in the amount of \$74.5 million, and Series 2017C bonds in the amount of \$74.5 million. Costs of issuance associated with the 2017A, 2017B, and 2017C bonds totaling \$2.5 million were paid for with Sharp's operating cash and will be amortized over the life of the bonds. The 2017A bonds provided bond proceeds of \$157.8 million as the bonds sold at a net premium. Sharp used 2017A bond proceeds to advance refund \$99.0 million in outstanding 2009B bonds and fund capital projects. The 2017B and 2017C bonds will fund capital projects. As a result of the advance refunding, \$10.9 million of debt service reserve fund for the 2009B bonds was released and a \$9.3 million loss on extinguishment of debt was recorded and is included in other nonoperating gain in the accompanying consolidated statements of operations for the year ended September 30, 2018, which represents advance interest payments through July 2019 and the write-off of the unamortized cost of issuance and bond discount of the 2009B bonds.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt (continued)

In June 2018, Sharp completed the unwinding of a New Markets Tax Credit (NMTC) financing arrangement that was established in June 2011 to finance the acquisition and construction of certain facilities and equipment. The NMTC program is administered by the federal government and provides tax incentives for the benefit of low-income communities. Upon inception of the arrangement in June 2011, Sharp loaned \$29.3 million to a special purpose entity that was owned and controlled by an unaffiliated banking partner. These loan proceeds, together with invested capital from the bank, were used to capitalize three community development entities (CDEs). Pursuant to terms of the federally managed NMTC program, these CDEs financed an SRS construction project and provided certain tax benefits to the bank for a period of seven years. In June 2018, the seven-year compliance period ended, and an exit agreement was executed between all parties, pursuant to which the bank exercised an option to “put” its interest to Sharp for \$519,000. Upon exercise, Sharp cancelled \$39.3 million in loans previously payable to the CDEs, wrote off the \$1.4 million unamortized cost of issuance, and terminated the \$29.3 million receivable from the special purpose entity. As a result, Sharp recognized an \$8.0 million gain on extinguishment of debt, which is net of \$569,000 in transaction costs and is included in other nonoperating gain in the accompanying consolidated statement of operations.

Scheduled principal payments on long-term debt and payments on capital lease obligations for years ending September 30 are as follows:

	Long-Term Debt	Capital Lease Obligations
	<i>(In Thousands)</i>	
2020	\$ 13,075	\$ 4,883
2021	29,610	4,970
2022	14,910	4,484
2023	16,015	7,100
2024	16,910	5,571
Thereafter	603,970	8,958

Scheduled interest payments Sharp is obligated to make on capital lease obligations referenced in the table noted above total approximately \$8,660,000.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt (continued)

A summary of interest cost on borrowed funds follows:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Interest cost:		
Capitalized	\$ 7,121	\$ 5,263
Charged to operations	19,566	21,842
	<u>\$ 26,687</u>	<u>\$ 27,105</u>

Interest Rate Swaps

During 2014, Sharp entered into a fixed-spread basis swap with a bank. The swap arrangement hedges an initial notional amount of \$80,000,000 at a fixed payor rate of the Securities Industry and Financial Markets Association Municipal Swap Index for the entire swap term, which expires on February 2, 2034, and receives 67% of one-month LIBOR plus 0.733%. Settlements are made quarterly. Cash received on the interest rate swap was \$622,000 and \$536,000 in 2019 and 2018, respectively, which reduced Sharp's overall cost of borrowing and was offset against interest expense. The change in fair value of the swap increased nonoperating income by \$1,354,000 in 2019 and decreased nonoperating income by \$32,000 in 2018.

During 2016, Sharp entered into a forward-starting floating-to-fixed interest rate on the Series 2009B Bonds that were refunded in 2018. The forward swap replaced fixed rates for the 2009B Bonds ranging from 6.00% to 6.25% with synthetic fixed rate debt. The swap agreement hedges an initial notional amount of \$99,075,000 at a fixed payor rate of 1.51% for the entire swap term, which expires on August 1, 2039, and receives 67% of one-month LIBOR. Settlements are to be made monthly, starting in September 2019. The change in fair value of the swap decreased nonoperating income by \$13,245,000 in 2019 and increased nonoperating income by \$4,944,000 in 2018.

During 2017, Sharp entered into a floating-to-fixed interest rate swap on the Series 2003A and B Bonds that were refunded in 2009. The swap agreement hedges an initial notional amount of \$50,175,000 at a fixed payor rate of 3.01% for the entire swap term, which expires on August 1, 2024, and receives 59% of the one-month LIBOR plus 0.14%. Settlements are made weekly. Cash paid on the interest rate swap was \$547,000 and \$797,000 in 2019 and 2018, respectively, which

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt (continued)

increased Sharp's overall cost of borrowing and was offset against interest expense. The change in fair value of the swap decreased nonoperating income by \$514,000 in 2019 and increased nonoperating income by \$1,568,000 in 2018.

During 2018, Sharp entered into a fixed-spread yield curve swap with a bank. The swap arrangement hedges an initial notional amount of \$80,000,000 and entails Sharp paying 67% of one-month LIBOR and receiving 67% of ten-year International Swaps and Derivative Association less 0.375% for the entire swap term, which expires on February 2, 2034. Under the terms of the agreement, Sharp may terminate the swap at any time. Cash paid on the interest rate swap was \$172,000 in 2019 which increased Sharp's overall cost of borrowing and was included in interest expense. Cash received on the interest rate swap was \$30,000 in 2018, which reduced Sharp's overall cost of borrowing and was offset against interest expense. The change in fair value of the swap decreased nonoperating income by \$148,000 in 2019 and \$793,000 in 2018.

