



**Baylor Scott & White**  
HEALTH

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**Baylor Scott & White Holdings  
and Its Controlled Affiliates**

**Combined Financial Statements and  
Supplemental Information**

**For the Years Ended June 30, 2020 and 2019**



**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

*Combined Financial Statements and Supplemental Information  
For the Years Ended June 30, 2020 and 2019*

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Combined Financial Statements and Supplemental Information

For the Years Ended June 30, 2020 and 2019

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## **Report of Independent Auditors**

To the Board of Trustees of Baylor Scott & White Holdings

We have audited the accompanying combined financial statements of Baylor Scott & White Holdings and its controlled affiliates which comprise the combined balance sheets as of June 30, 2020 and 2019, and the related combined statements of operations and changes in net assets and of cash flows for the years then ended.

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

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

### ***Auditors' Responsibility***

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the combined 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 Company'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 combined 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 combined financial statements referred to above present fairly, in all material respects, the financial position of Baylor Scott & White Holdings and its controlled affiliates as of June 30, 2020 and 2019, and the results of their operations, their changes in net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



***Emphasis of Matter***

As discussed in Note 2 to the combined financial statements, the Company changed the manner in which it accounts for leases as of July 1, 2019. Our opinion is not modified with respect to this matter.

***Other Matter***

Our audit was conducted for the purpose of forming an opinion on the combined financial statements taken as a whole. The other community benefits information is presented for purposes of additional analysis and is not a required part of the combined financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the combined financial statements and accordingly, we do not express an opinion or provide any assurance on it.

*PricewaterhouseCoopers LLP*

Dallas, Texas  
October 30, 2020

**BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

COMBINED BALANCE SHEETS - JUNE 30, 2020 and 2019

(In millions)

<b>ASSETS</b>	<u>2020</u>	<u>2019</u>	<b>LIABILITIES AND NET ASSETS</b>	<u>2020</u>	<u>2019</u>
<b>CURRENT ASSETS:</b>			<b>CURRENT LIABILITIES:</b>		
Cash and cash equivalents	\$ 1,965	\$ 813	Current maturities of long-term debt and finance lease obligations	\$ 102	\$ 142
Short-term investments	356	337	Long-term debt subject to short-term remarketing arrangements	95	95
THVG funds due from United Surgical Partners, Inc.	280	104	Commercial paper	208	208
Accounts receivable:			Trade accounts payable	344	349
Patient	781	845	Accrued liabilities:		
Premiums	118	111	Payroll related	522	454
Other	273	228	Third-party programs	848	104
Other current assets	<u>376</u>	<u>355</u>	Medical claims payable	65	73
			Operating lease liabilities	155	—
			Other	<u>615</u>	<u>479</u>
			Total current liabilities	<u>2,954</u>	<u>1,904</u>
Total current assets	<u>4,149</u>	<u>2,793</u>			
<b>LONG-TERM INVESTMENTS:</b>			<b>LONG-TERM DEBT AND FINANCE LEASE OBLIGATIONS, less</b>		
Unrestricted	4,094	4,201	current maturities	3,262	3,022
Restricted	<u>497</u>	<u>518</u>			
Total long-term investments	<u>4,591</u>	<u>4,719</u>	<b>OTHER LONG-TERM LIABILITIES:</b>		
			Self insurance and other insurance liabilities	119	114
<b>ASSETS WHOSE USE IS LIMITED:</b>			Interest rate swap liabilities, net	365	274
Other designated assets	175	151	Long-term operating lease liabilities	807	—
Self insurance reserves	<u>120</u>	<u>116</u>	Other	<u>257</u>	<u>336</u>
Total assets whose use is limited	<u>295</u>	<u>267</u>	Total other long-term liabilities	<u>1,548</u>	<u>724</u>
			Total liabilities	<u>7,764</u>	<u>5,650</u>
PROPERTY AND EQUIPMENT, net	4,062	3,890	<b>COMMITMENTS AND CONTINGENCIES</b>		
RIGHT OF USE OPERATING LEASE ASSETS, net	868	—			
CONTRIBUTIONS RECEIVABLE, net	169	203	<b>NONCONTROLLING INTERESTS – REDEEMABLE</b>	482	453
<b>OTHER LONG-TERM ASSETS:</b>			<b>NET ASSETS:</b>		
Equity investment in unconsolidated entities	63	64	Net assets without donor restrictions:		
Goodwill and intangible assets, net	873	878	Attributable to BSWH	5,840	5,727
Interest in net assets of related foundation	4	4	Noncontrolling interests-nonredeemable	326	278
Other	<u>18</u>	<u>17</u>	Total net assets without donor restrictions	<u>6,166</u>	<u>6,005</u>
Total other long-term assets	<u>958</u>	<u>963</u>	Net assets with donor restrictions	<u>680</u>	<u>727</u>
Total assets	<u>\$ 15,092</u>	<u>\$ 12,835</u>	Total net assets	<u>6,846</u>	<u>6,732</u>
			Total liabilities and net assets	<u>\$ 15,092</u>	<u>\$ 12,835</u>

The accompanying notes are an integral part of these financial statements.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

COMBINED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS

FOR THE YEARS ENDED JUNE 30, 2020 AND 2019

(In millions)

	2020	2019
OPERATING REVENUE:		
Net patient care revenue	\$ 8,334	\$ 8,447
Premium revenue	1,483	1,153
Other operating revenue	635	386
Net assets released from restrictions for operations	77	67
Total operating revenue	10,529	10,053
OPERATING EXPENSES:		
Salaries, wages, and employee benefits	4,923	4,561
Supplies	1,701	1,661
Other operating expenses	2,069	2,006
Medical claims	735	556
(Gains) losses on fixed asset sales and disposals, net	(1)	4
Depreciation and amortization	429	415
Interest	114	125
Total operating expenses	9,970	9,328
INCOME FROM OPERATIONS	559	725
NONOPERATING (LOSSES) GAINS:		
Gains on investments, net	58	224
Interest rate swap activity	(151)	(88)
Equity in earnings of unconsolidated entities	—	3
Loss from extinguishment of debt	(3)	—
Total nonoperating (losses) gains	(96)	139
REVENUE AND GAINS IN EXCESS OF EXPENSES AND LOSSES BEFORE TAXES	463	864
LESS INCOME TAX EXPENSE	10	15
REVENUE AND GAINS IN EXCESS OF EXPENSES AND LOSSES	453	849

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

COMBINED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS - continued

FOR THE YEARS ENDED JUNE 30, 2020 AND 2019

(In millions)

	2020	2019
OTHER CHANGES IN NET ASSETS WITHOUT DONOR RESTRICTIONS:		
Net assets released from restrictions for capital expenditures	\$ 45	\$ 31
Other changes in net assets attributable to noncontrolling interests - nonredeemable	(45)	(92)
Revenue and gains in excess of expenses and losses attributable to non controlling interests - redeemable	(290)	(274)
Net assets acquired	—	7
Cumulative change in accounting principle	(2)	—
Other	—	(10)
 INCREASE IN NET ASSETS WITHOUT DONOR RESTRICTIONS	 161	 511
 CHANGES IN NET ASSETS WITH DONOR RESTRICTIONS:		
Contributions	56	98
Realized gains on investments, net	20	28
Unrealized losses on investments, net	(9)	(1)
Change in value of split-interest agreements	4	2
Net assets released from restrictions for operations	(77)	(67)
Net assets released from restrictions for capital expenditures	(45)	(31)
Other	4	(2)
 (DECREASE) INCREASE IN NET ASSETS WITH DONOR RESTRICTIONS	 (47)	 27
 INCREASE IN NET ASSETS	 114	 538
 NET ASSETS, beginning of year	 6,732	 6,194
 NET ASSETS, end of year	 \$ 6,846	 \$ 6,732

The accompanying notes are an integral part of these financial statements.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

COMBINED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED JUNE 30, 2020 AND 2019

(In millions)

	2020	2019
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Increase in net assets	\$ 114	\$ 538
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Loss from extinguishment of debt	1	—
Unrealized losses (gains) on investments, net	67	(69)
Realized gains on investments, net	(54)	(100)
Unrealized losses on interest rate swap, net	129	70
Contributions restricted for long-term purposes	(1)	(15)
Depreciation and amortization	429	415
(Gains) losses on fixed asset sales and disposals, net	(1)	4
Equity in earnings of unconsolidated entities	—	(3)
Change in value of split-interest agreements	(4)	(2)
Deferred rent and other	9	(2)
Other changes attributable to noncontrolling interests	328	360
Cumulative change in accounting principle	2	—
Net assets acquired	—	(7)
Changes in operating assets and liabilities (net of acquisitions):		
Decrease (increase) in patient accounts receivable	64	(40)
Increase in other accounts receivable	(52)	(19)
Increase in other assets	(13)	(23)
Increase in trade accounts payable and accrued liabilities	949	4
Increase in other long-term liabilities	32	57
Net cash provided by operating activities	1,999	1,168
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(597)	(590)
Cash proceeds from sales of assets	4	6
Cash paid for acquisitions, net of cash received	—	(31)
(Increase) decrease in THVG funds due from United Surgical Partners, Inc.	(176)	14
Decrease (increase) in trading investments	101	(656)
Net payments on interest rate swaps	(60)	(34)
Purchases of other than trading investments	—	(19)
Sales of other than trading investments	—	19
Increase in assets whose use is limited	(28)	(16)
Net cash used in investing activities	(756)	(1,307)

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

COMBINED STATEMENTS OF CASH FLOWS - continued

FOR THE YEARS ENDED JUNE 30, 2020 AND 2019

(In millions)

	2020	2019
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Principal payments on long-term debt	\$ (855)	\$ (178)
Proceeds from issuance of long-term debt	1,067	140
Distributions to noncontrolling interests	(283)	(320)
Purchases of noncontrolling interests	(24)	(24)
Sales of noncontrolling interests	8	9
Cash receipts restricted for long-term purposes	1	3
Annuity payments to beneficiaries	(1)	(1)
Net cash used in financing activities	(87)	(371)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS AND RESTRICTED CASH</b>	<b>1,156</b>	<b>(510)</b>
<b>CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, beginning of year</b>	<b>819</b>	<b>1,329</b>
<b>CASH AND CASH EQUIVALENTS AND RESTRICTED CASH, end of year</b>	<b>\$ 1,975</b>	<b>\$ 819</b>
<b>SUPPLEMENTAL CASH FLOW DATA:</b>		
Cash paid for interest	\$ 115	\$ 125
Cash paid for income tax	\$ —	\$ 16
Property and equipment acquired under finance leases	\$ 3	\$ 3
Right of use assets acquired under operating leases	\$ 80	\$ —
Decrease in accounts payable due to property and equipment received but not paid	\$ (13)	\$ (13)
Decrease in contributions receivable for property and equipment	\$ 29	\$ 14
<b>RECONCILIATION OF CASH AND CASH EQUIVALENTS AND RESTRICTED CASH:</b>		
Cash and cash equivalents at beginning of year	\$ 813	\$ 1,264
Cash in unrestricted long-term investments at beginning of year	1	3
Cash in restricted long-term investments at beginning of year	4	8
Cash in assets whose use is limited at beginning of year	1	54
Cash and cash equivalents and restricted cash at beginning of year	\$ 819	\$ 1,329
Cash and cash equivalents at end of year	\$ 1,965	\$ 813
Cash in unrestricted long-term investments at end of year	1	1
Cash in restricted long-term investments at end of year	8	4
Cash in assets whose use is limited at end of year	1	1
Cash and cash equivalents and restricted cash at end of year	\$ 1,975	\$ 819

The accompanying notes are an integral part of these financial statements.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements

For the Years Ended June 30, 2020 and 2019

## **1. ORGANIZATION**

Baylor Scott & White Holdings (BSW Holdings), a Texas nonprofit corporation exempt from federal income taxation under Section 501(c)(3) of the Internal Revenue Code, and its controlled affiliates (collectively, the “System”) were created from the combination of two Texas healthcare systems, Baylor Health Care System (BHCS) and its affiliates, and Scott & White Healthcare (SWH) and its affiliates. BSW Holdings and Baylor Scott & White Health (BSW Health), a Texas nonprofit corporation, were created by BHCS and SWH in connection with their combination. BSW Holdings is the sole member of BHCS, SWH, and BSW Health and has control and substantial reserved powers over all BHCS and SWH material affiliates. BSW Holdings and its controlled affiliates are collectively referred to as the “System” or “BSWH”.

The combined financial statements include the accounts of BSW Holdings, BSW Health, BHCS, SWH, Baylor University Medical Center (BUMC), Scott & White Memorial Hospital (SWMH), five health plan entities (collectively referred to as the “Health Plan” or “Consolidated Health Plan”), five foundations, twenty-six community and specialty hospitals located throughout the Dallas and Fort Worth metroplex and the central Texas area, one wholly owned captive insurance subsidiary (Baylor Scott & White Assurance SPC (BSWA)), Baylor Quality Health Care Alliance, LLC, an accountable care organization, five physician practice organizations including HealthTexas Provider Network (HTPN), Scott & White Clinic, Hillcrest Family Health Center, Hillcrest Physician Services, and Century Integrated Partners, Inc., and other related entities. Investments in certain related entities with 50.0% or less ownership are accounted for using the equity method. The transactions and balances for investments in certain related entities with greater than 50.0% ownership, or where the System exercises board control, are included in the accompanying combined financial statements with related noncontrolling interests reported in the combined financial statements. These entities include four acute and specialty hospitals referenced above, along with partnerships in: Texas Health Ventures Group, LLC (THVG), providing short-stay hospital and outpatient surgery services, BIR JV, LLP, providing rehabilitation services, BTDI JV, LLP, providing imaging services, EBD JV, LLP, providing emergency medical services, and HTPN Gastroenterology Services, LLP, providing endoscopic services. All significant intercompany accounts and transactions among entities included in the combined financial statements have been eliminated.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

The following summarizes significant changes in the System in 2020 and 2019:

## **THVG**

BUMC has a majority ownership of 50.1% in THVG with USP North Texas, Inc. (USP), a Texas corporation and subsidiary of United Surgical Partners, Inc. (USPI) holding the remaining 49.9%. THVG had net patient care revenue included in the System's combined financial statements of approximately \$1,204 million and \$1,216 million for the years ended June 30, 2020 and 2019, respectively.

## **BT Garland JV, LLP**

On December 14, 2017, BSWH announced that a decision was made to close Baylor Scott & White Medical Center – Garland, a 113-bed hospital. The last day of operations was February 28, 2018. On April 1, 2020, BT Garland JV, LLP completed the donation of the Garland Hospital facilities to the U.S. Department of Veteran Affairs.

## **FirstCare Health Plans**

On January 1, 2019, the Health Plan acquired SHA, L.L.C. d/b/a FirstCare Health Plans and its subsidiary, Southwest Life & Health Insurance Company, from Covenant Health System in Lubbock, Texas and Hendrick Health System in Abilene, Texas. The Health Plan recorded goodwill and intangible assets, net of approximately \$7 million, fixed assets of approximately \$18 million and other net liabilities of approximately \$25 million in 2019.

## **Baylor Scott & White Medical Center - Pflugerville**

In December 2018, the System opened Baylor Scott & White Medical Center – Pflugerville, a 25-bed multi-specialty hospital.

## **Baylor Scott & White The Heart Hospital - McKinney**

In July 2019, the System opened Baylor Scott & White The Heart Hospital – McKinney, a 4-bed hospital on the McKinney campus. The hospital will provide heart and vascular care to patients in McKinney, Texas.

## **Baylor Scott & White Medical Center - Buda**

In September 2019, the System opened Baylor Scott & White Medical Center – Buda, a 15-bed multispecialty hospital.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **Baylor Scott & White Medical Center - Carrollton**

In November 2019, BSWH signed a definitive agreement for the transfer of operations of Baylor Medical Center at Carrollton (Carrollton) d/b/a Baylor Scott & White Medical Center - Carrollton to Sana Healthcare Carrollton, LLC, d/b/a Carrollton Regional Medical Center. The transaction was completed on March 1, 2020.

## **Baylor Scott & White Medical Center – Austin**

In January 2020, the System opened Baylor Scott & White Medical Center – Austin, a 25-bed hospital. This is the System’s first full-service hospital within the Austin city limits.

## **MEDCO Construction**

On February 29, 2020, BSWH and MEDCO Construction, LLC (MEDCO) completed the sale of substantially all of the assets of MEDCO to The Christman Company, a national construction management and real estate development firm.

## **2. SIGNIFICANT ACCOUNTING POLICIES**

The accompanying combined financial statements of the System have been prepared in conformity with accounting principles generally accepted in the United States. The following is a summary of the significant accounting and reporting policies used in preparing the financial statements.