Credit Facilities

Sharp has a \$50,000,000 line of credit with a bank, which expires on September 1, 2020, of which \$29,399,000 and \$20,504,000 was available at September 30, 2019 and 2018, respectively. As part of the workers' compensation insurance agreement, letters of credit have been provided as collateral. The total letters of credit used as collateral totaled \$20,601,000 and \$29,496,000 as of September 30, 2019 and 2018, respectively. These letters of credit are each considered a decrease in the available \$50,000,000 line of credit with the bank. There are no amounts outstanding as of September 30, 2019 or 2018.

Sharp has a bank liquidity facility to provide credit enhancement and liquidity support for the \$60,000,000 of Series 2009A Bonds. The bank liquidity facility was executed in February 2009 by a bank letter of credit that expires in April 2022. The letter of credit used as collateral totaled \$21,874,000 and \$26,016,000 at September 30, 2019 and 2018, respectively.

Sharp has a bank liquidity facility to provide credit enhancement and liquidity support for the \$99,880,000 of Series 2009C and D Bonds. The bank liquidity facility was executed in September 2009 by a bank letter of credit that expires in December 2020. The letters of credit used as collateral totaled \$101,391,000 at September 30, 2019 and 2018.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

6. Long-Term Debt (continued)

Sharp has a bank liquidity facility to provide credit enhancement and liquidity support for the \$149,075,000 of Series 2017B and C Bonds. The bank liquidity facility was executed in December 2017 by a bank letter of credit that expires in December 2021. The letters of credit used as collateral totaled \$151,967,000 at September 30, 2019 and 2018.

SHP has a bank credit facility that provides for the issuance of up to an aggregate of \$2,400,000 at September 30, 2019 and 2018, under letters of credit. Such letters of credit are under irrevocable standby letters of credit. At September 30, 2019 and 2018, none of these letters have been drawn upon.

7. Net Assets and Contributions

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

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Hospital programs	\$ 21,963	\$ 19,645
Hospital department	20,544	17,811
Health education	8,052	6,196
Research	6,597	7,074
Purchase of capital assets	2,130	2,699
Indigent care	834	836
Total	60,120	54,261
Subject to passage of time	16,265	12,766
Subject to donor restrictions in conjunction with Sharp spending policy:		
Investment in perpetuity – endowment	9,038	8,994
	\$ 85,423	\$ 76,021

Net assets with restrictions of \$9,038,000 and \$8,994,000 at September 30, 2019 and 2018, respectively, represent investments to be held in perpetuity, the income from which is expendable to support health care services.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

7. Net Assets and Contributions (continued)

From time to time, the Board will designate certain unrestricted funds to be used in the future for specific projects. Board-designated funds included in net assets without donor restrictions were maintained for the following purposes:

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Hospital departments	\$ 3,808	\$ 3,587
Hospital programs	1,130	1,036
Research	451	380
Health education	357	256
Purchase of capital assets	30	2,885
Indigent care	7	4
Total	<u>\$ 5,783</u>	<u>\$ 8,148</u>

As of September 30, 2019, Sharp's pledges receivable, which is included in other receivables and other noncurrent assets, consisted of the following unconditional promises to give:

Pledges due in 2020	\$ 3,463
Pledges due in 2021-2024	8,505
Pledges due after 2024	15,191
Less: Discount on pledges receivable	<u>(7,431)</u>
	<u>\$ 19,728</u>

Endowments

Sharp's endowments consist of 55 separate endowment funds included in assets limited as to use, established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Directors of Sharp's affiliated foundations to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

7. Net Assets and Contributions (continued)

On September 30, 2008, California Senate Bill No. 1329 was signed into law which enacted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) for California. California also adopted one of the optional provisions of the act, creating a rebuttable presumption of imprudence for spending more than 7% of the value of an endowment fund in one year (based on a three-year rolling average). The Board has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Sharp classifies as net assets with donor restriction (a) the original value of gifts donated to the endowment, (b) the original value of subsequent gifts to the endowment, and (c) accumulations to the endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. In accordance with UPMIFA, Sharp considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund, (2) the purposes of Sharp and the donor-restricted endowment fund, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of Sharp, and (7) the investment policies of Sharp.

Sharp has adopted investment and spending policies for endowment assets that attempt to provide a stream of funding to programs supported by its endowment while balancing the risk of investment loss with long-term preservation of purchasing power. Endowment assets include those assets of donor-restricted funds that Sharp must hold in perpetuity or for a donor-specified period as well as board-designated funds.

Sharp targets a diversified asset allocation that places greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints. Sharp's spending policy is to annually appropriate for distribution no more than 4% per year of each endowment fund's fair value.

If the fair market value of assets associated with individual endowment funds fall below the corpus, Sharp management assesses facts and circumstances to determine whether to suspend appropriation activities until the corpus has recovered or to continue to withdraw funds in compliance with UPMIFA in order to fund critical initiatives. Deficiencies of this nature reported in net assets with donor restrictions were a result of unfavorable investment market fluctuations and not material as of September 30, 2019 and 2018.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

7. Net Assets and Contributions (continued)

The endowment net asset composition by fund type was as follows:

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total
	<i>(In Thousands)</i>		
September 30, 2019			
Board-designated endowment funds	\$ 4,925	\$ 3,813	\$ 8,738
Donor-restricted endowment funds	–	16,094	16,094
Total funds	\$ 4,925	\$ 19,907	\$ 24,832
 September 30, 2018			
Board-designated endowment funds	\$ 4,572	\$ 3,699	\$ 8,271
Donor-restricted endowment funds	–	15,619	15,619
Total funds	\$ 4,572	\$ 19,318	\$ 23,890