### **Application of New Accounting Pronouncements**

In May 2014, August 2015, April 2016, May 2016, December 2016, and February 2017, Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, “*Revenue from Contracts with Customers (Topic 606)*”; ASU 2015-14, “*Revenue from Contracts with Customers*”; ASU 2016-10, “*Identifying Performance Obligations and Licensing*”; ASU 2016-12, “*Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients*”; ASU 2016-20, “*Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers*”; and ASU 2017-05, “*Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*”, respectively, which supersedes the revenue recognition requirements in Accounting Standards Codification (ASC) 605, “*Revenue Recognition*.” These ASU’s address when an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The System adopted the guidance under these ASU’s,

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

effective July 1, 2018 using the modified retrospective approach at the date of initial application. As a result of the adoption, amounts previously classified as provision for bad debts in the statements of operations are now reflected as implicit price concessions, and therefore, included as a reduction of net patient care revenue. The patient accounts receivable allowance for uncollectible accounts was treated similarly. Other than these presentation changes, the adoption of ASC 606 did not have a material impact on the combined financial statements.

In November 2015, FASB issued ASU 2015-17, *“Balance Sheet Classification of Deferred Taxes.”* This ASU requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The System applied the provisions of ASU 2015-17 in fiscal year 2019, which did not have a material impact on the combined financial statements.

In January 2016, FASB issued ASU 2016-01, *“Recognition and Measurement of Financial Assets and Financial Liabilities.”* This ASU primarily affects the accounting for equity investments, financial liabilities under the fair value options and the presentation and disclosure requirements for financial instruments. The System applied the provisions of ASU 2016-01 in fiscal year 2020, which did not have a material impact on the combined statements of operations.

In February 2016, January 2018, July 2018, December 2018, and March 2019, FASB issued ASU 2016-02, *“Leases”*; ASU 2018-01, *“Land Easement Practical Expedient”*; ASU 2018-10, *“Codification Improvements to Topic 842, Leases”* and ASU 2018-11, *“Leases (Topic 842): Targeted Improvements”*; ASU 2018-20, *“Leases (Topic 842): Narrow-Scope Improvements for Lessors”*, and ASU 2019-01, *“Leases (Topic 842): Codification Improvements”*, respectively. These ASU’s require lessees to record a lease liability that represents the lessee’s future lease obligation payments and a right-of-use asset that represents the lessee’s right to use or control of a specified asset for the lease term. The main difference with previous practice being that lessees are now required to record an asset and liability for what was considered an operating lease under ASC 840, *“Leases”*. The System adopted the guidance under these ASU’s, effective July 1, 2019 using the effective date method, a practical expedient allowing application of the guidance for the adoption date forward without adjusting comparative periods. The System also elected to apply the practical expedient to not use hindsight to determine the lease term and assess impairment of right of use assets. As a result of the adoption, the System recognized right of use assets of approximately \$943 million and operating lease liabilities of approximately \$1,028 million. The System also elected not to assess whether land easements entered into prior to the adoption date that were not previously accounted for as a lease should be reported as such under ASC 842. The adoption of this standard did not have a corresponding material impact on the combined statements of operations. The System elected the three packaged transitional practical expedients under ASC 842-10-65-1(f), to not reassess at adoption (i) expired or existing

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

contracts for whether they are or contain a lease, (ii) the lease classification of any existing leases or (iii) initial indirect costs for existing leases. The System also elected the practical expedient that allows lessees to choose to not separate lease and non-lease components for all classes of underlying assets.

In March 2016, FASB issued ASU 2016-05, *“Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships.”* This ASU clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria remain intact. The System applied the provisions of ASU 2016-05 in fiscal year 2019, which did not have a material impact on the combined financial statements.

In March 2016, FASB issued ASU 2016-06, *“Contingent Put and Call Options in Debt Instruments.”* This ASU clarifies what steps are required when assessing whether the economic characteristics and risks of call (put) options are clearly and closely related to the economic characteristics and risks of their debt hosts, which is one of the criteria for bifurcating an embedded derivative. Consequently, when a call (put) option is contingently exercisable, an entity does not have to assess whether the event that triggers the ability to exercise a call (put) option is related to interest rates or credit risks. The System applied the provisions of ASU 2016-06 in fiscal year 2019, which did not have a material impact on the combined financial statements.

In August 2016, FASB issued ASU 2016-14, *“Presentation of Financial Statements of Not-for-Profit Entities.”* This ASU requires not-for-profit entities to report two classes of net assets, as well as enhances disclosures on board designated funds, liquidity, and functional expenses. The System applied the provisions of ASU 2016-14 in fiscal year 2019, which did not have a material impact on the combined financial statements.

In August 2016, FASB issued ASU 2016-15, *“Classification of Certain Cash Receipts and Cash Payments.”* This ASU provides cash flow statement classification guidance related to debt extinguishment costs, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, distributions made from equity method investees, separately identifiable cash flows, and application of the predominance principle. The System applied the provisions of ASU 2016-15 in fiscal year 2020, which did not have a material impact on the combined financial statements.

In October 2016, FASB issued ASU 2016-16, *“Intra-Entity Transfers of Assets Other Than Inventory.”* This ASU requires an entity to recognize the income tax consequences of an intra-

# BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

## Notes to Combined Financial Statements - continued

entity transfer of an asset other than inventory when the transfer occurs. The System applied the provisions of ASU 2016-16 in fiscal year 2020, which did not have a material impact on the combined financial statements.

In November 2016, FASB issued ASU 2016-18, “*Restricted Cash: A Consensus of the FASB Emerging Issues Task Force.*” This ASU requires a statement of cash flows to explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The System applied the provisions of ASU 2016-18 in fiscal year 2020, which had an immaterial impact on the cash used in investing activities in the combined statements of cash flows.

In January 2017, FASB issued ASU 2017-01, “*Clarifying the Definition of a Business.*” By clarifying the definition of a business, the amendments of this ASU affect all companies and other reporting organizations that must determine whether they have acquired or sold a business. The System applied the provisions of ASU 2017-01 in fiscal year 2020, which did not have a material impact on the combined financial statements.

In March 2017, FASB issued ASU 2017-07, “*Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost.*” This ASU requires that an employer report the service cost component in the same line item as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. The System applied the provisions of ASU 2017-07 in fiscal year 2020, which did not have a material impact on the combined financial statements.

In June 2018, FASB issued ASU 2018-08, “*Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made.*” These amendments clarify the accounting guidance around contributions of cash and other assets made and received by not-for-profit organizations and business enterprises. The System applied the provisions of ASU 2018-08 in fiscal year 2019, which did not have a material impact on the combined financial statements.

### **Other Accounting Pronouncements**

In June 2016, November 2018, April 2019, and May 2019, FASB issued ASU 2016-13, “*Financial Instruments-Credit Losses (Topic 326)*”; ASU 2018-19, “*Codification Improvements to Topic 326, Financial Instruments - Credit Losses*”; ASU 2019-04, “*Codification Improvements to Topic 326, Financial Instruments-Credit Losses, Topic 815, Derivatives and*

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

*Hedging, and Topic 825, Financial Instruments*”; and ASU 2019-05, “*Financial Instruments-Credit Losses (Topic 326)*”, respectively. The current standard delays the recognition of a credit loss on a financial asset until the loss is probable of occurring. These ASU’s remove the requirement that a credit loss be probable of occurring for it to be recognized. Instead these ASU’s require entities to use historical experience, current conditions, and reasonable and supportable forecasts to estimate their future expected credit losses. The provisions of these ASU’s are effective for fiscal years beginning after December 15, 2020. The System is currently evaluating the impact of these ASU’s.

In January 2017, FASB issued ASU 2017-04, “*Simplifying the Test for Goodwill Impairment.*” This ASU eliminates Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit’s goodwill with the carrying amount of that goodwill. The provisions of ASU 2017-04 are effective for fiscal years beginning after December 15, 2019, and interim periods within those years for public business entities, and December 15, 2021, and interim periods within those years for all other entities. The System is currently evaluating the impact of this ASU.

In March 2017, FASB issued ASU 2017-08, “*Premium Amortization on Purchased Callable Debt Securities.*” This ASU shortens the amortization period for certain callable debt securities held at a premium and requires the premium to be amortized to the earliest call date. However, the amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. The provisions of ASU 2017-08 are effective for fiscal years beginning after December 15, 2018, and interim periods within those years for public business entities, and December 15, 2019, and interim periods thereafter for all other entities. The System is currently evaluating the impact of this ASU.

In August 2018, FASB issued ASU 2018-13, “*Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement.*” The amendments in ASU 2018-13 remove certain disclosure requirements related to transfers between fair value levels, the valuation of Level 3 assets and liabilities, as well as the changes in unrealized gains and losses included in earnings for Level 3. Additionally, these amendments modify certain disclosure requirements related to transfers, purchases, and issuances in and out of Level 3 for nonpublic entities. The provisions of ASU 2018-13 are effective for fiscal years beginning after December 15, 2019 and interim periods within those years. An entity is permitted to early adopt any removed or modified disclosures upon issuance of ASU 2018-13 and delay adoption of the additional disclosures until their effective date. This ASU is not expected to have a material impact on the combined financial statements.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

## Notes to Combined Financial Statements - continued

In August 2018, FASB issued ASU 2018-14, “*Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans.*” The amendments in ASU 2018-14 remove certain requirements related to the amount and timing of plan assets expected to be returned to the employer, related party disclosures, and disclosures related to Level 3 fair value. Additionally, these amendments clarify and enhance the disclosures for projected benefit obligation and accumulated benefit obligation. The provisions of ASU 2018-14 are effective for fiscal years ending after December 15, 2020, for public business entities and December 15, 2021, for all other entities. The System is currently evaluating the impact of this ASU.

In August 2018, FASB issued ASU 2018-15, “*Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract.*” The amendments in ASU 2018-15 determine which implementation costs to capitalize as an asset and which costs to expense. Additionally, these amendments clarify how the capitalized implementation costs should be presented within the financial statements. The provisions of ASU 2018-15 are effective for fiscal years beginning after December 15, 2019, for public business entities and December 15, 2020, for all other entities. The System is currently evaluating the impact of this ASU.

In September 2020, FASB issued ASU 2020-07, “*Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets.*” This ASU requires a not-for-profit entity to present contributed non-financial assets as a separate line item in the statement of activities apart from contributed cash and other financial assets, and disclose whether the assets were monetized or utilized during the reporting period. The provisions of ASU 2020-07 are effective for fiscal years beginning after June 15, 2021 and interim periods thereafter. The System is currently evaluating the impact of this ASU.

### **Cash and Cash Equivalents**

Cash equivalents are defined as investments which have original maturities of three months or less. Cash equivalents consist primarily of securities issued by the United States government or its agencies, certificates of deposit, commercial paper, and dollar denominated foreign issued investments.

**BAYLOR SCOTT & WHITE HOLDINGS  
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Notes to Combined Financial Statements - continued

**THVG Funds Due from United Surgical Partners, Inc.**

THVG participates in a shared services accounts payable program with USPI, wherein USPI has custody of substantially all of THVG's cash, paying THVG and its facilities interest income on the net balance at prevailing market rates. Amounts held by USPI on behalf of THVG totaled approximately \$280 million and \$104 million at June 30, 2020 and 2019, respectively. The funds due from USPI are available on demand.

**Investments**

For all investments, interest and dividends, realized gains, and unrealized gains (losses) are included in gains on investments, net, in the accompanying combined statements of operations and changes in net assets, unless restricted by donor.

Interest and dividends, realized gains and unrealized gains (losses) for the years ended June 30, 2020 and 2019 consisted of the following (in millions):

	2020			
	Interest and Dividends	Realized Gains	Unrealized Losses	Total
Nonoperating gains (losses)	\$ 66	\$ 50	\$ (58)	\$ 58
Changes in net assets with donor restrictions	16	4	(9)	11
	\$ 82	\$ 54	\$ (67)	\$ 69
	2019			
	Interest and Dividends	Realized Gains	Unrealized Gains (Losses)	Total
Nonoperating gains	\$ 67	\$ 87	\$ 70	\$ 224
Changes in net assets with donor restrictions	15	13	(1)	27
	\$ 82	\$ 100	\$ 69	\$ 251

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **Patient Accounts Receivable**

Patient accounts receivables are related to providing healthcare services to patients, whose costs are primarily paid by government-related programs (i.e., Medicare and Medicaid), managed care providers, commercial insurance companies, and other payors. The System reports patient accounts receivable at amounts equal to the consideration the System expects to receive in exchange for providing healthcare services to its patients. The expected consideration is estimated using contractual provisions associated with specific payors, historical reimbursement rates, and an analysis of historical adjustments.

Receivables from government-related programs (i.e., Medicare and Medicaid) represent the only concentrated group of payors for the System's receivables, and management does not believe there are any unusual collectability risks associated with these government programs. Approximately 35% and 37% of patient accounts receivable are from government-related programs at June 30, 2020 and 2019, respectively. Commercial and managed care receivables consist of receivables from various payors involved in diverse activities and are subject to differing economic conditions.

The primary collection risk relates to uninsured patient accounts, including the patient portion of insured accounts. Implicit price concessions on these accounts are based on management's assessment of historical write-offs, cash collections, aging of the accounts, and other economic factors. Accounts are written off when collection efforts are exhausted.

## **Premiums Receivable and Premium Revenue**

Premium revenue is recognized as income in the period that members are entitled to receive services, as specified by the provisions of the arrangement. Premiums billed or received in advance of the service period are reported as unearned premiums.

Premiums receivable also includes annual settlements under the cost contract established between the Health Plan and the Centers for Medicare & Medicaid Services (CMS). The CMS Medicare Part B (Section 1876) cost plan contract covers Medicare-covered members' medical services allowed under Medicare Part B coverage and contains provisions for risk sharing and reimbursement of allowed costs for which the Health Plan is not at risk. Final reporting of each plan year's total allowed costs is not completed until June 30 of the year following the plan year, at which time an interim settlement of costs due to/from the plan occurs. Part B cost report audits, conducted on a triennial basis, may result in further adjustments to the total allowable costs reported in the current period and may affect the reimbursement to the Health Plan. At June

**BAYLOR SCOTT & WHITE HOLDINGS  
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Notes to Combined Financial Statements - continued

30, 2020 and 2019, the settlement amounts receivable from CMS under this contract were \$21 million and \$11 million, respectively. Premiums receivable generally are not collateralized.

Significant concentrations of premiums receivable were 99% from local, state, and federal government-related programs at June 30, 2020 and 2019. Premium revenue from local, state, and federal agencies accounted for 78% and 77% of total premium revenue for the years ended June 30, 2020 and 2019, respectively.

**Property and Equipment**

Property and equipment are stated at cost on the date of purchase or fair value on the date of contribution or business acquisition. Property and equipment and related accumulated depreciation and amortization are summarized below as of June 30, 2020 and 2019 (in millions):

	Useful Life	2020	2019
Land	—	\$ 295	\$ 288
Building and improvements	5 - 40 Years	4,490	4,357
Major moveable equipment and other	3 - 20 Years	3,278	3,056
Construction-in-progress	—	415	312
		8,478	8,013
Accumulated depreciation		(4,416)	(4,123)
		<u>\$ 4,062</u>	<u>\$ 3,890</u>

Property and equipment financed under finance leases totaled approximately \$346 million and \$398 million at June 30, 2020 and 2019, respectively, and related accumulated amortization was approximately \$129 million and \$153 million at June 30, 2020 and 2019, respectively. Amortization expense is included in depreciation and amortization expense in the accompanying combined statements of operations and changes in net assets.

Depreciation and amortization expense is calculated using the straight-line method over the estimated useful lives of the property and equipment or the lease term, whichever is less. Depreciation expense was approximately \$427 million and \$401 million for the years ended June 30, 2020 and 2019, respectively. Routine maintenance and repairs are charged to expense as incurred. Expenditures that increase capacities or extend useful lives are capitalized.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **Impairment of Long-Lived Assets**

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset, or related groups of assets, may not be recoverable from estimated future undiscounted cash flows. If circumstances suggest that the recorded amounts cannot be recovered based upon estimated future undiscounted cash flows, the carrying values of such assets are reduced to fair value. In the event of impairment, measurement of the amount of impairment may be based on valuation models using Level 3 inputs consisting of appraisals, fair values of similar assets, or estimates of future discounted cash flows resulting from the use and ultimate disposition of the asset. No impairments were identified in 2020 or 2019.

## **Goodwill and Intangible Assets**

Goodwill and intangible assets recorded in connection with acquisitions completed by the System are accounted for under ASC 350, *"Intangibles - Goodwill and Other."* Goodwill consists of costs in excess of tangible and intangible net assets acquired. Intangible assets consist of management service contract rights and other intangibles.

The System amortizes definite-lived intangible assets over their respective useful lives to the estimated residual values and reviews for impairment in the same manner as long-lived assets, as discussed below. No impairments were identified in 2020 or 2019.

Goodwill and indefinite-lived intangible assets are tested for impairment annually or more frequently if changing circumstances warrant. No impairments were identified in 2019.