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

7. Net Assets and Contributions (continued)

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total
	<i>(In Thousands)</i>		
Endowment net assets, September 30, 2017	\$ 4,111	\$ 15,664	\$ 19,775
Investment return:			
Investment income	290	414	704
Net appreciation (realized and unrealized)	247	300	547
Total investment return	537	714	1,251
Contributions	(39)	3,043	3,004
Appropriation of endowment assets for expenditure	(37)	(103)	(140)
Endowment net assets, September 30, 2018	4,572	19,318	23,890
Investment return:			
Investment income	248	268	516
Net appreciation (realized and unrealized)	137	165	302
Total investment return	385	433	818
Contributions	–	225	225
Appropriation of endowment assets for expenditure	(32)	(69)	(101)
Endowment net assets, September 30, 2019	<u>\$ 4,925</u>	<u>\$ 19,907</u>	<u>\$ 24,832</u>

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

8. Functional Expenses

Sharp provides general health care services to residents within its geographic locations. Expenses related to providing these services in the year ended September 30, 2019, are as follows:

	Patient Services	General and Administrative	Purchased Services Under Capitated Agreements	Total
<i>(In Thousands)</i>				
Salaries and wages	\$ 1,219,876	\$ 195,042	\$ —	\$ 1,414,918
Employee benefits	303,829	49,152	—	352,981
Medical fees	586,041	1,907	44,331	632,279
Purchased services	182,707	53,676	148,820	385,203
Supplies	443,651	15,934	—	459,585
Provider tax	100,809	—	—	100,809
Maintenance, utilities, and rentals	110,435	24,561	—	134,996
Depreciation and amortization	110,755	14,051	—	124,806
Business insurance	11,140	2,379	—	13,519
Interest	18,445	1,121	—	19,566
Other	33,399	17,177	—	50,576
Total	\$ 3,121,087	\$ 375,000	\$ 193,151	\$ 3,689,238

Expenses related to providing these services in the year ended September 30, 2018, were as follows (in thousands):

Patient services	\$ 3,058,903
General and administrative	331,788
Purchased services under capitated agreements	191,678
	\$ 3,582,369

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

8. Functional Expenses (continued)

The financial statements report certain expense categories that are attributable to more than one healthcare service or support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including depreciation, amortization, interest, and other occupancy costs, are allocated to a functional region based on a square-footage or units-of-service basis. Allocated healthcare services costs not allocated on a units-of-service basis are otherwise allocated based on revenue.

9. Pension Plans

Sharp sponsors a voluntary retirement plan (the Plan), which consists of defined benefit cash balance plans and a defined contribution plan. Under the defined benefit cash balance plans, Sharp made contributions of \$29,520,000 and \$21,984,000 in 2019 and 2018, respectively.

The following sets forth the funded status of Sharp's defined benefit pension plans:

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 491,438	\$ 496,168
Service cost	23,839	23,794
Interest cost	19,309	15,632
Actuarial loss (gain)	90,126	(26,267)
Plan participant contributions	9,715	9,171
Benefits paid	(26,890)	(27,060)
Benefit obligation at end of year	607,537	491,438
Change in plan assets:		
Fair value of plan assets at beginning of year	487,783	471,818
Actual gain on plan assets	54,468	11,870
Plan participant contributions	9,715	9,171
Employer contributions	29,520	21,984
Benefits paid	(26,890)	(27,060)
Fair value of plan assets at end of year	554,596	487,783
Funded status	\$ (52,941)	\$ (3,655)

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

9. Pension Plans (continued)

The accumulated benefit obligation was \$577,861 and \$467,517 as of September 30, 2019 and 2018, respectively.

The net liability at September 30, 2019, is included on the balance sheet in long-term liabilities. The net liability at September 30, 2018, consists of an unfunded balance of \$4,646,000 related to Sharp's primary defined benefit pension included on the balance sheet in long-term liabilities, partially offset by an overfunded balance of \$991,000 related specifically to the separate defined benefit plan for employees of SGH included on the balance sheet in other assets.

Included in unrestricted net assets are the following amounts that have not yet been recognized in net periodic pension cost:

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Net actuarial loss	\$ 177,109	\$ 117,004
	\$ 177,109	\$ 117,004

Net periodic pension cost includes the following components:

	Year Ended September 30	
	2019	2018
	<i>(In Thousands)</i>	
Employee benefits:		
Service cost	\$ 23,839	\$ 23,794
Other nonoperating gain:		
Interest cost	19,309	15,632
Expected return on plan assets	(30,378)	(29,468)
Recognized net actuarial loss	5,931	8,074
Net periodic pension cost	\$ 18,701	\$ 18,032

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

9. Pension Plans (continued)

Weighted average assumptions used to determine benefit obligations were as follows:

	September 30	
	2019	2018
Discount rate	3.31%	4.33%
Rate of compensation increase	3.00	3.00

Weighted average assumptions used to determine net periodic pension cost were as follows:

	September 30	
	2019	2018
Discount rate	4.33%	3.85%
Expected return on plan assets, net of expenses	6.25	6.25
Rate of compensation increase	3.00	3.00

The expected rate of return on plan assets is updated annually, taking into consideration the Plan's asset allocation, historical returns on the types of assets held in the pension trust, and the current economic environment.

The estimated net actuarial loss for the defined benefit pension plans that will be amortized from net assets into net periodic pension cost during the 2019 fiscal year is \$10,876,000.

Plan Assets

The Plan's assets are invested in an institutional trust company commingled employee benefit plan trust (Commingled Plan Trust). The Plan's asset allocation utilizes a long-range asset allocation strategy. The target asset allocation gradually shifts as the funded ratio increases from an initial mix of 52% equity securities and 48% fixed income when the Plan's funded ratio is less than 100% to an ultimate target of 46% equity securities and 54% fixed income when the Plan's funded ratio reaches 110%.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

9. Pension Plans (continued)

As of September 30, based on the Plan's funded ratio, the Plan's allocation of investments in the Commingled Plan Trust was as follows:

	<u>2019</u>	<u>2018</u>
Asset category:		
Equity securities	50%	53%
Fixed income	50	47
Total	<u>100%</u>	<u>100%</u>

Plan assets are managed according to an investment policy adopted by Sharp's Retirement Committee. Professional investment managers are retained to manage plan assets. The primary objective of the Plan is to generate a consistent total investment return sufficient to pay present and future Plan benefits to retirees. The investment policy includes an asset allocation that includes equities and fixed-income instruments. The target mix represents a long-term asset allocation strategy for the Plan. Although the Retirement Committee will seek to maintain the target mix over the long term, short-term deviations may occur due to market impact and cash flow. The timing and degree of rebalancing of the actual portfolio will be determined by the Retirement Committee.