Based on the divestiture of a non-performing facility, and the resulting impact on projections of future cash flows, BSWH determined impairment indicators were present in 2020. The long-lived assets that were reviewed for impairment consisted of an acquired contract indefinite-lived intangible. In 2020, management determined the estimated fair value of the contract was less than its carrying value and was impaired. Accordingly, BSWH recorded impairments of approximately \$3 million for the year ended June 30, 2020, which are included in other operating expenses in the accompanying combined statements of operations and changes in net assets.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

At June 30, 2020 and 2019, intangible assets and goodwill consisted of the following (in millions):

	2020		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets:			
Definite-lived intangible assets	\$ 44	\$ (32)	\$ 12
Indefinite-lived intangible assets	26	—	26
Total intangible assets	70	(32)	38
Goodwill	835	—	835
Total intangible assets and goodwill	\$ 905	\$ (32)	\$ 873

	2019		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets:			
Definite-lived intangible assets	\$ 45	\$ (31)	\$ 14
Indefinite-lived intangible assets	29	—	29
Total intangible assets	74	(31)	43
Goodwill	835	—	835
Total intangible assets and goodwill	\$ 909	\$ (31)	\$ 878

**Income Taxes**

Due to the organizational structure, certain of the System's entities are taxable under the Internal Revenue Code and some entities are tax exempt but are required to pay income taxes for unrelated business activities. The overall impact of federal income taxes to the System's combined financial statements is not significant. In addition, certain of the System's entities file partnership income tax returns in the U.S. federal jurisdiction and franchise tax returns in the state of Texas. These entities are no longer subject to U.S. federal, state, and local income tax examinations by authorities for years prior to 2015.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

The Texas franchise tax applies to certain of the System's entities. The tax is calculated on a margin base, and is therefore, reflected in the System's combined statements of operations and changes in net assets as income tax expense.

The System follows the provisions of ASC 740, "*Income Taxes.*" As of June 30, 2020 and 2019, the System had no material gross unrecognized tax benefits.

#### **Insurance**

For 2020 and 2019, excess policies that covered claims that exceeded \$10 million per incident and \$50 million in the general aggregate (shared) for hospital professional liability, general liability, and HTPN professional liability were provided by BSWA. The excess liability policies are reinsured 100% by ACE American Insurance Company (Chubb) and various other reinsurers.

#### **Reserves for Self-Insurance Losses and Loss Adjustment Expenses**

The reserve for losses and loss adjustment expenses are based upon management's estimate of the ultimate liability for outstanding losses and loss adjustment expenses determined in comparison with historical and industry loss statistics. Management uses case basis evaluations and actuarial analysis to develop their estimate. Management believes that the reserves for losses and loss adjustment expenses are adequate. However, because of the extended period of time over which losses are settled and the general uncertainty surrounding the estimates, the ultimate settlement cost of the losses and the related loss adjustment expenses could vary, and these differences could be material. The estimate is continuously reviewed and, as adjustments to the liability become necessary, they are reflected in current operations.

Liabilities for outstanding claims, including estimates for claims incurred but not reported, as well as reported claims pending settlement, are actuarially determined and discounted using an interest rate of 2.0% in both 2020 and 2019. Total undiscounted reserves for losses and loss adjustment expenses were approximately \$118 million and \$108 million at June 30, 2020 and 2019, respectively. Discounted reserves for losses and loss adjustment expenses, including a risk margin at an approximate seventy percent confidence level, were approximately \$120 million and \$110 million at June 30, 2020 and 2019, respectively.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **Contributions and Gifts**

When received or pledged, unrestricted gifts are reported as contributions to net assets without donor restrictions and donor-restricted items are reported as contributions to net assets with donor restrictions. Donor-restricted contributions are restricted as to use and are transferred from net assets with donor restrictions to net assets without donor restrictions when the restrictions are satisfied or, in the case of endowment funds, when related earnings are appropriated for expenditure.

## **Net Assets with Donor Restrictions**

Net assets with donor restrictions are donor restricted as to use or time, and are transferred from net assets with donor restrictions to net assets without donor restrictions when the restrictions are satisfied. Net assets are primarily available for patient care, medical education, and research.

Net assets with donor restrictions include donor-restricted endowments in which the principal is invested in perpetuity and only the income from the investments is expended for designated purposes. Income on endowment funds restricted for specified purposes, or which is required to be invested in perpetuity, is reported in the accompanying combined statements of operations and changes in net assets without and with donor restrictions.

## **Revenue and Gains in Excess of Expenses and Losses**

The combined statements of operations and changes in net assets include revenues and gains in excess of expenses and losses. Other changes in net assets without donor restrictions which are excluded from revenue and gains in excess of expenses and losses, consistent with industry practice, include unrealized losses on investments, transactions related to noncontrolling interests, and net assets released from restrictions for capital expenditures.

## **Derivative Financial Instruments**

ASC 815, "*Derivatives and Hedging*," requires that all derivative financial instruments be recognized in the combined financial statements and measured at fair value regardless of the purpose or intent for holding them. Changes in the fair value of derivative financial instruments are recognized periodically in nonoperating gains. The System's policy is to not hold or issue derivatives for trading purposes and to avoid derivatives with leverage features.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **Use of Estimates**

The preparation of 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 as of the date of the combined balance sheets, disclosure of contingent assets and liabilities as of the date of the combined financial statements, and reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

## **Reclassification**

Certain reclassifications were made to the 2019 financial statements to conform to the 2020 presentation.

## **CARES Act**

In March 2020, the global COVID-19 pandemic began to impact the operations of the System. In response to the COVID-19 pandemic, the United States government passed the Coronavirus, Aid, Relief, and Economic Security Act (CARES Act). Under programs included in the CARES Act, the System received and recognized approximately \$187 million of emergency relief funds in other operating revenue and approximately \$23 million of employee retention tax credit in salaries, wages, and employee benefits. The System also received approximately \$765 million in Medicare advance payments in April 2020 and recorded a contract liability in accordance with ASC 606, "*Revenue Recognition*", which is included in third-party program liabilities. Repayment of the advance payments begin one year after payment was issued to the System. The System deferred approximately \$47 million of the employer portion of FICA taxes, which will be paid over a two year period with one half due in December 2021 and the other half due in December 2022.

## **3. FAIR VALUE OF FINANCIAL INSTRUMENTS**

### **Fair Value Measurements**

As defined in ASC 820, "*Fair Value Measurements*", fair value is based on the prices that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, ASC 820 establishes a three-tier fair value hierarchy for disclosure of fair value measurements.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

## Notes to Combined Financial Statements - continued

The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 - Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable by market participants for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - Inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability that are unobservable and developed based on the best information available in the circumstances.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The carrying values of cash and cash equivalents, THVG funds due from USPI, patient accounts receivable, other receivables, trade accounts payable, accrued liabilities, and third-party programs payable are reasonable estimates of their fair value due to the short-term nature of these financial instruments.

Fair values of short-term investments and long-term investments are generally 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. Inputs are obtained from various sources including market participants, dealers, and brokers. This applies to investments such as domestic equities, U.S. treasuries, exchange-traded mutual funds, and agency securities.

### **Alternative Investments**

Investments held consist of marketable securities as well as securities that do not have readily determinable fair values. Private equity investments, real estate investments, and hedge funds are collectively referred to as "alternative investments." These are included in unrestricted and restricted long-term investments in the accompanying combined balance sheets. The investments in alternative investments are valued by management at fair value utilizing the net asset value (NAV) provided by the underlying investment companies unless management determines some

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

other valuation is more appropriate. Such fair value estimates do not reflect early redemption penalties as the System does not intend to sell such investments before the expiration of the early redemption periods. The fair values of the securities held by limited partnerships that do not have readily determinable fair values are determined by the general partner and are based on historical cost, appraisals, or other estimates that require varying degrees of judgment. If no public market exists for the investment securities, the fair value is determined by the general partner taking into consideration, among other things, the cost of securities, prices of recent significant placements of securities of the same issuer, and subsequent developments concerning the companies to which the securities relate. Investments valued at NAV are not leveled within the fair value hierarchy. BHCS Foundation also has other real estate and oil and gas interests which are carried at the lower of cost or market and represent Level 3 assets.

### **Beneficial Interests**

The System records charitable remainder trusts, where it is not the trustee, at the discounted present value of the estimated future cash flows. These trusts are reported in contributions receivable, net, in the accompanying combined balance sheets. When a third-party serves as trustee, the beneficial interests are required to be measured at fair value on a recurring basis. As beneficial interests utilize multiple unobservable inputs, including no active markets, and are measured using management's assumption about risk inherent in the valuation technique, beneficial interests in split-interest agreements represent Level 3 assets.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the System believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

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**BAYLOR SCOTT & WHITE HOLDINGS  
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Notes to Combined Financial Statements - continued

The following tables set forth below, by level, the financial assets and liabilities measured at fair value on a recurring basis at June 30, 2020 and 2019 (in millions):

<b>Assets:</b>	June 30, 2020			
	Total	Level 1	Level 2	Level 3
Cash and cash equivalents				
Cash	\$ 1,923	\$ 1,923	\$ —	\$ —
Money market funds	42	42	—	—
Total cash and cash equivalents	1,965	1,965	—	—
Short-term investments				
Mutual funds	349	349	—	—
Fixed income securities	2	—	2	—
U.S. government securities	4	—	4	—
Other	1	1	—	—
Total short-term investments	356	350	6	—
Unrestricted long-term investments				
Cash	1	1	—	—
Certificates of deposit	1	1	—	—
Mutual funds	529	529	—	—
Equity securities	1,106	253	853	—
Fixed income securities	681	—	681	—
U.S. government securities	512	—	512	—
Mortgage-backed securities	146	—	146	—
Split-interest agreements	1	—	1	—
Cash surrender value of life insurance	1	—	—	1
Common funds				
Group investment fund	1	—	1	—
Assets held at NAV practical expedient <sup>(1)</sup>				
Hedge funds/diversifiers alternative investments	586			
Private equity/debt alternative investments	269			
Real estate alternative investments	130			
Total unrestricted long-term investments	3,964	784	2,194	1

In the accompanying combined balance sheets, unrestricted long-term investments at June 30, 2020, includes an investment of approximately \$130 million accounted for under the measurement alternative.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

<b>Assets (continued):</b>	June 30, 2020			
	Total	Level 1	Level 2	Level 3
Restricted long-term investments				
Cash	\$ 8	\$ 8	\$ —	\$ —
Mutual funds	83	83	—	—
Equity securities	163	39	124	—
Fixed income securities	33	—	33	—
U.S. government securities	26	—	26	—
Mortgage-backed securities	7	—	7	—
Split-interest agreements	5	—	5	—
Cash surrender value of life insurance	1	—	—	1
Common funds				
Group investment fund	48	—	48	—
Group bond fund	3	—	3	—
Group equity fund	5	—	5	—
Other funds	2	2	—	—
Assets held at NAV practical expedient <sup>(1)</sup>				
Hedge funds/diversifiers alternative investments	61			
Private equity/debt alternative investments	42			
Real estate alternative investments	10			
Total restricted long-term investments	497	132	251	1

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**BAYLOR SCOTT & WHITE HOLDINGS  
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Notes to Combined Financial Statements - continued

	June 30, 2020			
<b>Assets (continued):</b>	Total	Level 1	Level 2	Level 3
Assets whose use is limited				
Cash	\$ 1	\$ 1	\$ —	\$ —
Money market funds	6	6	—	—
Mutual funds	231	231	—	—
Equity securities	2	2	—	—
Fixed income securities	20	—	20	—
U.S. government securities	25	—	25	—
Mortgage-backed securities	10	—	10	—
Total assets whose use is limited	295	240	55	—
Contributions receivable, net				
Total beneficial interests in split-interest agreements	33	—	—	33
Total assets at fair value	\$ 7,110	\$ 3,471	\$ 2,506	\$ 35
<b>Liabilities:</b>				
Interest rate swap agreements, net of collateral	\$ 365	\$ —	\$ 365	\$ —
Total liabilities at fair value	\$ 365	\$ —	\$ 365	\$ —

<sup>(1)</sup> Hedge fund/diversifiers alternative investments, private equity/debt alternative investments, real estate alternative investments, and other investments for which fair value is measured using the NAV per share as a practical expedient are not leveled within the fair value hierarchy and are included as a reconciling item to total investments.

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**BAYLOR SCOTT & WHITE HOLDINGS  
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Notes to Combined Financial Statements - continued

	June 30, 2019			
	Total	Level 1	Level 2	Level 3
<b>Assets:</b>				
Cash and cash equivalents				
Cash	\$ 788	\$ 788	\$ —	\$ —
Money market funds	25	25	—	—
Total cash and cash equivalents	813	813	—	—
Short-term investments				
Mutual funds	330	330	—	—
Fixed income securities	5	—	5	—
Other	2	2	—	—
Total short-term investments	337	332	5	—
Unrestricted long-term investments				
Cash	1	1	—	—
Certificates of deposit	1	1	—	—
Mutual funds	535	535	—	—
Equity securities	1,129	277	852	—
Fixed income securities	765	—	765	—
U.S. government securities	538	—	538	—
Mortgage-backed securities	134	—	134	—
Split-interest agreements	1	—	1	—
Cash surrender value of life insurance	1	—	—	1
Common funds				
Group investment fund	1	—	1	—
Assets held at NAV practical expedient <sup>(1)</sup>				
Hedge funds/diversifiers alternative investments	580			
Private equity/debt alternative investments	249			
Real estate alternative investments	137			
Total unrestricted long-term investments	4,072	814	2,291	1

In the accompanying combined balance sheets, unrestricted long-term investments at June 30, 2019, includes an investment of approximately \$129 million accounted for under the cost method.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

<b>Assets (continued):</b>	June 30, 2019			
	Total	Level 1	Level 2	Level 3
Restricted long-term investments				
Cash	\$ 4	\$ 4	\$ —	\$ —
Mutual funds	89	89	—	—
Equity securities	168	42	126	—
Fixed income securities	35	—	35	—
U.S. government securities	26	—	26	—
Mortgage-backed securities	7	—	7	—
Split-interest agreements	5	—	5	—
Cash surrender value of life insurance	1	—	—	1
Common funds				
Group investment fund	49	—	49	—
Group bond fund	3	—	3	—
Group equity fund	6	—	6	—
Other funds	1	1	—	—
Assets held at NAV practical expedient <sup>(1)</sup>				
Hedge funds/diversifiers alternative investments	67			
Private equity/debt alternative investments	45			
Real estate alternative investments	12			
Total restricted long-term investments	518	136	257	1

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**BAYLOR SCOTT & WHITE HOLDINGS  
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Notes to Combined Financial Statements - continued

	June 30, 2019			
	Total	Level 1	Level 2	Level 3
<b>Assets (continued):</b>				
Assets whose use is limited				
Cash	\$ 1	\$ 1	\$ —	\$ —
Money market funds	6	6	—	—
Mutual funds	202	202	—	—
Equity securities	2	2	—	—
Fixed income securities	16	—	16	—
U.S. government securities	30	—	30	—
Mortgage-backed securities	10	—	10	—
Total assets whose use is limited	267	211	56	—
Contributions receivable, net				
Total beneficial interests in split-interest agreements	29	—	—	29
Total assets at fair value	\$ 6,036	\$ 2,306	\$ 2,609	\$ 31
<b>Liabilities:</b>				
Interest rate swap agreements, net of collateral	\$ 274	\$ —	\$ 274	\$ —
Total liabilities at fair value	\$ 274	\$ —	\$ 274	\$ —

<sup>(1)</sup> Hedge funds/diversifiers alternative investments, private equity/debt alternative investments, real estate alternative investments, and other investments for which fair value is measured using the NAV per share as a practical expedient are not leveled within the fair value hierarchy and are included as a reconciling item to total investments.