Financial assets measured at fair value are grouped in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to estimate fair value. These levels and associated valuation methodologies are described in Note 2. All of the Plan's investments in the Commingled Plan Trust are measured using net asset value in accordance with the practical expedient offered by ASU 2015-07 as of September 30, 2019 and 2018.

Contributions

Sharp expects to contribute \$27,900,000 to the Plan in 2020.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

9. Pension Plans (continued)

Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid (in thousands):

2020	\$	32,479
2021		33,170
2022		33,653
2023		34,629
2024		36,958
2025–2029		172,894

10. Long-Term Liabilities

Long-term liabilities consist of the following:

	September 30	
	2019	2018
	<i>(As Adjusted)</i>	
	<i>(In Thousands)</i>	
Defined benefit pension plan unfunded liability	\$ 52,941	\$ 4,646
Workers' compensation	45,595	42,266
Deferred income	27,890	26,256
Provider tax payable	9,510	15,180
Swap payable	4,788	–
Other	9,236	8,284
	\$ 149,960	\$ 96,632

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

11. Commitments and Contingencies

Leases

Sharp leases various equipment and facilities under operating leases expiring at various dates through 2037. Total rental expense in 2019 and 2018 for all operating leases was \$33,774,000 and \$33,067,000, respectively.

The following is a schedule by year of future minimum lease payments under operating leases as of September 30, 2019, that have initial or remaining lease terms in excess of one year (in thousands):

2020	\$ 25,060
2021	22,770
2022	21,611
2023	20,391
2024	18,696
Thereafter	160,179
	<u>\$ 268,707</u>

Commitments

Effective October 1, 2018, Sharp entered into a strategic information technology agreement to purchase a suite of software subscriptions, support, and services. The agreement is effective through 2026 and Sharp will make quarterly payments over the term of the agreement. The original commitment totaled \$145,064,000, with 2019 purchases totaling \$15,839,000. As of September 30, 2019, the remaining contracted commitment expected to be paid as follows (in thousands):

2020	\$ 17,785
2021	18,180
2022	19,306
2023	19,018
2024	18,678
Thereafter	36,706
	<u>\$ 129,673</u>

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

11. Commitments and Contingencies (continued)

Legal Matters

The health care industry is subject to numerous complex federal, state and local laws and regulations. These laws and regulations are subject to ongoing government review, interpretations and regulatory actions, and include matters such as licensure, accreditation, controlled substances, privacy, government program participation, government reimbursement for patient services, antitrust, anti-kickback, prohibited referrals by physicians, false claims, and, in the case of tax exempt organizations, the requirements for tax exemption. Compliance with these laws and regulations is required for participation in government health care programs. Government continues to increase the activities with respect to investigations and allegations concerning possible violations of laws and regulations by health care providers, some of which could result in the imposition of significant civil and/or criminal fines and/or penalties, repayment of previously billed and collected revenues for patient services, and exclusion from Medicare, Medi-Cal or other government programs.

In addition to the regulatory matters described above, in the normal course of business, Sharp is involved in legal proceedings. Management assesses the probable outcome of unresolved litigation or investigations, and accrues a contingent liability for such matters when it is probable that a liability has been incurred and the amount can be reasonably estimated. The accrual for a loss contingency might include, for example, estimates of potential damages, interest penalties, and other directly related costs expected to be incurred. As of September 30, 2019 and 2018, there were no material losses recorded for probable legal liabilities.

In January 2017, a class action complaint was filed in the Superior Court of California for the County of San Diego against Sharp HealthCare and Sharp Grossmont Hospital, seeking damages associated with alleged privacy violations in connection with video recordings conducted in operating rooms at Sharp Grossmont Hospital's Women's Center as part of an investigation into missing drugs and equipment. In March 2018, the Superior Court determined not to grant class certification for the action, although the issue remains outstanding. Since then, a number of individual lawsuits on behalf of approximately 450 women have been filed that mirror the allegations in the original class action lawsuit. While the timing and outcome of these cases remains uncertain, and Sharp HealthCare and Sharp Grossmont Hospital continue the vigorous defense of these actions, there can be no assurance that the final resolution of these matters against Sharp HealthCare and Sharp Grossmont Hospital will not have a material effect on the consolidated financial statements of Sharp Healthcare.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

11. Commitments and Contingencies (continued)

Labor Matters

Not-for-profit health care providers and their employees are under the jurisdiction of the National Labor Relations Board. As of September 30, 2019, approximately 26% of Sharp employees are represented by unions. Such unionized employees are represented by the Sharp Professional Nurses Network/United Nurses Association of California. The collective bargaining agreement with the union expires in 2021.

Professional Liability

CQI SPC is a wholly owned captive insurance company that insures a portion of the medical malpractice (professional liability) claims of certain affiliates of Sharp. Malpractice losses are accrued based on estimates of the ultimate costs for both reported claims and claims incurred but not reported. Sharp's liability is limited to \$3,000,000 per individual claim. As of September 30, 2019 and 2018, Sharp's liability was limited in the aggregate each year to \$16,000,000. Sharp has obtained excess loss insurance covering claims above these amounts up to \$40,000,000.

Professional and general liability costs have been accrued based upon an actuarial determination. Accrued malpractice losses have been discounted at 3.0% at September 30, 2019 and 2018. The current portion of professional liability costs is included in accounts payable and accrued liabilities on the consolidated balance sheets.