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

The following table is a roll forward of the combined balance sheet amounts for financial instruments classified by the System within Level 3 of the valuation hierarchy defined above for the years ended June 30, 2020 and 2019 (in millions):

	2020		
	Split-Interest Agreements	Other	Total
Balance, beginning of year	\$ 29	\$ 2	\$ 31
Realized gains, net	2	—	2
Unrealized gains, net	2	—	2
Balance, end of year	\$ 33	\$ 2	\$ 35

  

	2019		
	Split-Interest Agreements	Other	Total
Balance, beginning of year	\$ 25	\$ 2	\$ 27
Realized gains, net	1	—	1
Purchases	1	—	1
Settlements	2	—	2
Balance, end of year	\$ 29	\$ 2	\$ 31

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

At June 30, 2020 and 2019, alternative investments recorded at NAV consisted of the following (in millions):

	2020			
	Fair Value	Unfunded Commitments	Redemption Frequency if Currently Eligible	Redemption Notice Period
Equity-linked investments <sup>a</sup>	\$ 52	\$ —	quarterly, annually	60-90 days
Event-driven investments <sup>b</sup>	79	—	quarterly, annually	30-90 days
Credit-linked investments <sup>c</sup>	89	—		
Multi-strategy investments <sup>d</sup>	1	—	monthly, quarterly	30-90 days
Tactical trading investments <sup>e</sup>	101	—	daily, monthly	2-90 days
Risk parity and global asset allocation fund <sup>f</sup>	325	—	monthly	5-30 days
Real estate funds - open ended <sup>g</sup>	55	—	quarterly	90 days
Real estate funds - close ended <sup>h</sup>	85	18		
Private equity funds <sup>i</sup>	240	122		
Private debt funds <sup>j</sup>	71	32		
Total	<u>\$ 1,098</u>	<u>\$ 172</u>		

  

	2019			
	Fair Value	Unfunded Commitments	Redemption Frequency if Currently Eligible	Redemption Notice Period
Equity-linked investments <sup>a</sup>	\$ 51	\$ —	quarterly, annually	60-90 days
Event-driven investments <sup>b</sup>	85	—	quarterly, annually	30-90 days
Credit-linked investments <sup>c</sup>	85	—		
Multi-strategy investments <sup>d</sup>	1	—	monthly, quarterly	30-90 days
Tactical trading investments <sup>e</sup>	107	—	daily, monthly	2-90 days
Risk parity and global asset allocation fund <sup>f</sup>	318	—	monthly	5-30 days
Real estate funds - open ended <sup>g</sup>	57	—	quarterly	90 days
Real estate funds - close ended <sup>h</sup>	92	21		
Private equity funds <sup>i</sup>	222	158		
Private debt funds <sup>j</sup>	72	61		
Total	<u>\$ 1,090</u>	<u>\$ 240</u>		

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

- a) Equity-linked fund managers buy equities that are expected to increase in value and sell short equities that are expected to decrease in value. Portfolios range from net short to net long, depending on market conditions. Aggressive funds may capture returns by exceeding 100% exposure while conservative funds mitigate market risk by maintaining net exposures of between 0-50%. Typically, equity-linked strategies are based on "bottom up" fundamental analysis of the individual companies, in which investments are made. There may also be "top down" analysis of the risks and opportunities offered by industries, sectors, countries, and the macroeconomic situation. Equity-linked managers may be generalists or focus on certain industries, sectors, regions, or equity category (i.e. small or large cap and value or growth). There are many trading styles, with frequent or dynamic traders and some longer-term investors. Returns are generally more correlated with the direction of the equity markets, although reduction in market risk exposure through shorting is expected to enhance the absolute and risk-adjusted returns relative to the overall performance of the asset class. The fair values of the investments in this class have been estimated using the net asset value per share of the funds.
- b) Event-driven fund managers seek to exploit pricing inefficiencies that may occur before or after corporate events such as an earnings announcement, bankruptcy, merger, acquisition, or spinoff. Returns are less correlated with the general direction of market movements primarily due to the idiosyncratic nature of individual events. Several investment managers include quarterly percentage redemption limits. The fair values of the investments in this class have been estimated using the net asset value per share of the funds.
- c) Credit-linked fund managers seek to profit from the mispricing of related securities. These strategies utilize quantitative and qualitative analysis to identify securities or spreads between securities that deviate from their fair value and/or historical norms. Examples include convertible arbitrage, fixed arbitrage, statistical arbitrage, and select global macro strategies. Fund returns are generally not dependent on the direction of market movements. The fair values of the investments in this class have been estimated using the net asset value per share of the funds.
- d) Multi-strategy fund managers focus on large, long-term mispricing in the global fixed-income, equity and credit markets, capturing relative-value anomalies via multi-product trades. Returns are relatively uncorrelated with the general direction of market movements since they avoid taking a directional bias with regards to the price movement of a specific stock or market. Several investment managers include quarterly percentage redemption limits and/or early redemption penalties. The fair values of the investments in this class have been estimated using the net asset value per share of the funds.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

- e) Tactical trading fund managers generally invest on a large scale around the world using economic theory to justify the decision making process on either a discretionary or systematic basis. Strategies are typically based on forecasts and analysis about interest rate trends, the general flow of funds, political changes, government policies, inter-government relations, and other broad systemic and technical factors. Returns are relatively uncorrelated with the general direction of market movements. Several investment managers include quarterly percentage redemption limits. The fair values of the investments in this class have been estimated using the net asset value per share of the funds.
- f) Risk parity and global asset allocation fund managers invest across global markets including equities, nominal government bonds, inflation linked bonds, commodities, and emerging markets on a risk balanced framework. Typically, these strategies incorporate leverage to increase the risk contribution from low volatility asset classes (e.g., inflation-linked bonds and nominal government bonds). The fair values of the investments in this class have been estimated using the net asset value per share of the funds.
- g) Real estate – open end fund managers invest in U.S. commercial real estate. Redemptions are available on a quarterly basis, subject to the discretion of the General Partners. The General Partners may elect to establish a redemption queue should the level of redemptions for a given quarter be detrimental to the fund’s overall performance. The fair values of the investments in this class have been estimated using the net asset value, which is based on the ownership interest of partners' capital.
- h) Real estate – closed end fund managers invest primarily in U.S. commercial real estate and industries related to real estate, with some having minimal exposure outside of the U.S. These partnerships are illiquid, and therefore do not have a redemption feature. Distributions from each fund will be received as the underlying investments of the funds are liquidated. It is estimated that the underlying assets of these funds will be liquidated over the next six years with the value of those underlying assets being replaced by investments in new real estate funds. The fair values of the investments in this class have been estimated using the net asset value, which is based on the ownership interest of partners' capital.
- i) Forty-five private equity fund managers invest in a variety of mostly private companies. These investments have a drawdown structure where a portion of commitments (which are made upon entering the partnership) are called gradually over the first 3-6 years of the partnership’s life. It is expected that most of the unfunded commitments should be called within the next 6 years. These partnerships are illiquid, and therefore do not have a redemption feature. Instead, the nature of the investments, in this class, is that distributions

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

are received as the investment in the underlying companies are sold. It is estimated that the current underlying assets of these partnerships should be liquidated within the next 10 years. The investments are valued based on each partnership's valuation policy which is then subject to annual third-party financial audits. Financial audits are available approximately 90 days following year end. Therefore, the valuation at year end reflects the latest reported manager valuation with adjustments for new capital calls and distributions.

- j) Fourteen private debt fund managers invest in a variety of mostly private companies. These investments have a drawdown structure where a portion of commitments (which are made upon entering the partnership) are called gradually over the first 1-3 years of the partnership's life. It is expected that most of the unfunded commitments should be called within the next 4 years. These partnerships are illiquid, and therefore do not have a redemption feature. Instead, distributions are received as income from the debt and as the investment in the underlying companies are sold or the debt principal is repaid. It is estimated that the current underlying assets of these partnerships should be liquidated within the next 6 years. The investments are valued based on each partnership's valuation policy which is then subject to annual third party financial audits. Financial audits are available approximately 90 days following year end. Therefore, the valuation at year end reflects the latest reported manager valuation with adjustments for new capital calls and distributions.

### **Long-term Debt**

The System's long-term debt obligations, excluding finance leases, are reported in the accompanying combined balance sheets at carrying value which totaled approximately \$3,321 million and \$3,032 million at June 30, 2020 and 2019, respectively. The fair value of these obligations is estimated based primarily on quoted market prices for related bonds and is therefore classified as Level 2. The fair value of the System's long-term debt obligations, excluding finance leases, totaled approximately \$3,174 million at June 30, 2019.

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# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **4. LIQUIDITY**

The System's financial assets available as of June 30, 2020 and 2019, for general expenditure within one year of the balance sheet date, are comprised of the following (in millions):

	<u>2020</u>	<u>2019</u>
Cash and cash equivalents	\$ 1,965	\$ 813
Short-term investments	356	337
THVG funds due from USPI	280	104
Patient accounts receivable	781	845
	<u>\$ 3,382</u>	<u>\$ 2,099</u>

As a part of the System's liquidity management plan, BSWH structures its financial assets to be available for general operating expenses, current liabilities, and other obligations as they become due. Excess daily cash requirements are invested in short-term obligations. Additionally, BSWH has access to public and private debt-markets.

## **5. MEDICAL CLAIMS PAYABLE**

Medical claims payable represents management's estimate of the ultimate net cost of all reported and unreported medical claims and claim adjustment expenses incurred through June 30, 2020 and 2019. Reserves for unpaid medical claims are actuarially estimated using individual case-basis valuations and statistical analysis. These estimates are subject to the effects of trends in claim severity and frequency. Although considerable variability is inherent in such estimates, management believes that reserves for unpaid medical claims are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known. Such adjustments are included in operations when determined. There were no material adjustments recorded to these estimates during the years ended June 30, 2020 and 2019.

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

A roll forward of medical claims payable for the years ended June 30, 2020 and 2019, is as follows (in millions):

	<u>2020</u>	<u>2019</u>
Medical claims payable - beginning of year	\$ 73	\$ 29
Incurred related to:		
Current year	745	563
Prior years	<u>(10)</u>	<u>(7)</u>
	<u>735</u>	<u>556</u>
Paid related to:		
Current year	(684)	(492)
Prior years	<u>(59)</u>	<u>(20)</u>
	<u>(743)</u>	<u>(512)</u>
Medical claims payable - end of year	<u>\$ 65</u>	<u>\$ 73</u>

The following table provides information about incurred and paid medical claims development for the years ended June 30, 2020 and 2019 (in millions):

	<u>2020</u>	<u>2019</u>
Incurred medical claims by claim year		
2017	\$ 354	\$ 354
2018	285	284
2019	554	563
2020	<u>745</u>	<u>—</u>
Total incurred medical claims	<u>1,938</u>	<u>1,201</u>
Paid medical claims by claim year		
2017	354	351
2018	285	285
2019	550	492
2020	<u>684</u>	<u>—</u>
Total paid medical claims	<u>1,873</u>	<u>1,128</u>
Medical claims payable	<u>\$ 65</u>	<u>\$ 73</u>

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **6. OPERATING LEASE LIABILITIES**

The System determines if an arrangement is a lease at inception of the contract. The right of use assets represent the System's right to use the underlying assets for the lease term and the lease liabilities represent the System's obligation to make lease payments arising from the leases. Right of use assets and lease liabilities are recognized at commencement date based on the present value of lease payments over the lease term. The System uses its estimated incremental borrowing rate, which is derived from information available at the lease commencement date, in determining the present value of lease payments. The System estimates an incremental borrowing rate for each lease by utilizing historical and projected financial data, estimating a hypothetical credit rating using publicly available market data, and adjusting the market data to reflect the effects of collateralization.

The System's operating leases are primarily for real estate including office space, as well as medical and office equipment. The System's finance leases are primarily for select real estate properties, medical equipment, and vehicles. For finance leases related disclosures see Note 7. The System's real estate agreements typically have initial terms of three to fifteen years with longer terms for select properties. Renewal options are typically negotiated for real estate leases, most commonly for one or more renewal option terms of five to ten years each. Equipment lease agreements typically have initial terms of two to seven years. The System does not record leases with an initial term of 12 months or less (referred to as "short-term leases") in its combined balance sheets.

Certain real estate and equipment leases also include options to purchase the leased property. The useful life of assets and leasehold improvements are limited by the lease term, unless there is a purchase or renewal option reasonably certain of exercise or a transfer of title. Certain medical equipment leases have terms with a bargain purchase option that is reasonably certain of exercise, so medical equipment assets can have useful lives that can range on average from two to seven years. Certain lease agreements for real estate include additional payments for actual common area maintenance and other operating expenses while others include rental payments adjusted periodically for inflation. These variable lease payments are recognized in other operating expenses but are not included in the right of use asset or liability balances. The System's lease agreements do not contain any material residual value guarantees, restrictions or covenants.

The weighted-average remaining lease term for operating leases is 7.73 years and the weighted-average discount rate is 2.19% for the year ended June 30, 2020.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

For the year ended June 30, 2020, the System's total lease cost was as follows (in millions):

Operating lease cost	\$	176
Short-term lease cost		29
Variable lease cost		57
Sublease income		(3)
Total lease cost	<u>\$</u>	<u>259</u>

For the year ended June 30, 2020, supplemental cash flow information related to operating leases was as follows (in millions):

Operating cash flows from operating leases	\$	146
Right of use assets obtained in exchange for lease obligations		80

Future maturities of operating lease liabilities as of June 30, 2020 are as follows (in millions):

2021	\$	172
2022		164
2023		143
2024		126
2025		106
Thereafter		372
		<u>1,083</u>
Less imputed interest		121
	<u>\$</u>	<u>962</u>

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

The System leases various equipment and property under operating leases. As of June 30, 2019, these payments are due monthly through March 2033. Future minimum lease commitments under operating leases that have initial or remaining non-cancelable lease terms in excess of one year are as follows as of June 30, 2019 (in millions):

2020	\$	169
2021		152
2022		140
2023		124
2024		109
Thereafter		463
	<u>\$</u>	<u>1,157</u>

The System has incurred rental expense for both cancelable and noncancelable equipment and space leases totaling approximately \$216 million for the year ended June 30, 2019. Rental expense is included in other operating expenses in the accompanying combined statements of operations and changes in net assets.

**7. LONG-TERM DEBT AND FINANCE LEASE OBLIGATIONS**

Long-term debt and finance lease obligations as of June 30, 2020 and 2019, consist of the following:

	2020	2019
	(In millions)	
BSW Holdings -		
Series 2015 Bonds (Taxable) -		
Term Bonds, fixed interest rates ranging from 2.12% to 4.19%, payable semi-annually, principal payable November 2020, 2025 and 2045	\$ 550	\$ 550
Series 2015A Revenue Bonds -		
Term Bonds, fixed interest rate of 2.19%, payable semi-annually, principal payable through November 2027	158	167

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

	2020	2019
	(In millions)	
Series 2015B Revenue Bonds - Variable interest rate payable monthly, principal payable November 2032 through November 2050	\$ —	\$ 45
Series 2015C Revenue Bonds - Variable interest rate payable monthly, principal payable August 2030 through August 2041	—	86
Series 2016 Bonds (Taxable) - Term Bonds, fixed interest rates ranging from 1.95% to 3.97%, payable semi-annually, principal payable November 2021, 2026 and 2046	535	535
Series 2016A Revenue Bonds - Serial and Term Bonds, fixed interest rates ranging from 3.00% to 5.00%, payable semi-annually, principal payable through November 2045	355	360
Series 2017A Revenue Bonds - Variable interest rate payable monthly, principal payable August 2030 through August 2050	—	75
Series 2017B Revenue Bonds - Variable interest rate payable monthly, principal payable August 2030 through August 2050	—	75
Series 2017C Revenue Bonds - Variable interest rate payable monthly, principal payable August 2030 through August 2050	—	44
Series 2019A Revenue Bonds (Taxable)- Fixed interest rate payable semi-annually (2.36% at June 30, 2020), principal payable through November 2030	41	—

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

	2020	2019
	(In millions)	
Series 2019B Revenue Bonds - Variable interest rate payable monthly (0.61% at June 30, 2020), principal payable November 2032 through November 2050	\$ 97	\$ —
Series 2019C Revenue Bonds - Variable interest rate payable monthly (0.42% at June 30, 2020), principal payable August 2030 through August 2046	180	—
Series 2019D Revenue Bonds - Variable interest rate payable monthly (0.36% at June 30, 2020), principal payable November 2032 through November 2050	45	—
Series 2019E Revenue Bonds - Variable interest rate payable monthly ranging from 0.50% to 0.53% at June 30, 2020, principal payable through August 2050	96	—
Series A Commercial Paper Notes (Taxable) - Variable interest rate (0.20% to 0.28% at June 30, 2020)	208	208
Credit Line Revolver (Taxable) - Variable interest rate payable monthly (0.49% at June 30, 2020), principal payable January 2023	400	79
BHCS -		
Series 2011A Revenue Bonds - Serial Bonds, fixed interest rates ranging from 3.38% to 4.63%, payable semi-annually, principal payable through November 2028	2	41
Series 2011B Revenue Bonds - Window Variable Rate Demand Bonds, variable interest rate (0.43% at June 30, 2020), payable monthly, principal payable November 2032 through 2050	50	50

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

	2020	2019
	(In millions)	
Series 2011C Revenue Bonds - Variable Rate Demand Bonds, variable interest rate (0.11% at June 30, 2020), payable monthly, principal payable November 2032 through 2050	\$ 45	\$ 45
Series 2013A Revenue Bonds - Serial and Term Bonds, fixed interest rates ranging from 3.38% to 5.00%, payable semi-annually, principal payable November 2028 through 2043	169	169
Series 2013B Revenue Bonds - Window Variable Rate Demand Bonds, variable interest rate (.43% at June 30, 2020), payable monthly, principal payable November 2033 through 2050	45	45
Series 2013C Revenue Bonds (Taxable) - Term Bonds, fixed interest rate of 4.45%, payable semi-annually, principal payable November 2033 through 2043	63	63
SWH -		
Series 2013A Revenue Bonds - Serial and Term Bonds, fixed interest rates ranging from 4.00% to 5.00%, payable semi-annually, principal payable through August 2043	166	169
Series 2013C Revenue Bonds - Variable interest rate payable monthly, principal payable August 2030 through August 2046	—	94
Lake Pointe Construction Loan - Interest rate of 4.21% payable monthly, principal and interest payable through December 2026	44	45

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

	2020	2019
	(In millions)	
Baylor Medical Center at Irving - Building Lease - Interest rate of 3.7% payable monthly, principal and interest payments through March 2045	\$ 143	\$ 147
Baylor Medical Center at Carrollton - Building Lease - Interest rate of 9.50%, payable monthly, principal and interest payments through December 2033	—	52
Baylor Scott & White Sports Therapy & Research at The Star in Frisco - Building Leases - Interest rates ranging from 4.10% to 6.80%, payable monthly, principal and interest payments through May 2033	57	59
THVG - Equipment Notes Payable - Interest rates ranging from 2.32% to 8.00%, payable monthly, principal and interest payments through December 2025	42	52
Building Lease, Frisco Medical Center, LLP - Interest rate of 11.63%, payable monthly, principal and interest payments through June 2027	48	41
Building Lease, Arlington Orthopedic and Spine Hospital - Interest rate of 8.61%, payable monthly, principal and interest payments through February 2030	23	24
Building Lease, Dallas Uptown - Interest rate of 9.43%, payable monthly, principal and interest payments through January 2031	20	21
Other THVG Leases - Interest rates ranging from 1% to 12.66%, payable monthly, principal and interest payments through May 2033	3	15

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

	2020	2019
	(In millions)	
Other finance leases and long-term debt	\$ 35	\$ 61
	3,620	3,417
Net unamortized original issue premium/discount and bond issuance costs	47	50
Current maturities	(102)	(142)
Commercial paper	(208)	(208)
Long-term debt subject to short-term remarketing arrangements	(95)	(95)
	\$ 3,262	\$ 3,022

**BSW Holdings**

BSW Holdings and certain of its affiliates issue and secure debt under a Master Indenture of Trust and Security Agreement, dated as of February 1, 2014, as supplemented and amended (the “Master Indenture”), among BSW Holdings, the affiliates from time to time obligated thereunder (the “Obligated Affiliates”), and The Bank of New York Mellon Trust Company, National Association, as trustee. The following entities are currently Obligated Affiliates: BSW Holdings, BSW Health, BHCS, SWH, BUMC, SWMH, Baylor All Saints Medical Center, a Texas nonprofit corporation, Baylor Medical Centers at Garland and McKinney, Baylor Regional Medical Center at Grapevine, a Texas nonprofit corporation, Baylor Medical Center at Waxahachie, a Texas nonprofit corporation, Baylor Regional Medical Center at Plano, a Texas nonprofit corporation, Scott & White Hospital – College Station (College Station), a Texas nonprofit corporation, Scott & White Clinic, a Texas nonprofit corporation, Scott & White Hospital – Round Rock, a Texas nonprofit corporation, Scott & White Continuing Care Hospital, a Texas nonprofit corporation, and Hillcrest Baptist Medical Center, a Texas nonprofit corporation. BSW Holdings is currently the Combined Group Representative under the Master Indenture.

BSW Holdings maintained a \$400 million revolving line of credit with an expiration date of January 2020. Under that line of credit, BSW Holdings could borrow at variable rates. In September 2019, the balance of \$79 million was paid off with operating cash. Effective January 2020, BSWH entered into a new \$400 million line of credit with an expiration date of January 2023. BSWH drew \$400 million on the line of credit in April 2020, which remains the balance as of June 30, 2020.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

In April and May 2015, BSW Holdings issued the \$550 million Series 2015 Taxable Bonds and the \$177 million Series 2015A Revenue Bonds (collectively, the “BSW Holdings Series 2015 Bonds”). Proceeds of the BSW Holdings Series 2015 Bonds were used to advance refund approximately \$407 million of the outstanding principal of the SWH Series 2008A and BHCS Series 2009 Bonds and to partially advance refund the SWH Series 2010 Bonds. Upon issuance of the BSW Holdings Series 2015 Bonds, \$271 million of the SWH Series 2010 bonds remained outstanding. Remaining proceeds of the BSW Holdings Series 2015 Bonds were used to fund development and construction costs of various expansion and construction projects, pay costs of issuance, and provide for any eligible corporate purpose.

In December 2015, BSW Holdings placed the \$45 million Series 2015B, \$86 million Series 2015C, and \$44 million Series 2015D Revenue Bonds (the “BSW Holdings Series 2015B, C, and D Bonds”) with various banks. Proceeds of the BSW Holdings Series 2015B, C and D Bonds were used to refinance the following variable rate demand bonds issued via the Tarrant County Cultural Education Facilities Corporation (TCCEFC) conduit issuer: Hospital Revenue Bonds (Scott and White Memorial Hospital and Scott, Sherwood and Brindley Foundation Project) Series 2008-1, Hospital Revenue Bonds (Baylor Health Care System Project) Series 2011D, and Hospital Revenue Bonds (Baylor Health Care System Project) Series 2011E (collectively, the “Refinanced VRDBs”) with an aggregate outstanding balance of \$175 million. In conjunction with redemption of the Refinanced VRDBs, three supporting direct-pay letters of credit were terminated: two with Wells Fargo Bank, N.A. and one with J.P. Morgan Bank, N.A.

In April 2016, BSW Holdings issued the \$535 million Series 2016 Taxable Bonds (the “BSW Holdings Series 2016 Bonds”). Proceeds were used to pay off a \$250 million bridge facility and costs of issuance. The remaining BSW Holdings Series 2016 Bonds proceeds were used for eligible corporate purposes.

Additionally, in April 2016, BSW Holdings issued the \$373 million Series 2016A Revenue Bonds through TCCEFC. Proceeds from the BSW Holdings Series 2016A Bonds were used to completely advance refund \$267 million of the outstanding par value of the TCCEFC Hospital Revenue Bonds (Scott & White Healthcare Project) Series 2010 Revenue Bonds plus accrued interest. In connection with the defeasance of the SWH Series 2010 Revenue Bonds, the Obligated Affiliates’ revenue pledge under the Master Indenture was released as provided in such document. As a result, no collateral secures the debt and swap obligations issued by the Obligated Affiliates under the Master Indenture. The remaining BSW Holdings Series 2016A Bonds proceeds were used for various tax-exempt project expenditures and to pay costs of issuance.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

In September 2017, BSW Holdings created a taxable commercial paper program (“BSW Holdings CP Program”). The BSW Holdings CP Program allows for the issuance of up to \$400 million of commercial paper notes, of which an aggregate amount of \$188 million was issued in September 2017. Additionally, in September 2017 BSW Holdings placed the \$77 million Series 2017A, \$75 million Series 2017B, and \$44 million Series 2017C Revenue Bonds (collectively “BSW Holdings Series 2017A, B, and C Bonds”) with various banks. Proceeds from the BSW Holdings CP Program issuance and BSW Holdings Series 2017A, B, and C Bonds were used to redeem the SWH Series 2010, BHCS Series 2011F, BHCS Series 2011G, BSW Holdings Series 2015D Bonds as well as a SWH taxable loan, a SWH tax-exempt note, and a BHCS taxable loan. In November 2018, BSW Holdings issued additional commercial paper, increasing the amount outstanding under the BSW Holdings CP Program by \$20 million to an undiscounted total of \$208 million. Proceeds of the additional commercial paper issuance were used to redeem the outstanding BHCS Series 2000 Auction Rate Securities in full.

In December 2019, BSW Holdings issued the \$41 million Series 2019A, \$97 million Series 2019B, \$180 million Series 2019C, \$45 million Series D, and \$96 million Series E Revenue Bonds (collectively “BSW Holdings Series 2019A, B, C, D and E”) through TCCEFC with various banks. Proceeds from this issuance were used to defease \$38 million of the BHCS 2011A and redeem the SWH 2013C, BSW Holdings 2015B and 2015C, BSW Holdings Series 2017A, 2017B and 2017C bonds.

### **BHCS**

In June 2011, BHCS issued the Series 2011A, B, C, D, E, F, and G Revenue Bonds (“BHCS Series 2011 Bonds”) in the aggregate amount of \$359 million through TCCEFC. Proceeds from the BHCS Series 2011 Bonds were used to repay \$75 million in borrowings under the taxable revolving line of credit and refund \$150 million of the Series 2006B and 2006C Revenue Bonds. The remaining BHCS Series 2011 Bonds proceeds were used for various project expenditures and to pay cost of issuance.

The BHCS Series 2011 Bonds issuance included \$50 million of Window Variable Rate Demand Bonds. These bonds are subject to long-term amortization periods and may be put to BHCS at the option of the bondholders in connection with certain remarketing arrangements. To the extent the bondholders may, under the terms of the debt, put their bonds within 12 months after June 30, 2020 and 2019, the principal amount of such bonds has been classified as a current obligation in the accompanying combined balance sheets. Although management believes the likelihood to be remote, management has taken steps to provide various sources of liquidity in the event any bonds were to be put back to BHCS.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

In April 2013, BHCS issued the Series 2013A and B Hospital Revenue Bonds and Series 2013C Taxable Hospital Revenue Bonds (“BHCS Series 2013 Bonds”) through the TCCEFC in the aggregate amount of \$277 million. Proceeds from the BHCS Series 2013 Bonds were used to repay \$112 million in borrowings under a taxable revolving line of credit. The remaining bond proceeds were used for various project expenditures and to pay cost of issuance. The BHCS Series 2013 Bonds issuance included \$45 million of Window Variable Rate Demand Bonds. These bonds are subject to long-term amortization and may be put to BHCS at the option of the bondholders in connection with certain remarketing arrangements. To the extent the bondholders may, under the terms of the debt, put their bonds within 12 months after June 30, 2020 and 2019, the principal amount of such bonds has been classified as a current obligation in the accompanying combined balance sheets. Although management believes the likelihood to be remote, management has taken steps to provide various sources of liquidity in the event any bonds were to be put back to BHCS.

### **SWH**

In March 2013, SWH issued Series 2013A, B, and C Revenue Bonds (“SWH Series 2013 Bonds”) with an aggregate principal of \$354 million through TCCEFC. Proceeds of the SWH Series 2013 Bonds were used to refund the Hillcrest 2006A Revenue Bonds and the SWH Series 2008-2 Bonds. The remaining SWH Series 2013 Bonds proceeds were used for various project expenditures and to pay cost of issuance.

### **FINANCE LEASES**

The System's finance lease costs for the year ended June 30, 2020 included approximately \$23 million in interest and approximately \$16 million of depreciation of financed property and equipment. The weighted-average remaining lease term for finance leases is 16.9 years and weighted average discount rate is 6.4% as of June 30, 2020. Renewal options are typically negotiated for real estate leases, most commonly for one or more renewal option terms of five to ten years each. With only one exception, renewal options on finance leases are not considered reasonably certain to be exercised and are not included in financed asset and liability calculations. Interest rates on finance leases range from 1 to 16 percent.

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

For the year ended June 30, 2020, supplemental cash flow information related to finance leases was as follows:

Operating cash flows from finance leases	\$	23
Financing cash flows from finance leases		91
Property and equipment acquired under finance leases		3

Future maturities of long-term debt and finance lease obligations as of June 30, 2020, are shown below (in millions):

	Long-Term Debt	Finance Lease Obligations	Total
2021	\$ 389	\$ 34	\$ 423
2022	90	34	124
2023	437	32	469
2024	36	33	69
2025	40	33	73
Thereafter	2,329	286	2,615
	3,321	452	3,773
Less imputed interest	—	153	153
	<u>\$ 3,321</u>	<u>\$ 299</u>	<u>\$ 3,620</u>

**8. INTEREST RATE SWAPS**

Effective July 30, 2014, BSWH consolidated its separate International Swaps and Derivatives Association (ISDA) agreements with Goldman Sachs Bank USA (Goldman) and related swap portfolios at BHCS and SWH under a single BSW Holdings ISDA. Upon completion of the BSW Holdings ISDA, BHCS and SWH swaps with Goldman were novated to the new BSW Holdings ISDA in an aggregate notional amount of \$250 million.

Effective August 29, 2014, SWH novated a portion (cash flows through August 15, 2022) of two swaps with JP Morgan to Wells Fargo. The residual remaining cash flows (from September 15, 2022 through August 15, 2045) remain at JP Morgan under the SWH ISDA.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

Effective October 23, 2014, BHCS novated the two SWH swaps with Wells Fargo (originally novated from JP Morgan to Wells Fargo on August 29, 2014) from the SWH ISDA to the BHCS ISDA. Concurrent with this novation, the Wells Fargo collateral thresholds under the BHCS Credit Support Annex were increased to accommodate the novated swaps.

Effective November 15, 2016, BSW Holdings, BHCS, and SWH entered into a swap novation transaction that novated two swaps previously between BHCS and Deutsche Bank, N.A. and two swaps previously between SWH and Deutsche Bank, N.A. such that all four swaps are now between BSW Holdings and Citibank, N.A. under the BSW Holding ISDA.

At June 30, 2020, BSW Holdings, SWH and BHCS (collectively, the “BSWH Swap Entities”) had twenty interest rate swap agreements with a total notional amount of \$898 million comprised of \$ 414 million in notional fixed payer swaps held by BSW Holdings, \$289 million in notional fixed payer swaps held by BHCS, and \$195 million in fixed payer swaps held by SWH.

Net settlements on interest rate swap agreements totaled \$23 million and \$18 million for the years ended June 30, 2020 and 2019, respectively. Net settlements and the change in fair value on interest rate swap agreements are reported in interest rate swap activity in the nonoperating section of the accompanying combined statements of operations and changes in net assets. The fair value of interest rate swap agreements is reported in other long-term liabilities on the accompanying combined balance sheets. The change in the fair value of interest rate swap agreements was an unrealized loss of approximately \$129 million and \$70 million for the fiscal years ended June 30, 2020 and 2019, respectively.

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## BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

Notes to Combined Financial Statements - continued

The following table summarizes the fair value of interest rate swaps by counterparty as of June 30, 2020 and 2019 (in millions):

	Notional* Amount	Fair Value	
		2020	2019
Bank of America, N.A.	\$ 67	\$ (42)	\$ (28)
Citibank, N.A.	178	(95)	(67)
Goldman Sachs Bank, USA	235	(130)	(91)
JP Morgan	139	(69)	(45)
Wells Fargo Bank, N.A.	279	(93)	(70)
Total interest rate swap liability	898	(429)	(301)
Less interest rate swap collateral	—	64	27
Total interest rate swap liability, net	<u>\$ 898</u>	<u>\$ (365)</u>	<u>\$ (274)</u>

\*Notional amount is the face value of a financial instrument used in the calculation of interest.

### 9. NET PATIENT CARE REVENUE

Net patient care revenue generally relates to contracts with patients, in which the performance obligation is to provide healthcare services. The contractual relationship with patients typically involves a third-party payor. The System has agreements with third-party payors that provide for payments to the System at amounts different from the System's established rates, which are explicit price concessions. The transaction prices for services provided are dependent upon the terms provided by, or negotiated with, third-party payors. Payment arrangements include prospectively determined rates per case, reimbursed costs, discounted charges, and per diem payments. The System offers discounts to uninsured patients, which are also explicit price concessions. Implicit price concessions relate primarily to uninsured patients and patient copays, co-insurance, and deductibles, and are estimated using historical collection data. Net patient care revenue (exclusive of charity care - see Note 10) is recognized as performance obligations are satisfied and reported at the amounts that reflect the consideration that the System expects to be entitled in exchange for providing patient care.

Generally, performance obligations satisfied over time relate to inpatient acute care services from the time of admission to discharge. Performance obligations satisfied at a point in time relate to outpatient services at the time the services are provided. Because performance obligations relate

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

to contracts with a duration of less than one year, the System has elected to apply the optional exemption provided in ASC 606. Therefore, the System is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially satisfied at fiscal year end. Unsatisfied or partially satisfied performance obligations primarily relate to inpatients (i.e., inhouse patients at year end) in which the patients are generally discharged within days or weeks of fiscal year end.

Settlements with third-party payors for retroactive revenue adjustments due to audits, reviews, or investigations are considered variable consideration, and are included in the determination of the estimated transaction price for providing patient care using the most likely outcome method. These settlements are estimated in the period the related services are rendered and adjusted in future periods based on contract terms, correspondence with payors, and historical settlement activity. Estimates include an assessment to ensure that it is probable that a significant reversal in the amount of revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as new information becomes available.

Federal regulations require submission of annual cost reports covering medical costs and expenses associated with services provided to program beneficiaries. Medicare and Medicaid cost report settlements are estimated in the period services are provided to beneficiaries. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, there is a reasonable possibility that recorded estimates may change by a material amount, as interpretations are clarified and cost reports are settled. These initial estimates are revised as needed until the final cost report is settled. Net patient care revenue from the Medicare and Medicaid programs increased approximately \$12 million and \$16 million for the years ended June 30, 2020 and 2019, respectively, due to changes in previously estimated amounts due to Medicare and Medicaid, as a result of changes in regulations, and final settlement of numerous cost reports.