Included on the consolidated balance sheets are the following amounts related to professional and general liability:

	September 30	
	2019	2018
	<i>(In Thousands)</i>	
Reserves for professional and general liabilities	\$ 9,649	\$ 12,729
Accounts payable and accrued liabilities	11,745	10,827
	\$ 21,394	\$ 23,556

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

11. Commitments and Contingencies (continued)

Claims, including alleged malpractice, have been asserted against Sharp and are currently in various stages of litigation. Additional claims may be asserted against Sharp arising from services provided to patients through September 30, 2019. In management's opinion, however, the estimated liability accrued at September 30, 2019, is adequate to provide for potential losses resulting from pending or threatened litigation. It is management's opinion that the ultimate disposition of such litigation will not have a material adverse effect on the consolidated financial position, results of operations, or cash flows of Sharp.

Sharp Health Plan

SHP is required to meet certain financial responsibility regulations of the California Department of Managed Healthcare (DMHC). Pursuant to these regulations, SHP maintains a reserve totaling \$500,000 on deposit with various financial institutions. In addition, SHP is required to maintain two times the normal requirement of tangible net equity, as defined in regulations of the DMHC. At September 30, 2019 and 2018, SHP was required to maintain tangible net equity totaling \$23,870,000 and \$17,863,000, respectively. SHP's tangible net equity was \$110,882,000 and \$87,334,000 at September 30, 2019 and 2018, respectively. Management believes it is in compliance with these requirements at September 30, 2019 and 2018.

Unemployment Claims and Workers' Compensation

Sharp has elected to self-insure for unemployment claims through various group plans. Prior to January 1, 1996, Sharp was also self-insured for workers' compensation claims. Since 1996, Sharp has purchased high-deductible insurance policies and has been responsible for workers' compensation claims up to amounts covered by these insurance policies (Sharp was responsible for individual claims up to \$1,000,000 in 2019 and 2018). For workers' compensation, Sharp accrues for the unpaid portion of claims that have been reported and estimates of claims that have been incurred but not reported, based on an actuarial study. Accrued workers' compensation have been discounted at 2.40% and 2.90% at September 30, 2019 and 2018, respectively. Workers' compensation liabilities of \$59,768,000 and \$54,911,000 at September 30, 2019 and 2018, respectively, are included in other current liabilities and long-term liabilities on the consolidated balance sheets.

Sharp HealthCare

Notes to Consolidated Financial Statements (continued)

12. Subsequent Events

In preparing these consolidated financial statements, management has evaluated and disclosed all material subsequent events up to December 19, 2019, which is the date that the accompanying consolidated financial statements were issued.

Supplementary Information

Sharp HealthCare

Consolidating Balance Sheet
(In Thousands)

September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Sharp Coronado Hospital and HealthCare Center	Sharp Health Plan	Continuous Quality Insurance	Sharp HealthCare Foundation	Grossmont Hospital Foundation	Combined Totals	Eliminations	Totals
Assets												
Current assets:												
Cash and cash equivalents	\$ 255,340	\$ 907	\$ 582	\$ 41,846	\$ 106	\$ 61,371	\$ 3,918	\$ 1,822	\$ 9,095	\$ 374,987	\$ -	\$ 374,987
Short-term investments	25,712	-	-	7,318	-	3,057	-	-	-	36,087	-	36,087
Accounts receivable, net	40,470	173,160	73,975	134,299	13,887	28,782	-	2,831	1,245	468,649	(24,665)	443,984
Intercompany receivables	-	2,524,128	136,914	-	39,830	-	-	-	44	2,700,916	(2,700,916)	-
Inventories	9,170	18,211	7,805	12,548	3,048	-	-	-	-	50,782	-	50,782
Prepaid expenses and other	40,288	5,031	3,155	4,318	577	1,191	5	42	777	55,384	-	55,384
Total current assets	370,980	2,721,437	222,431	200,329	57,448	94,401	3,923	4,695	11,161	3,686,805	(2,725,581)	961,224
Long-term investments	257,091	-	-	15,950	-	77,378	-	-	-	350,419	-	350,419
Assets limited as to use:												
Designated for property	2,053,258	-	-	461,821	-	-	-	-	-	2,515,079	-	2,515,079
Under bond indentures	42	1,173	40,650	1,356	-	-	-	-	-	43,221	-	43,221
Other restricted investments	-	-	-	-	-	552	-	51,894	15,386	67,832	-	67,832
Under self-insurance programs	-	-	-	-	-	-	11,256	-	-	11,256	-	11,256
Total assets limited as to use	2,053,300	1,173	40,650	463,177	-	552	11,256	51,894	15,386	2,637,388	-	2,637,388
Property and equipment, net	380,214	377,714	330,171	420,351	34,021	540	-	179	-	1,543,190	-	1,543,190
Other assets	56,324	19,941	20,278	31,113	12,811	234	27,521	44,012	9,846	222,080	(65,862)	156,218
Beneficial interest in foundations	77,492	-	-	35,582	-	-	-	-	-	113,074	(113,074)	-
Total assets	\$ 3,195,401	\$ 3,120,265	\$ 613,530	\$ 1,166,502	\$ 104,280	\$ 173,105	\$ 42,700	\$ 100,780	\$ 36,393	\$ 8,552,956	\$ (2,904,517)	\$ 5,648,439
Liabilities and net assets												
Current liabilities:												
Accounts payable and accrued liabilities	\$ 174,103	\$ 41,633	\$ 34,225	\$ 32,311	\$ 4,361	\$ 56,832	\$ 13,075	\$ 342	\$ 8	\$ 356,890	\$ (24,330)	\$ 332,560
Intercompany payable	2,690,731	-	-	8,212	-	1,275	103	565	-	2,700,886	(2,700,886)	-
Accrued compensation and benefits	54,764	47,407	19,325	32,724	5,246	3,488	-	587	148	163,689	3	163,692
Current portion of long-term debt	3,819	7,210	2,535	4,394	-	-	-	-	-	17,958	-	17,958
Estimated settlements payable to government programs, net	-	688	727	1,276	45	-	-	-	-	2,736	-	2,736
Accrued interest	266	1,876	1,054	512	-	-	-	-	-	3,708	-	3,708
Total current liabilities	2,923,683	98,814	57,866	79,429	9,652	61,595	13,178	1,494	156	3,245,867	(2,725,213)	520,654
Long-term liabilities	113,854	23,111	8,270	20,304	1,756	628	23,196	21,796	656	213,571	(63,611)	149,960
Reserves for professional and general liabilities	6,000	-	-	-	-	-	3,649	-	-	9,649	-	9,649
Long-term debt	61,300	321,186	271,567	75,901	-	-	-	-	-	729,954	-	729,954
Total liabilities	3,104,837	443,111	337,703	175,634	11,408	62,223	40,023	23,290	812	4,199,041	(2,788,824)	1,410,217
Net assets:												
Without donor restrictions	25,473	2,677,154	275,827	965,386	98,021	110,882	2,677	12,400	10,099	4,177,919	(25,120)	4,152,799
With donor restrictions	65,091	-	-	25,482	(5,149)	-	-	65,090	25,482	175,996	(90,573)	85,423
Total net assets	90,564	2,677,154	275,827	990,868	92,872	110,882	2,677	77,490	35,581	4,353,915	(115,693)	4,238,222
Total liabilities and net assets	\$ 3,195,401	\$ 3,120,265	\$ 613,530	\$ 1,166,502	\$ 104,280	\$ 173,105	\$ 42,700	\$ 100,780	\$ 36,393	\$ 8,552,956	\$ (2,904,517)	\$ 5,648,439