Net patient care revenue from the Medicare and Medicaid programs accounted for approximately 40% and 38% of total net patient care revenue for the years ended June 30, 2020 and 2019, respectively. Net patient care revenue from managed care contracts accounted for approximately 57% and 60% of total net patient care revenue for the years ended June 30, 2020 and 2019, respectively. Net patient care revenue from other payors accounted for approximately 3% and 2% of total net patient care revenue for the years ended June 30, 2020 and 2019, respectively.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

The estimated amount of net patient care revenue, net of all price concessions for the years ended June 30, 2020 and 2019, disaggregated by major service line, is as follows (in millions):

	2020	2019
Inpatient	\$ 3,357	\$ 3,252
Outpatient	4,977	5,195
Total	\$ 8,334	\$ 8,447

Charity Care Access

Since 2007 BSWH hospitals in North Texas have voluntarily participated in non-profit, indigent care corporations (established by the BSWH hospitals and other private hospitals) in order to improve access to and the quality of health care for indigent patients in the community. These non-profit, indigent care corporations, the Dallas County Indigent Care Corporation (DCICC) and the Tarrant County Indigent Care Corporation (TCICC), have arranged for the provision of health care services to indigent patients in the hospitals' respective communities under various services agreements, with the compensation methodology set in advance, and such total compensation being consistent with fair market value and commercially reasonable for the services performed as determined by an independent expert analysis. These DCICC and TCICC services agreements expired or were effectively terminated in September 2017. As a result, for the years ended June 30, 2020 and 2019, BSWH hospitals did not provide any funds to DCICC or TCICC for professional health care and related services furnished to and for the benefit of indigent patients receiving services under these services agreements, which amounts were previously recorded as other operating expenses in the combined statements of operations and changes in net assets. On June 1, 2018, DCICC began providing limited dialysis and related services for indigent patients in the community through two contracts that support unmet community needs.

BSWH hospitals in Central Texas also voluntarily participate in nonprofit, indigent care corporations (established by the Scott & White hospitals and other private hospitals) in order to improve access to and the quality of health care for indigent patients. These nonprofit, indigent care corporations arrange for the provision of health care services to indigent patients under certain services agreements, with the compensation methodology set in advance, and such total compensation being consistent with fair market value and commercially reasonable for the services performed. The total expenditures related to these programs were approximately \$1 million and \$6 million for the years ended June 30, 2020, and 2019, respectively, and are

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

included in other operating expenses in the combined statements of operations and changes in net assets. These programs are being wound down.

### Section 1115 Waiver Program

In December 2011, the Centers for Medicare & Medicaid Services (CMS) approved the Texas Health and Human Services Commission's (THHSC) request for a Section 1115 waiver (Waiver Program) replacing Upper Payment Limit funding with new supplemental payment methodology, coupled with allowing managed care expansion to additional areas of the State. CMS initially approved the Waiver Program for the time period December 12, 2011, through September 30, 2016. Subsequently, CMS approved two extensions of the Waiver Program through September 30, 2022. The current Waiver Program is entitled the "Texas Healthcare Transformation and Quality Improvement Program." The Waiver Program provides for two pools of Medicaid supplemental funding – an uncompensated care (UC) pool and a delivery system reform incentive pool (DSRIP). UC pool payments are intended to improve access to and the quality of health care for patients as served under a Regional Healthcare Partnership (RHP). DSRIP pool payments are incentive payments to hospitals and other providers that develop programs or strategies (approved by CMS) to enhance access to health care and to improve the quality of care, the cost-effectiveness of care provided, and the health of the patients and families served. A provider's eligibility to receive UC pool payments and/or DSRIP pool payments requires participation in a RHP and affiliation with a local governmental entity.

During the years ended June 30, 2020 and 2019, certain BSWH hospitals (legacy Baylor Health Care System (BHCS) hospitals except as otherwise noted herein) participated in the Waiver Program.

During the years ended June 30, 2020 and 2019, BHCS (on behalf of Baylor University Medical Center, Baylor Medical Center at Irving d/b/a Baylor Scott & White Medical Center – Irving, and Baylor Scott & White Medical Center – Carrollton) (effective March 1, 2020, Baylor Scott & White Medical Center – Carrollton ceased operations), Baylor Heart and Vascular Center, LLP d/b/a Baylor Jack and Jane Hamilton Heart and Vascular Hospital, BT Garland JV, LLP d/b/a Baylor Scott & White Medical Center – Garland (on February 28, 2018, this hospital ceased operations), BT East Dallas JV, LLP d/b/a Baylor Scott & White Medical Center – White Rock, and Texas Regional Medical Center, LLC d/b/a Baylor Scott & White Medical Center – Sunnyvale were parties to the Amended and Restated Dallas and Neighboring Counties Indigent Care Affiliation Agreement with the Dallas County Hospital District d/b/a Parkland Health & Hospital System (Dallas Affiliation Agreement) and participated in RHP Nine and the Waiver Program.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

During the years ended June 30, 2020 and 2019, Baylor Scott & White All Saints Medical Center – Fort Worth and Baylor Regional Medical Center at Grapevine d/b/a Baylor Scott & White Medical Center – Grapevine were parties to the Tarrant County Regional Healthcare Partnership Affiliation Agreement with the Tarrant County Hospital District d/b/a JPS Health Network (Tarrant Affiliation Agreement) and participated in RHP Ten and the Waiver Program.

As recipients of Waiver Program payments, these BSWH hospitals are subject to extensive federal and state laws, regulations, conditions of participation, and certification requirements.

For the years ended June 30, 2020 and 2019, as a result of their participation in the Waiver Program, these BSWH hospitals (as parties to the Dallas Affiliation Agreement and Tarrant Affiliation Agreement) achieved required metrics, recorded as other receivables in the accompanying combined balance sheets, and received Waiver Program payments (DSRIP payments and UC funds) totaling approximately \$131 million and \$136 million, respectively, which amounts are Medicaid supplemental payments and recognized as net patient care revenue in the combined statements of operations and changes in net assets.

BSWH hospitals in North Texas incurred expenditures of approximately \$13 million for the years ended June 30, 2020 and 2019, in the operation and maintenance of the hospital's DSRIP projects approved under the 1115 Waiver Program, which are recorded as other operating expenses in the combined statements of operations and changes in net assets.

In a September 30, 2014, letter to THHSC, CMS announced that it was deferring the federal share (Federal Financial Participation (FFP)) of Waiver Program UC payments to private hospitals in certain counties, including those that were parties to the Dallas Affiliation Agreement and the Tarrant Affiliation Agreement during the third quarter of federal fiscal year 2014. The initial total amount of the deferral was \$74,891,536 in FFP for Waiver Program UC payments made during the third quarter of federal fiscal year 2014 to private hospitals in Dallas, Tarrant, and Nueces Counties (\$47,403,926 of which was attributable to private hospitals in Dallas and Tarrant Counties). Medicaid supplemental payments to certain BSWH hospitals were subject to the deferral. CMS indicated that it would review various funding arrangements under the Waiver Program to ensure that the arrangements complied with applicable federal requirements. CMS ultimately released this deferral, which allowed for the continuation of UC payments subject to CMS's continuing review.

In a letter dated September 1, 2016, to THHSC, CMS announced that it was disallowing \$26,844,551 in FFP as reported on the CMS-64 form for the quarter ending December 31, 2015. The disallowed amount was based on the projected value of purported in-kind donations to the Dallas County Hospital District and the Tarrant County Hospital District by DCICC and TCICC,

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

respectively, during the fourth quarter of 2015. CMS alleges that these Medicaid payments failed to comply with the federal provider-related donation requirements. The services agreements that were the subject of the disallowance expired or were effectively terminated on September 30, 2017. BSWH hospitals and affiliated hospitals subject to the disallowance are: (i) BHCS (on behalf of Baylor University Medical Center, Baylor Medical Center at Irving (now Baylor Medical Center at Irving d/b/a Baylor Scott & White Medical Center – Irving), Baylor Medical Center at Carrollton (subsequently renamed Baylor Scott & White Medical Center – Carrollton and effective March 1, 2020, this hospital ceased operations), and Baylor Medical Centers at Garland and McKinney d/b/a Baylor Medical Center at Garland) (effective January 1, 2016, this hospital was replaced by BT Garland JV, LLP d/b/a Baylor Scott & White Medical Center – Garland; on February 28, 2018, this hospital ceased operations); (ii) Baylor Heart and Vascular Center, LLP d/b/a Baylor Jack and Jane Hamilton Heart and Vascular Hospital; (iii) Baylor All Saints Medical Center (now Baylor Scott & White All Saints Medical Center – Fort Worth); (iv) Baylor Regional Medical Center at Grapevine (now Baylor Regional Medical Center at Grapevine d/b/a Baylor Scott & White Medical Center – Grapevine); and (v) and Baylor Medical Center at Waxahachie (now Baylor Scott & White Medical Center – Waxahachie). THHSC requested reconsideration of the disallowance, which request was denied. THHSC then appealed the disallowance to the Department of Health and Human Services' Departmental Appeals Board – Appellate Division (DAB or Board). BHCS (on behalf of the BSWH hospitals participating in the Dallas and Tarrant County Affiliations) and certain other private hospital systems were intervenors in the DAB litigation and requested the Board to reverse CMS's disallowance. In August 2018, the DAB upheld CMS's disallowance, but reduced the disallowed amount to \$25,276,116. THHSC and the intervenor hospitals, including BHCS, filed with the Board a joint motion for reconsideration and reversal of the DAB decision, which motion was denied. In the meantime, CMS issued a formal negative grant award, seeking recoupment from THHSC as a result of the disallowance. THHSC, in turn, requested that the private hospitals remit payment to satisfy CMS's demand. BHCS returned its approximately 40 percent share (based on payment amounts received in the fourth quarter of 2015) of the total disallowed amount of \$25,276,116 – and the other private hospitals returned their respective percentage shares of the total disallowed amount as well. On December 2, 2019, HHSC filed a complaint in the United States District Court for the Northern District of Texas, Dallas Division, requesting the court to set aside and reverse the DAB decision affirming the disallowance. On December 18, 2019, the private hospitals, including BHCS, filed a motion to intervene in HHSC's lawsuit against Secretary Azar and the U.S. Department of Health and Human Services. On March 5, 2020, the motion to intervene was granted and the private hospitals' complaint in intervention was filed. The lawsuit is ongoing.

At this time, management cannot predict the ultimate outcome of the dispute or its possible financial impact on BSWH hospitals.

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

The Texas Legislature approved legislation effective in May 2017, amending the Texas Health & Safety Code to enable the Dallas County Hospital District to create and operate a Local Provider Participation Fund program (LPPF) that would require mandatory payments by all hospitals in the county based upon net patient revenue and the option of using the mandatory payment revenue as the non-federal share of supplemental Medicaid payments. The Dallas County Hospital District's board of managers subsequently authorized creation of a LPPF in Dallas County and chose to utilize mandatory payment revenue as the non-federal share of Medicaid payments under the Waiver Program. BSWH hospitals that are parties to the Dallas Affiliation Agreement are eligible to receive supplemental payments funded through the LPPF program. Effective July 20, 2017, BSWH (on behalf of Baylor Medical Center at Waxahachie d/b/a Baylor Scott & White Medical Center -Waxahachie, Baylor Medical Centers at Garland and McKinney d/b/a Baylor Scott & White Medical Center – McKinney, Baylor Regional Medical Center at Plano d/b/a Baylor Scott & White Medical Center – Plano), BT East Dallas JV, LLP, d/b/a Baylor Scott & White Medical Center – Centennial, and Lake Pointe Operating Company, LLC, d/b/a Baylor Scott & White Medical Center – Lake Pointe entered into an Indigent Care Affiliation Agreement with the Dallas County Hospital District for purposes of participating in the LPPF program in Dallas County and being eligible to receive Medicaid supplemental payments. Also effective July 20, 2017, Texas Heart Hospital of the Southwest, L.L.P., d/b/a The Heart Hospital Baylor Plano and THHBP Management Company, L.L.C., d/b/a The Heart Hospital Baylor Denton entered into an Indigent Care Affiliation Agreement with the Dallas County Hospital District for purposes of participating in the LPPF program in Dallas County and being eligible to receive Medicaid supplemental payments.

The Texas Legislature approved legislation effective in June 2017, amending the Texas Health & Safety Code to enable the Tarrant County Hospital District to create and operate a health care provider participation program that would require mandatory payments by all hospitals in the county based upon net patient revenue and the option of using the mandatory payment revenue as the non-federal share of Medicaid payments. The Tarrant County Hospital District's board of managers subsequently authorized creation of a LPPF in Tarrant County and chose to utilize mandatory payment revenue as the non-federal share of Medicaid payments under the Waiver Program. BSWH hospitals that are parties to the Tarrant County Affiliation Agreement are eligible to receive supplemental payments funded through the LPPF program.

Effective June 2019, the Texas Legislature approved legislation amending the Texas Health & Safety Code to enable Ellis County to create and operate a health care provider participation program that would require mandatory payments by all hospitals in the county based upon net patient revenue and the option of using the mandatory payment revenue as the non-federal share of Medicaid payments. The Ellis County Commissioners Court subsequently authorized creation of a LPPF in Ellis County and chose to utilize mandatory payment revenue as the non-federal

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

share of Medicaid payments under the Waiver Program. Baylor Medical Center at Waxahachie d/b/a Baylor Scott & White Medical Center -Waxahachie is a party to the Ellis County Affiliation Agreement and is eligible to receive supplemental payments funded through the LPPF program.

BSWH hospitals in North Texas incurred expenditures of approximately \$31 million and \$55 million for the years ended June 30, 2020 and 2019, respectively, through the hospital's participation in the various LPPF programs discussed above.

During the years ended June 30, 2020 and 2019, certain BSWH hospitals (from legacy Scott & White Healthcare) participated in the Waiver Program.

Scott & White Memorial Hospital is a party to an Indigent Care Affiliation agreement with Bell County and under this agreement participates in RHP Eight and the Waiver Program.

Hillcrest Baptist Medical Center, Scott & White Hospital - Round Rock, Scott & White Hospital – Taylor, Scott & White Hospital – Marble Falls and Baylor Medical Center at Waxahachie are parties to the Indigent Care Affiliation Agreements with McLennan County and under these agreements participate in RHP Sixteen and the Waiver Program.

Scott & White Hospital - Round Rock, Scott & White Hospital – Taylor, Scott & White Hospital – Llano and Scott & White Hospital – Marble Falls are parties to Indigent Care Affiliation Agreements with Williamson County and under these agreements participate in RHP Eight and the Waiver Program.

Scott & White Hospital Brenham is a party to an Indigent Care Affiliation Agreement with Washington County and under this agreement participates in RHP Seventeen and the Waiver Program.

Scott & White Hospital - Llano is a party to an Indigent Care Affiliation Agreement with Llano and under this agreement participates in RHP Eight and the Waiver Program.

Scott & White Memorial Hospital, Scott & White Hospital – College Station, and Hillcrest Baptist Medical Center participate in LPPF programs in Bell, Brazos, and McLennan Counties respectively pursuant to legislation enacted into law by the Texas Legislature. The bills amended the Texas Health & Safety Code to create health care provider participation programs that would require mandatory payments by all hospitals in the counties based upon net revenue and the option of using the mandatory payment revenue as the non-federal share of Medicaid payments. Bell, Brazos and McLennan Counties authorized creation of LPPF programs in the respective counties and chose to utilize mandatory payment revenue as the non-federal share of Medicaid

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

payments. Scott & White Memorial Hospital, Scott & White Hospital – College Station, and Hillcrest Baptist Medical Center are eligible to receive Medicaid payments as a result of their participation in these LPPF programs. Baylor Medical Center at Waxahachie d/b/a Baylor Scott & White Medical Center -Waxahachie, Scott & White Hospital - Round Rock, Scott & White Hospital - Marble Falls, Scott & White Hospital – Taylor, and Scott & White Hospital - Llano are also affiliated with Brazos and McLennan Counties and are eligible to receive Medicaid payments under the McLennan County LPPF program.

BSWH hospitals in Central Texas incurred expenditures of approximately \$37 million and \$64 million for the years ended June 30, 2020 and 2019, respectively, through the hospital's participation in the various LPPF programs discussed above.

As recipients of Waiver Program payments, these BSWH hospitals are subject to extensive federal and state laws, regulations, conditions of participation, and certification requirements.

BSWH hospitals in Central Texas incurred expenditures of approximately \$4 million and \$2 million for the years ended June 30, 2020 and 2019, respectively, in the operation and maintenance of the hospital's DSRIP projects approved under the 1115 Waiver Program, which are recorded as other operating expenses in the combined statements of operations and changes in net assets.

For the years ended June 30, 2020 and 2019, BSWH hospitals in Central Texas achieved required metrics, recorded as other receivables in the accompanying combined balance sheets, and received Waiver Program payments totaling approximately \$118 million and \$108 million, respectively, which amounts are Medicaid supplement payments and recognized as net patient care revenue in the combined statements of operations and changes in net assets.

### **10. CHARITY CARE**

BSWH provides care to patients who lack financial resources and are deemed medically or financially indigent. Because BSWH does not pursue collection of amounts determined to qualify as charity care, these amounts have been removed from net patient care revenue. The estimated direct and indirect cost of providing these services, calculated using the ratio of patient care cost to charges, was approximately \$344 million and \$310 million for the years ended June 30, 2020 and 2019, respectively. The ratio of cost to charges is an estimate calculated based on total expenses, less non-patient care activities and other community benefit expenses, divided by gross patient care charges. In addition, BSWH provides services through government-sponsored indigent health care programs to other indigent patients.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

BSWH also commits time and resources to endeavors and critical services which meet otherwise unfulfilled community needs. Many of these activities are entered into with the understanding that they will not be self-supporting or financially viable. The expenditures for medical research activities and direct medical education are reported in Note 12.

## **11. RETIREMENT BENEFITS**

ASC 715, “*Compensation - Retirement Benefits*,” requires the System to recognize the unfunded status (i.e., the difference between the fair value of plan assets and the benefit obligation) of its defined benefit pension and other postretirement benefit plans in the accompanying combined balance sheets with a corresponding adjustment to net assets without donor restrictions. The net unrecognized actuarial losses and unrecognized prior service benefits are recognized as a component of future net periodic cost pursuant to the System’s policy for amortizing such amounts. Further, actuarial gains and losses that arise in subsequent periods are not recognized as net periodic pension cost in the same periods and are recognized as other changes in net assets without donor restrictions. Those amounts are recognized as a component of net periodic cost.

The System provides 401(k) defined contribution plans for eligible employees. Employees are eligible to contribute to the plans immediately with no minimum service or age requirement. The System’s contributions to the 401(k) plans totaled approximately \$119 million and \$110 million for the years ended June 30, 2020 and 2019, respectively, and are included in salaries, wages, and employee benefits in the accompanying combined statements of operations and changes in net assets.

BHCS and six of its affiliated hospitals provided a defined benefit plan, the Baylor Health Care System Retirement Security Plan (the “BEST Plan”), for employees, which was discontinued on January 1, 1984. All BEST Plan assets were invested in cash and cash equivalents at June 30, 2020 and 2019.

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

The following table sets forth the benefit obligations, plan assets, and funded status of the BEST Plan as of June 30, 2020 and 2019 (in millions):

	2020	2019
Fair value of plan assets	\$ 2	\$ 2
Benefit obligation	(19)	(18)
Unfunded benefit obligation	\$ (17)	\$ (16)

All Saints Health System provided a defined benefit plan, the All Saints Health System Pension Plan (the "All Saints Plan"), for employees of All Saints, which was frozen to future benefit accruals as of January 1, 2002, with the All Saints Health System purchase by BHCS. Effective December 31, 2016, the All Saints Plan was merged into the Texas Hospital Association Retirement Plan for King's Daughters (the "King's Daughters Plan").

King's Daughters Hospital provided a defined benefit plan, the King's Daughters Plan, for employees of King's Daughters Hospital, which was frozen to future benefit accruals as of March 31, 2009, with the King's Daughters Hospital purchase by Scott & White. Effective March 31, 2017, the King's Daughters Plan was merged into the Texas Hospital Association Defined Benefit Retirement Plan for Scott & White Hospital-Brenham (the "Brenham Plan").

Scott & White Hospital-Brenham provided a defined benefit plan, the Brenham Plan, for employees of Scott & White Hospital-Brenham, which was frozen to future benefit accruals as of June 30, 2010, with the Brenham Hospital purchase by Scott & White. Effective March 31, 2017, the Brenham Plan was renamed the Baylor Scott & White Health Consolidated Frozen Benefit Plan (the "BSWH Plan").

The following table sets forth the benefit obligations, plan assets, and funded status of the BSWH Plan as of June 30, 2020 and 2019 (in millions):

	2020	2019
Fair value of plan assets	\$ 70	\$ 72
Benefit obligation	(103)	(94)
Unfunded benefit obligation	\$ (33)	\$ (22)

Certain Scott & White employees participate in Scott & White's medical postretirement benefit plan. This plan provides medical and dental benefits to retirees who meet specific eligibility

# BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

## Notes to Combined Financial Statements - continued

requirements upon retirement. The plan is unfunded and requires covered retirees to contribute a portion of the cost of benefits, based on age at retirement and years of service.

Scott & White uses an incremental cost approach in estimating the annual accrued cost related to the postretirement benefit plan, which is based on estimates by independent actuaries. Such an approach is considered appropriate, since substantially all of the health care benefits are provided by Scott & White to retirees, using the Health Plan to manage the care provided.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 introduced a prescription drug benefit under Medicare (Medicare Part D), as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. Scott & White has not made the determination that the prescription drug benefit provided by its medical postretirement benefit plan is actuarially equivalent to the benefit provided by Medicare Part D. Therefore, the measures of the accumulated benefit obligation or net periodic benefit cost do not reflect any amounts associated with the federal subsidy.

The following table sets forth a reconciliation of benefit obligations, plan assets, and balance sheet position for the postretirement benefit obligation as of June 30, 2020 and 2019 (in millions):

	2020	2019
Fair value of plan assets	\$ —	\$ —
Benefit obligation	(14)	(25)
Unfunded benefit obligation	<u>\$ (14)</u>	<u>\$ (25)</u>

## 12. FUNCTIONAL EXPENSES

The System provides general health care services to residents within its geographic area. The combined financial statements report expenses that can be attributable to more than one function. These expenses require an allocation, on a reasonable basis, that is consistently applied. The System allocates expenses by function based on the nature of each business units' operations.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

Expenses related to providing these services are as follows for the years ended June 30, 2020 and 2019 (in millions):

	2020				Total
	Patient Care	Education and Research	Health Plan and Other <sup>(1)</sup>	General and Administrative	
Salaries, wages, and employee benefits	\$ 4,132	\$ 111	\$ 113	\$ 567	\$ 4,923
Supplies	1,443	2	156	100	1,701
Other operating expenses	1,309	42	139	579	2,069
Medical claims	—	—	735	—	735
Tangible and intangible asset related expenses	205	—	2	221	428
Interest	77	—	—	37	114
Total	<u>\$ 7,166</u>	<u>\$ 155</u>	<u>\$ 1,145</u>	<u>\$ 1,504</u>	<u>\$ 9,970</u>

  

	2019				Total
	Patient Care	Education and Research	Health Plan and Other <sup>(1)</sup>	General and Administrative	
Salaries, wages, and employee benefits	\$ 3,859	\$ 109	\$ 92	\$ 501	\$ 4,561
Supplies	1,429	4	127	101	1,661
Other operating expenses	1,283	58	123	542	2,006
Medical claims	—	—	556	—	556
Tangible and intangible asset related expenses	205	—	2	212	419
Interest	97	—	3	25	125
Total	<u>\$ 6,873</u>	<u>\$ 171</u>	<u>\$ 903</u>	<u>\$ 1,381</u>	<u>\$ 9,328</u>

<sup>(1)</sup> Other includes expenses related to the System's construction activities and professional office building management.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **13. NONCONTROLLING INTERESTS**

The System controls, and therefore consolidates, certain investees of its subsidiaries. The System regularly engages in the purchase and sale of noncontrolling interests in these investees that do not result in a change of control. These transactions are accounted for as equity transactions as they are undertaken among the System, its consolidated subsidiaries, and noncontrolling interests, and their cash flow effect is classified within financing activities. The System reflects noncontrolling interests in subsidiaries as either noncontrolling interests - redeemable in the mezzanine section of the accompanying combined balance sheets, or noncontrolling interests - nonredeemable in net assets in the accompanying combined balance sheets, according to ASC 810, "*Consolidation*".

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## BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

### Notes to Combined Financial Statements - continued

The activity for net assets without donor restrictions presented as attributable to BSWH and noncontrolling interests - nonredeemable for the years ended June 30, 2020 and 2019 is summarized below (in millions):

	Attributable to BSWH	Noncontrolling Interest- Nonredeemable	Total Net Assets Without Donor Restrictions
Balance, as of June 30, 2018	\$ 5,212	\$ 282	\$ 5,494
Revenue and gains in excess of expenses and losses	761	88	849
Net assets released from restrictions for capital expenditures	31	—	31
Distributions to noncontrolling interests	—	(77)	(77)
Purchases of noncontrolling interests	—	(11)	(11)
Sales of noncontrolling interests	—	2	2
Other changes in noncontrolling interests	—	(6)	(6)
Revenue and gains in excess of expenses and losses attributable to noncontrolling interests - redeemable	(274)	—	(274)
Net assets acquired	7	—	7
Other	(10)	—	(10)
Change in net assets without donor restrictions	<u>515</u>	<u>(4)</u>	<u>511</u>
Balance, as of June 30, 2019	<u>\$ 5,727</u>	<u>\$ 278</u>	<u>\$ 6,005</u>
Revenue and gains in excess of expenses and losses	360	93	453
Net assets released from restrictions for capital expenditures	45	—	45
Distributions to noncontrolling interests	—	(43)	(43)
Purchases of noncontrolling interests	—	(2)	(2)
Sales of noncontrolling interests	—	2	2
Other changes in noncontrolling interests	—	(2)	(2)
Revenue and gains in excess of expenses and losses attributable to noncontrolling interests - redeemable	(290)	—	(290)
Cumulative change in accounting principle	(2)	—	(2)
Change in net assets without donor restrictions	<u>113</u>	<u>48</u>	<u>161</u>
Balance, as of June 30, 2020	<u><u>\$ 5,840</u></u>	<u><u>\$ 326</u></u>	<u><u>\$ 6,166</u></u>

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

The activity for noncontrolling interests - redeemable for the years ended June 30, 2020 and 2019 is summarized below (in millions):

Balance, as of June 30, 2018	\$ 425
Net income attributable to noncontrolling interests - redeemable	274
Distributions to noncontrolling interests	(243)
Purchases of noncontrolling interests	(11)
Sales of noncontrolling interests	6
Noncontrolling interests of acquired entities	3
Other changes	(1)
Balance, as of June 30, 2019	<u>\$ 453</u>
Net income attributable to noncontrolling interests - redeemable	290
Distributions to noncontrolling interests	(240)
Purchases of noncontrolling interests	(22)
Sales of noncontrolling interests	5
Other changes	(4)
Balance, as of June 30, 2020	<u><u>\$ 482</u></u>

**14. ENDOWMENTS**

The System's endowments consist of donor-restricted and board-designated endowment funds for a variety of purposes. The net assets associated with endowment funds are classified and reported based on the existence or absence of donor imposed restrictions. The System has interpreted the State of Texas Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor stipulation to the contrary. As a result of this interpretation, the System classifies as donor-restricted endowments, (a) the original value of gifts donated to the donor-restricted endowment, (b) the original value of subsequent gifts to the donor-restricted endowment, and (c) accumulations to the donor-restricted endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not subject to explicit donor stipulations, is classified as net assets with donor restrictions until those amounts are appropriated for expenditure by the System in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA,

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

the System considers the following factors in making a determination to appropriate or accumulate endowment funds:

- 1) The duration and preservation of the fund
- 2) The purposes of the System 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 the System and
- 7) The investment policies of the System

Endowment fund composition by type of fund as of June 30, 2020 and 2019, is as follows (in millions):

	2020		
	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted endowment funds	\$ —	\$ 370	\$ 370
Board-designated endowment funds	23	—	23
Total endowment funds	\$ 23	\$ 370	\$ 393
	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted endowment funds	\$ 1	\$ 381	\$ 382
Board-designated endowment funds	48	—	48
Total endowment funds	\$ 49	\$ 381	\$ 430

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

Changes in endowment funds for the years ended June 30, 2020 and 2019 are as follows (in millions):

	2020		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment funds, as of June 30, 2019	\$ 49	\$ 381	\$ 430
Investment return	1	3	4
Appropriation of endowment assets for expenditure	(25)	(15)	(40)
Other	(2)	1	(1)
Endowment funds, as of June 30, 2020	<u>\$ 23</u>	<u>\$ 370</u>	<u>\$ 393</u>

  

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment funds, as of June 30, 2018	\$ 68	\$ 380	\$ 448
Investment return	3	11	14
Gifts	—	3	3
Appropriation of endowment assets for expenditure	(22)	(14)	(36)
Other	—	1	1
Endowment funds, as of June 30, 2019	<u>\$ 49</u>	<u>\$ 381</u>	<u>\$ 430</u>

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# BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

Notes to Combined Financial Statements - continued

The portion of perpetual endowment funds that is required to be retained permanently either by explicit donor stipulation or by State of Texas UPMIFA as of June 30, 2020 and 2019 is as follows (in millions):

	2020	2019
Education	\$ 51	\$ 51
Patient care	134	134
Research	75	74
General operations	2	2
Total	<u>\$ 262</u>	<u>\$ 261</u>

## Underwater Endowment Funds

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts. When donor endowment deficits exist, they are classified as a reduction of net assets with donor restrictions. Deficiencies of this nature existed in 2020 and 2019 and were less than \$1 million in total. These deficits resulted from unfavorable market fluctuations and authorized appropriation that was deemed prudent.

## Endowment Return Objectives and Risk Parameters

The System follows an investment policy that attempts to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of endowment assets. Under this policy, the return objective for the endowment assets, measured over a full market cycle, shall be to maximize the return against various indices, based on the endowment's target allocation applied to the appropriate individual benchmarks. To achieve its long-term rate of return objectives, the System relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends). The System targets a diversified asset allocation that places greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

## Relationship of Endowment Spending Practices to Investment Objectives

The System determines the appropriation of endowment funds for expenditure reimbursement through the budgeting process. Distribution policies for the System's endowments govern the amount of endowment funds that may be appropriated during this process. In establishing its

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

policies, the System considered the long-term expected return on its endowments. Accordingly, over the long-term, the System expects the current distribution policies to allow its endowments to grow at an average of the long-term rate of inflation and maintain its purchasing power. In order to maintain the purchasing power of endowment assets, expenditures are based on investment performance and spending is curbed in response to deficit situations. Over the long-term, the System expects its endowments to grow consistent with its intention to maintain the purchasing power of the endowment assets as well as to provide additional real growth through new gifts.

## **15. COMMITMENTS AND CONTINGENCIES**

### **BSWH**

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, physician ownership and self-referral, and Medicare and Medicaid fraud and abuse. The System has government activity and litigation with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the System is in compliance with applicable fraud and abuse laws and regulations as well as other applicable federal and state laws and regulations.

### **Irving**

The Irving Hospital Authority (the "Authority") entered into a Master Agreement (the "Master Agreement") with Baylor Medical Center at Irving (Irving) and BHCS, and a Lease Agreement (the "Lease Agreement") with Irving.

Under the terms of the Lease Agreement, Irving agreed to manage and lease substantially all properties of the Authority over an initial lease term of twenty years, beginning August 1, 1995, with an option to renew the lease for two additional ten year terms. An Amended and Restated Lease Agreement (the "Amended Lease Agreement") was entered into by the Authority and Irving effective April 1, 2010, to extend the lease thirty-five years through March 31, 2045, and to supersede nearly all the obligations of the original Master Agreement and Lease Agreement.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

## Notes to Combined Financial Statements - continued

The Amended Lease Agreement is accounted for as a finance lease with (a) fixed rent payments of approximately \$9 million per year, as adjusted by a September 24, 2010 amendment to the Amended Lease Agreement, plus (b) a contingent rent payment equal to 20.0% of the excess operating cash flow derived from the prior fiscal year's operations, as defined in the Amended Lease Agreement. Irving accrued approximately \$3.2 million and \$1 million at June 30, 2020 and 2019, respectively, for the contingent rent payment due to the Authority within five business days following the issuance of Irving's audited statements of operations and changes in net assets.

BHCS signed a Limited Joinder to evidence its agreement with the BHCS obligations included in the Amended Lease Agreement and to covenant that BHCS will pay the rent and the early termination fee/liquidated damages if Irving fails to pay those obligations. During the initial six year term, ending April 2016, of the Revised Lease Agreement, Irving paid BHCS a management fee, based on a percentage of the excess operating cash flow, as defined in the Revised Lease Agreement. BHCS continues to be required to contribute \$100,000 per year to Irving, to be matched by the Irving Healthcare Foundation, for community health projects, which are mutually agreed upon by BHCS and Irving. BHCS contributed \$100,000 directly to Irving in 2020 and 2019. At the end of the lease term, the leased facilities will be surrendered to the Authority. At June 30, 2020 and 2019, no liability under the Revised Lease Agreement was recorded as no amount can be reasonably estimated.

### **16. AFFILIATION AGREEMENTS**

On February 1, 2007, BHCS entered into a five year affiliation agreement (that automatically renews for additional five year terms) with 99-bed Decatur Hospital Authority d/b/a Wise Health System, located in Decatur, Texas (approximately 40 miles northwest of Fort Worth). Under the affiliation agreement, BHCS makes available certain services which include advisory services, physician recruitment, and access to continuing education programs. Purchasing and purchased services organization sponsorship are also available for an additional fee, in addition to advisory services that exceed the time and resource requirements outlined in the affiliation agreement. Wise Health System is not owned or controlled by any member of the System.

On October 1, 2008, BHCS entered into a five year affiliation agreement (that automatically renews for additional five year terms) with Glen Rose Medical Foundation d/b/a Glen Rose Medical Center, a 16-bed hospital located in Glen Rose, Texas (approximately 54 miles southwest of Fort Worth). As of March 24, 2010, the agreement was assigned to Somervell County Hospital Authority, which assumed operation of the hospital. Under the affiliation

## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### Notes to Combined Financial Statements - continued

agreement, BHCS makes available certain services which include advisory services, physician recruitment, and access to continuing education programs. Purchasing and purchased services organization sponsorship are also available for an additional fee, in addition to advisory services that exceed the time and resource requirements outlined in the affiliation agreement. Glen Rose Medical Center is not owned or controlled by any member of the System.