Sharp HealthCare

Consolidating Statement of Operations
(In Thousands)

Year Ended September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Sharp Coronado Hospital and HealthCare Center	Sharp Health Plan	Continuous Quality Insurance	Sharp HealthCare Foundation	Grossmont Hospital Foundation	Combined Totals	Eliminations	Totals
Revenues:												
Patient service	\$ 196,612	\$ 1,190,936	\$ 360,567	\$ 652,423	\$ 93,063	\$ –	\$ –	\$ –	\$ –	\$ 2,493,601	\$ (427,400)	\$ 2,066,201
Provider tax	–	71,505	39,122	69,925	9,289	–	–	–	–	189,841	–	189,841
Net patient service	196,612	1,262,441	399,689	722,348	102,352	–	–	–	–	2,683,442	(427,400)	2,256,042
Premium	1,075,801	–	–	–	–	786,117	–	–	–	1,861,918	(383,780)	1,478,138
Other	328,416	10,941	6,958	37,932	3,653	44	7,730	–	–	395,674	(284,259)	111,415
Total revenues	1,600,829	1,273,382	406,647	760,280	106,005	786,161	7,730	–	–	4,941,034	(1,095,439)	3,845,595
Expenses:												
Salaries and wages	409,161	447,756	172,504	316,390	47,691	21,416	–	–	–	1,414,918	–	1,414,918
Employee benefits	110,392	109,041	42,399	75,078	11,458	4,613	–	–	–	352,981	–	352,981
Medical fees	326,555	18,011	10,741	13,490	1,639	685,997	–	–	–	1,056,433	(424,154)	632,279
Purchased services	210,133	75,381	33,286	51,106	9,203	27,300	156	–	–	406,565	(21,362)	385,203
Supplies	91,174	181,451	63,755	107,382	15,552	271	–	–	–	459,585	–	459,585
Provider tax	–	39,378	20,954	38,388	2,089	–	–	–	–	100,809	–	100,809
Maintenance, utilities, and rentals	74,980	30,472	9,108	20,827	4,590	1,452	–	–	–	141,429	(6,433)	134,996
Depreciation and amortization	35,663	45,680	13,936	37,974	4,823	566	5	–	–	138,647	(13,841)	124,806
Business insurance	4,941	4,010	1,446	2,526	379	226	8,137	–	–	21,665	(8,146)	13,519
Interest	3,098	12,439	1,571	3,302	(17)	5	–	–	–	20,398	(832)	19,566
Purchased services from affiliate	406,171	131,280	48,830	85,663	11,544	5,971	100	–	–	689,559	(689,559)	–
Other	16,019	8,552	2,299	4,353	1,008	18,335	10	–	–	50,576	–	50,576
Total expenses	1,688,287	1,103,451	420,829	756,479	109,959	766,152	8,408	–	–	4,853,565	(1,164,327)	3,689,238
Income (loss) from operations	(87,458)	169,931	(14,182)	3,801	(3,954)	20,009	(678)	–	–	87,469	68,888	156,357
Other nonoperating income (loss)	(14,702)	2,109	856	151	217	51	–	(586)	553	(11,351)	9,729	(1,622)
Investment income	100,977	57,580	20,414	20,527	4,433	4,058	692	1,230	526	210,437	(78,617)	131,820
Excess (deficit) of revenues over expenses	(1,183)	229,620	7,088	24,479	696	24,118	14	644	1,079	286,555	–	286,555
Net assets transferred from related party	–	–	–	3,727	–	–	–	–	–	3,727	–	3,727
Net assets released from restrictions used for purchase of property and equipment	68	1,762	2,760	124	–	–	–	–	–	4,714	–	4,714
Pension related changes other than net periodic pension cost	(18,447)	(20,854)	(6,937)	(13,719)	(1,727)	(557)	–	–	–	(62,241)	–	(62,241)
Other changes in net assets without donor restrictions	641	–	–	1,194	3,034	–	–	–	–	4,869	(1,724)	3,145
Increase (decrease) in net assets without donor restrictions	\$ (18,921)	\$ 210,528	\$ 2,911	\$ 15,805	\$ 2,003	\$ 23,561	\$ 14	\$ 644	\$ 1,079	\$ 237,624	\$ (1,724)	\$ 235,900