On January 1, 2009, BHCS entered into a five year affiliation agreement (that automatically renews for additional five year terms) with Hunt Memorial Hospital District (HMHD), which operates Hunt Medical Center at Greenville located approximately 45 miles northeast of Dallas and is a 201-bed acute care hospital. Under the affiliation agreement, both organizations remain independent, but BHCS provides certain services for a fee including advisory services, physician recruitment, and access to continuing education programs. HMHD is not owned or controlled by any member of the System. The affiliation agreement with HMHD was discontinued, effective December 31, 2018.

On December 17, 2013, BHCS entered into a five year affiliation agreement (that automatically renews for additional five year terms) with Essent PRMC LP d/b/a Paris Regional Medical Center (PRMC). PRMC is a 360-bed hospital located in Paris, Texas (approximately 105 miles northeast of Dallas). In March 2016, Apollo Global Management, LLC became the capital partner for a new entity, Regional Care Capella Health Partners (RCCH) which operates PRMC. Under the affiliation agreement, both organizations remain independent, but BHCS provides certain services for a fee including advisory services, physician recruitment, and access to continuing education programs. PRMC is not owned or controlled by any member of the System. The affiliation agreement with PRMC was discontinued, effective November 23, 2018.

On August 11, 2016, BSWH entered into a five year affiliation agreement (that automatically renews for additional five year terms) with Fairfield Hospital District. The hospital is operating as Freestone Medical Center under a management agreement with Community Hospital Corporation in Plano. Freestone Medical Center is a 25-bed hospital located in Fairfield, Texas (approximately 90 miles southeast of Dallas). The hospital also operates a rural health care clinic staffed by primary care physicians and advanced practice providers. Under the affiliation agreement, both organizations remain independent, but BSWH provides certain services for a fee including advisory services, physician recruitment/alignment, and access to continuing education programs. Freestone Medical Center is not owned or controlled by any member of the System.

# **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

Notes to Combined Financial Statements - continued

## **17. SUBSEQUENT EVENTS**

### **Provider Relief Funds Reporting Requirements**

During September and October 2020, the Department of Health and Human Services (HHS) issued updated reporting requirements significantly changing the previous guidance regarding utilization of the funds granted from the Provider Relief Funds under the CARES Act and other legislation. As a result of the updated guidance from HHS, BSWH could be required to derecognize and return a portion of the original grant income recorded, which is not expected to be material. BSWH is continuing to monitor the reporting requirements as they evolve.

### **Risk Corridor Program**

The Risk Corridor program was created as part of the Affordable Care Act to stabilize the individual product market for pricing volatility during the early years of the public health insurance exchanges from 2014 through 2016. After the program was in operation, CMS took the position that the Risk Corridor program was budget neutral, and would only pay Risk Corridor funding out to insurers that had losses based on collections from insurers that had excess profitability within the program, creating a shortfall for Scott and White Health Plan (SWHP) and Insurance Company of Scott and White (ICSW). SWHP and ICSW sued the United States to obtain recovery of funds believed to be owed through this program. The Supreme Court held oral arguments and ruled in favor of the insurers. In August 2020, SWHP and ICSW collected the full amount owed from this program, which resulted in an increase in net assets of approximately \$64 million.

The System has performed an evaluation of subsequent events through October 30, 2020, which is the date the financial statements were issued.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Supplementary Unaudited Information

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## **BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES**

### **OTHER COMMUNITY BENEFITS - UNAUDITED**

Nonprofit hospitals are required to report community benefits under the requirements of Texas Health and Safety Code Chapter 311. For Texas state law purposes, unaudited community benefits include the unreimbursed cost of charity care; the unreimbursed cost of government-sponsored indigent health care (i.e., Medicaid); the unreimbursed cost of government-sponsored health care (i.e., Medicare), medical education, medical research, and other community benefits and services. The amount of community benefits reportable for Texas state law purposes by all BSWH nonprofit hospitals totaled approximately \$769 million and \$966 million for the years ended June 30, 2020 and 2019, respectively.



## Report of Independent Auditors

To the Board of Trustees of Baylor Scott & White Holdings

We have audited the combined financial statements of Baylor Scott & White Holdings and its controlled affiliates as of and for the year ended June 30, 2020 and our report thereon appears on page one of this document. That audit was conducted for the purpose of forming an opinion on the combined financial statements taken as a whole. The combining information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the combined financial statements. The combining information has been subjected to the auditing procedures applied in the audit of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining information is fairly stated, in all material respects, in relation to the combined financial statements taken as a whole. The combining information is presented for purposes of additional analysis of the combined financial statements rather than to present the financial position, results of operations and changes in the net assets and cash flows of the individual companies and is not a required part of the combined financial statements. Accordingly, we do not express an opinion on the financial position, results of operations and changes in net assets and cash flows of the individual companies.

A handwritten signature in black ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive, flowing style.

Dallas, TX  
October 30, 2020

# BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

## Combining Balance Sheets

(Note A)

June 30, 2020

(In millions)

ASSETS	Obligated Affiliates	Consolidated Health Plan	Other System Entities	Reclassifications & Eliminations	Total Financials
<b>CURRENT ASSETS:</b>					
Cash and cash equivalents	\$ 1,344	\$ 198	\$ 423	\$ —	\$ 1,965
Short-term investments	157	49	150	—	356
THVG funds due from United Surgical Partners, Inc.	—	—	280	—	280
Accounts receivable:					
Patient	491	—	335	(45)	781
Premiums	—	118	—	—	118
Affiliates, net	127	—	—	(127)	—
Other	125	53	99	(4)	273
Other current assets	250	20	107	(1)	376
Total current assets	<u>2,494</u>	<u>438</u>	<u>1,394</u>	<u>(177)</u>	<u>4,149</u>
<b>LONG-TERM INVESTMENTS:</b>					
Unrestricted	3,458	172	464	—	4,094
Restricted	2	—	495	—	497
Total long-term investments	<u>3,460</u>	<u>172</u>	<u>959</u>	<u>—</u>	<u>4,591</u>
<b>ASSETS WHOSE USE IS LIMITED:</b>					
Other designated assets	164	2	9	—	175
Self insurance reserves	—	—	120	—	120
Total assets whose use is limited	<u>164</u>	<u>2</u>	<u>129</u>	<u>—</u>	<u>295</u>
PROPERTY AND EQUIPMENT, net	2,923	28	1,125	(14)	4,062
RIGHT OF USE OPERATING LEASE ASSETS, net <sup>(1)</sup>	364	—	746	(242)	868
CONTRIBUTIONS RECEIVABLE, net	2	—	167	—	169
DUE FROM AFFILIATES	203	—	61	(264)	—
INVESTMENTS IN SUBSIDIARIES AND AFFILIATES	2,228	—	—	(2,228)	—
<b>OTHER LONG-TERM ASSETS:</b>					
Equity investment in unconsolidated entities	42	—	21	—	63
Goodwill and intangible assets, net	86	5	784	(2)	873
Interest in net assets of related foundations	427	—	107	(530)	4
Other	12	2	7	(3)	18
Total other long-term assets	<u>567</u>	<u>7</u>	<u>919</u>	<u>(535)</u>	<u>958</u>
Total assets	<u>\$ 12,405</u>	<u>\$ 647</u>	<u>\$ 5,500</u>	<u>\$ (3,460)</u>	<u>\$ 15,092</u>

Note (A): The accompanying supplemental combining financial information was derived from the accounting records used to prepare the combined financial statements and has been presented only for purposes of additional analysis. The first column represents information for the Obligated Affiliates, which are detailed in Note 7 to the combined financial statements. The second and third column represents information for all remaining System controlled affiliates. The fourth column, "Reclassifications and Eliminations," represents all material combining entries and intracompany/intercompany eliminations. Other than as described above, the schedules of supplemental combining financial information are prepared in accordance with accounting policies described in the accompanying notes to the combined financial statements. These schedules are not intended to be a presentation in accordance with accounting principles generally accepted in the United States of America.

(1) Combining balance sheets exclude intercompany operating leases which eliminate at the System level.

# BAYLOR SCOTT & WHITE HOLDINGS AND ITS CONTROLLED AFFILIATES

## Combining Balance Sheets - continued

(Note A)

June 30, 2020

(In millions)

LIABILITIES AND NET ASSETS	Obligated Affiliates	Consolidated Health Plan	Other System Entities	Reclassifications & Eliminations	Total Financials
<b>CURRENT LIABILITIES:</b>					
Current maturities of long-term debt and finance lease obligations	\$ 65	\$ —	\$ 37	\$ —	\$ 102
Long-term debt subject to short-term remarketing arrangements	95	—	—	—	95
Commercial paper	208	—	—	—	208
Accounts payable:					
Trade accounts payable	211	11	122	—	344
Affiliates, net	—	37	90	(127)	—
Accrued liabilities:					
Payroll related	419	1	102	—	522
Third-party programs	522	4	294	28	848
Medical claims payable	—	138	—	(73)	65
Operating lease liabilities <sup>(1)</sup>	60	—	111	(16)	155
Other	327	114	190	(16)	615
Total current liabilities	<u>1,907</u>	<u>305</u>	<u>946</u>	<u>(204)</u>	<u>2,954</u>
<b>LONG-TERM DEBT AND FINANCE LEASE OBLIGATIONS, less current maturities</b>					
	2,907	—	355	—	3,262
<b>OTHER LONG-TERM LIABILITIES:</b>					
Self insurance and other insurance liabilities	—	—	120	(1)	119
Interest rate swap liabilities, net	365	—	—	—	365
Long term operating lease liabilities <sup>(1)</sup>	341	—	696	(230)	807
Other	181	15	62	(1)	257
Total other long-term liabilities	<u>887</u>	<u>15</u>	<u>878</u>	<u>(232)</u>	<u>1,548</u>
<b>DUE TO AFFILIATES</b>					
Total liabilities	<u>5,701</u>	<u>320</u>	<u>2,441</u>	<u>(698)</u>	<u>7,764</u>
<b>COMMITMENTS AND CONTINGENCIES</b>					
<b>NONCONTROLLING INTERESTS - REDEEMABLE</b>					
	—	—	354	128	482
<b>NET ASSETS:</b>					
Net assets without donor restrictions:					
Attributable to BSWH	6,244	327	1,886	(2,617)	5,840
Noncontrolling interests-nonredeemable	26	—	43	257	326
Total net assets without donor restrictions	<u>6,270</u>	<u>327</u>	<u>1,929</u>	<u>(2,360)</u>	<u>6,166</u>
Net assets with donor restrictions	434	—	776	(530)	680
Total net assets	<u>6,704</u>	<u>327</u>	<u>2,705</u>	<u>(2,890)</u>	<u>6,846</u>
Total liabilities and net assets	<u>\$ 12,405</u>	<u>\$ 647</u>	<u>\$ 5,500</u>	<u>\$ (3,460)</u>	<u>\$ 15,092</u>

Note (A): The accompanying supplemental combining financial information was derived from the accounting records used to prepare the combined financial statements and has been presented only for purposes of additional analysis. The first column represents information for the Obligated Affiliates, which are detailed in Note 7 to the combined financial statements. The second and third column represents information for all remaining System controlled affiliates. The fourth column, "Reclassifications and Eliminations," represents all material combining entries and intracompany/intercompany eliminations. Other than as described above, the schedules of supplemental combining financial information are prepared in accordance with accounting policies described in the accompanying notes to the combined financial statements. These schedules are not intended to be a presentation in accordance with accounting principles generally accepted in the United States of America.

(1) Combining balance sheets exclude intercompany operating leases which eliminate at the System level.

**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Combining Statements of Operations and Changes in Net Assets

(Note A)

For the Year Ended June 30, 2020

(In millions)

	Obligated Affiliates	Consolidated Health Plan	Other System Entities	Reclassifications & Eliminations	Total Financials
<b>OPERATING REVENUE:</b>					
Net patient care revenue	\$ 4,971	\$ —	\$ 3,864	\$ (501)	\$ 8,334
Premium revenue	—	1,483	—	—	1,483
Other operating revenue	600	30	716	(711)	635
Net assets released from restrictions for operations	6	—	87	(16)	77
Total operating revenue	<u>5,577</u>	<u>1,513</u>	<u>4,667</u>	<u>(1,228)</u>	<u>10,529</u>
<b>OPERATING EXPENSES:</b>					
Salaries, wages, and employee benefits	2,978	76	1,908	(39)	4,923
Supplies	861	—	840	—	1,701
Other operating expenses	1,286	108	1,439	(764)	2,069
Medical claims	—	1,251	—	(516)	735
(Gains) losses on fixed asset sales and disposals, net	(3)	—	2	—	(1)
Depreciation and amortization	278	3	150	(2)	429
Interest	88	—	38	(12)	114
Total operating expenses	<u>5,488</u>	<u>1,438</u>	<u>4,377</u>	<u>(1,333)</u>	<u>9,970</u>
<b>INCOME FROM OPERATIONS</b>	<u>89</u>	<u>75</u>	<u>290</u>	<u>105</u>	<u>559</u>
<b>NONOPERATING GAINS (LOSSES):</b>					
Gains (losses) on investments, net	38	13	19	(12)	58
Interest rate swap activity	(151)	—	—	—	(151)
Contributions	93	—	—	(93)	—
Loss from extinguishment of debt	(3)	—	—	—	(3)
Other	199	—	19	(218)	—
Total nonoperating gains (losses)	<u>176</u>	<u>13</u>	<u>38</u>	<u>(323)</u>	<u>(96)</u>
<b>REVENUE AND GAINS IN EXCESS (DEFICIT) OF EXPENSES AND LOSSES BEFORE INCOME TAXES</b>					
	265	88	328	(218)	463
<b>LESS INCOME TAX (BENEFIT) EXPENSE</b>	<u>(1)</u>	<u>—</u>	<u>11</u>	<u>—</u>	<u>10</u>
<b>REVENUE AND GAINS IN EXCESS (DEFICIT) OF EXPENSES AND LOSSES</b>					
	266	88	317	(218)	453

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**BAYLOR SCOTT & WHITE HOLDINGS  
AND ITS CONTROLLED AFFILIATES**

Combining Statements of Operations and Changes in Net Assets - continued  
(Note A)  
For the Year Ended June 30, 2020  
(In millions)

	Obligated Affiliates	Consolidated Health Plan	Other System Entities	Reclassifications & Eliminations	Total Financials
OTHER CHANGES IN NET ASSETS					
WITHOUT DONOR RESTRICTIONS:					
Net assets released from restrictions for capital expenditures	\$ —	\$ —	\$ 45	\$ —	\$ 45
Other changes in net assets attributable to noncontrolling interests-nonredeemable	(2)	—	(285)	242	(45)
Revenue and gains in deficit of expenses and losses attributable to noncontrolling interests - redeemable	—	—	(210)	(80)	(290)
Transfers between entities under common control	(57)	—	186	(129)	—
Cumulative change in accounting principle	1	—	(4)	1	(2)
Other	3	—	(11)	8	—
<b>INCREASE (DECREASE) IN NET ASSETS WITHOUT DONOR RESTRICTIONS</b>					
	<u>211</u>	<u>88</u>	<u>38</u>	<u>(176)</u>	<u>161</u>
CHANGES IN NET ASSETS WITH DONOR RESTRICTIONS:					
Contributions	5	—	63	(12)	56
Realized gains on investments, net	—	—	20	—	20
Unrealized losses on investments, net	—	—	(9)	—	(9)
Change in value of split-interest agreements	—	—	4	—	4
Net assets released from restrictions for operations	(6)	—	(87)	16	(77)
Net assets released from restrictions for capital expenditures	—	—	(45)	—	(45)
Change in net assets of related foundations	(68)	—	(25)	93	—
Other	8	—	(4)	—	4
<b>(DECREASE) INCREASE IN NET ASSETS WITH DONOR RESTRICTIONS</b>					
	<u>(61)</u>	<u>—</u>	<u>(83)</u>	<u>97</u>	<u>(47)</u>
<b>INCREASE (DECREASE) IN NET ASSETS</b>					
	<u>150</u>	<u>88</u>	<u>(45)</u>	<u>(79)</u>	<u>114</u>
NET ASSETS, beginning of year	<u>6,554</u>	<u>239</u>	<u>2,750</u>	<u>(2,811)</u>	<u>6,732</u>
NET ASSETS, end of year	<u>\$ 6,704</u>	<u>\$ 327</u>	<u>\$ 2,705</u>	<u>\$ (2,890)</u>	<u>\$ 6,846</u>

Note (A): The accompanying supplemental combining financial information was derived from the accounting records used to prepare the combined financial statements and has been presented only for purposes of additional analysis. The first column represents information for the Obligated Affiliates, which are detailed in Note 7 to the combined financial statements. The second and third column represents information for all remaining System controlled affiliates. The fourth column, "Reclassifications and Eliminations," represents all material combining entries and intracompany/intercompany eliminations. Other than as described above, the schedules of supplemental combining financial information are prepared in accordance with accounting policies described in the accompanying notes to the combined financial statements. These schedules are not intended to be a presentation in accordance with accounting principles generally accepted in the United States of America.