Sharp HealthCare

Consolidating Statement of Changes in Net Assets
(In Thousands)

Year Ended September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Sharp Coronado Hospital and HealthCare Center	Sharp Health Plan	Continuous Quality Insurance	Sharp HealthCare Foundation	Grossmont Hospital Foundation	Combined Totals	Eliminations	Totals
Net assets without donor restrictions:												
Excess of revenues over expenses	\$ (1,183)	\$ 229,620	\$ 7,088	\$ 24,479	\$ 696	\$ 24,118	\$ 14	\$ 644	\$ 1,079	\$ 286,555	\$ -	\$ 286,555
Net assets transferred from related party	-	-	-	3,727	-	-	-	-	-	3,727	-	3,727
Net assets released from restrictions used for purchase of property and equipment	68	1,762	2,760	124	-	-	-	-	-	4,714	-	4,714
Pension related changes other than net periodic pension cost	(18,447)	(20,854)	(6,937)	(13,719)	(1,727)	(557)	-	-	-	(62,241)	-	(62,241)
Other changes in net assets without donor restrictions	641	-	-	1,194	3,034	-	-	-	-	4,869	(1,724)	3,145
Increase (decrease) in net assets without donor restrictions	(18,921)	210,528	2,911	15,805	2,003	23,561	14	644	1,079	237,624	(1,724)	235,900
Net assets with donor restrictions:												
Contributions	-	-	-	-	-	-	-	10,924	8,075	18,999	-	18,999
Investment income	-	-	-	-	-	-	-	556	79	635	-	635
Change in net unrealized gains on investments	-	-	-	-	-	-	-	170	16	186	-	186
Net assets released from restrictions	-	-	-	-	-	-	-	(9,452)	(3,646)	(13,098)	-	(13,098)
Other changes in net assets with donor restrictions	2,198	-	-	4,524	2,680	-	-	-	-	9,402	(6,722)	2,680
Increase in net assets with donor restrictions	2,198	-	-	4,524	2,680	-	-	2,198	4,524	16,124	(6,722)	9,402
Increase (decrease) in net assets	(16,723)	210,528	2,911	20,329	4,683	23,561	14	2,842	5,603	253,748	(8,446)	245,302
Net assets, beginning of the year	107,287	2,466,626	272,916	970,539	88,189	87,321	2,663	74,648	29,978	4,100,167	(107,247)	3,992,920
Net assets, end of the year	\$ 90,564	\$ 2,677,154	\$ 275,827	\$ 990,868	\$ 92,872	\$ 110,882	\$ 2,677	\$ 77,490	\$ 35,581	\$ 4,353,915	\$ (115,693)	\$ 4,238,222

Sharp HealthCare

Consolidating Balance Sheet – Obligated Group (In Thousands)

September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Combined Totals	Eliminations	Totals
Assets							
Current assets:							
Cash and cash equivalents	\$ 255,340	\$ 907	\$ 582	\$ 41,846	\$ 298,675	\$ –	\$ 298,675
Short-term investments	25,712	–	–	7,318	33,030	–	33,030
Accounts receivable, net	40,470	173,160	73,975	134,299	421,904	(2,120)	419,784
Intercompany receivables	–	2,524,128	136,914	–	2,661,042	(2,660,410)	632
Inventories	9,170	18,211	7,805	12,548	47,734	–	47,734
Prepaid expenses and other	40,288	5,031	3,155	4,318	52,792	–	52,792
Total current assets	370,980	2,721,437	222,431	200,329	3,515,177	(2,662,530)	852,647
Long-term investments	257,091	–	–	15,950	273,041	–	273,041
Assets limited as to use:							
Designated for property	2,053,258	–	–	461,821	2,515,079	–	2,515,079
Under bond indentures	42	1,173	40,650	1,356	43,221	–	43,221
Other restricted investments	–	–	–	–	–	–	–
Under self-insurance programs	–	–	–	–	–	–	–
Total assets limited as to use	2,053,300	1,173	40,650	463,177	2,558,300	–	2,558,300
Property and equipment, net	380,214	377,714	330,171	420,351	1,508,450	–	1,508,450
Other assets	56,324	19,941	20,278	31,113	127,656	(132)	127,524
Beneficial interest in foundations	77,492	–	–	35,582	113,074	–	113,074
Total assets	\$ 3,195,401	\$ 3,120,265	\$ 613,530	\$ 1,166,502	\$ 8,095,698	\$ (2,662,662)	\$ 5,433,036

Sharp HealthCare

Consolidating Balance Sheet – Obligated Group (continued) (In Thousands)

September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Combined Totals	Eliminations	Totals
Liabilities and net assets							
Current liabilities:							
Accounts payable and accrued liabilities	\$ 174,629	\$ 41,633	\$ 34,225	\$ 32,311	\$ 282,798	\$ (2,120)	\$ 280,678
Intercompany payable	2,690,205	–	–	8,212	2,698,417	(2,660,410)	38,007
Accrued compensation and benefits	54,764	47,407	19,325	32,724	154,220	–	154,220
Current portion of long-term debt	3,819	7,210	2,535	4,394	17,958	–	17,958
Estimated settlements payable to government programs, net	–	688	727	1,276	2,691	–	2,691
Accrued interest	266	1,876	1,054	512	3,708	–	3,708
Total current liabilities	2,923,683	98,814	57,866	79,429	3,159,792	(2,662,530)	497,262
Long-term liabilities	113,854	23,111	8,270	20,304	165,539	(132)	165,407
Reserves for professional and general liabilities	6,000	–	–	–	6,000	–	6,000
Long-term debt	61,300	321,186	271,567	75,901	729,954	–	729,954
Total liabilities	3,104,837	443,111	337,703	175,634	4,061,285	(2,662,662)	1,398,623
Net assets:							
Without donor restrictions	25,473	2,677,154	275,827	965,386	3,943,840	–	3,943,840
With donor restrictions	65,091	–	–	25,482	90,573	–	90,573
Total net assets	90,564	2,677,154	275,827	990,868	4,034,413	–	4,034,413
Total liabilities and net assets	\$ 3,195,401	\$ 3,120,265	\$ 613,530	\$ 1,166,502	\$ 8,095,698	\$ (2,662,662)	\$ 5,433,036

Sharp HealthCare

Consolidating Statement of Operations – Obligated Group (In Thousands)

Year Ended September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Combined Totals	Eliminations	Totals
Revenues:							
Patient service	\$ 196,612	\$ 1,190,936	\$ 360,567	\$ 652,423	\$ 2,400,538	\$ (396,148)	\$ 2,004,390
Provider tax	–	71,505	39,122	69,925	180,552	–	180,552
Net patient service	196,612	1,262,441	399,689	722,348	2,581,090	(396,148)	2,184,942
Premium	1,075,801	–	–	–	1,075,801	–	1,075,801
Other	328,416	10,941	6,958	37,932	384,247	(248,835)	135,412
Total revenues	1,600,829	1,273,382	406,647	760,280	4,041,138	(644,983)	3,396,155
Expenses:							
Salaries and wages	409,161	447,756	172,504	316,390	1,345,811	–	1,345,811
Employee benefits	110,392	109,041	42,399	75,078	336,910	–	336,910
Medical fees	326,555	18,011	10,741	13,490	368,797	(24,743)	344,054
Purchased services	210,133	75,381	33,286	51,106	369,906	(18,337)	351,569
Supplies	91,174	181,451	63,755	107,382	443,762	–	443,762
Provider tax	–	39,378	20,954	38,388	98,720	–	98,720
Maintenance, utilities, and rentals	74,980	30,472	9,108	20,827	135,387	(5,260)	130,127
Depreciation and amortization	35,663	45,680	13,936	37,974	133,253	(12,773)	120,480
Business insurance	4,941	4,010	1,446	2,526	12,923	–	12,923
Interest	3,098	12,439	1,571	3,302	20,410	(810)	19,600
Purchased services from affiliate	406,171	131,280	48,830	85,663	671,944	(658,139)	13,805
Other	16,019	8,552	2,299	4,353	31,223	–	31,223
Total expenses	1,688,287	1,103,451	420,829	756,479	3,969,046	(720,062)	3,248,984
Income (loss) from operations	(87,458)	169,931	(14,182)	3,801	72,092	75,079	147,171

(Continued on next page)

Sharp HealthCare

Consolidating Statement of Operations – Obligated Group (continued) (In Thousands)

Year Ended September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Combined Totals	Eliminations	Totals
Income (loss) from operations <i>(from previous page)</i>	\$ (87,458)	\$ 169,931	\$ (14,182)	\$ 3,801	\$ 72,092	\$ 75,079	\$ 147,171
Other nonoperating income (loss)	(14,702)	2,109	856	151	(11,586)	(897)	(12,483)
Investment income	100,977	57,580	20,414	20,527	199,498	(74,182)	125,316
Excess (deficit) of revenues over expenses	(1,183)	229,620	7,088	24,479	260,004	–	260,004
Net assets transferred from related party	–	–	–	3,727	3,727	–	3,727
Net assets released from restrictions used for purchase of property and equipment	68	1,762	2,760	124	4,714	–	4,714
Pension-related changes other than net periodic pension cost	(18,447)	(20,854)	(6,937)	(13,719)	(59,957)	–	(59,957)
Other changes in net assets without donor restriction	641	–	–	1,194	1,835	–	1,835
Increase (decrease) in net assets without donor restrictions	\$ (18,921)	\$ 210,528	\$ 2,911	\$ 15,805	\$ 210,323	\$ –	\$ 210,323

Sharp HealthCare

Consolidating Statement of Changes in Net Assets – Obligated Group (In Thousands)

Year Ended September 30, 2019

	Sharp HealthCare	Sharp Memorial Hospital	Sharp Chula Vista Medical Center	Sharp Grossmont Hospital	Combined Totals	Eliminations	Totals
Net assets without donor restrictions:							
Excess (deficit) of revenues over expenses	\$ (1,183)	\$ 229,620	\$ 7,088	\$ 24,479	\$ 260,004	\$ –	\$ 260,004
Net assets transferred from related party	–	–	–	3,727	3,727	–	3,727
Net assets released from restrictions used for purchase of property and equipment	68	1,762	2,760	124	4,714	–	4,714
Pension-related changes other than net periodic pension cost	(18,447)	(20,854)	(6,937)	(13,719)	(59,957)	–	(59,957)
Other changes in net assets without donor restrictions	641	–	–	1,194	1,835	–	1,835
Increase (decrease) in net assets without donor restrictions	(18,921)	210,528	2,911	15,805	210,323	–	210,323
Net assets with donor restrictions:							
Contributions	–	–	–	–	–	–	–
Investment income	–	–	–	–	–	–	–
Change in net unrealized gains on investments	–	–	–	–	–	–	–
Net assets released from restriction	–	–	–	–	–	–	–
Other changes in net assets with donor restrictions	2,198	–	–	4,524	6,722	–	6,722
Increase in net assets with donor restrictions	2,198	–	–	4,524	6,722	–	6,722
Increase (decrease) in net assets	(16,723)	210,528	2,911	20,329	217,045	–	217,045
Net assets, beginning of the year	107,287	2,466,626	272,916	970,539	3,817,368	–	3,817,368
Net assets, end of the year	\$ 90,564	\$ 2,677,154	\$ 275,827	\$ 990,868	\$ 4,034,413	\$ –	\$ 4,034,413

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