

Novant Health, Inc. and Affiliates

**Consolidated Financial Statements and
Supplemental Information
December 31, 2020 and 2019**

Novant Health, Inc. and Affiliates
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December 31, 2020 and 2019

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Report of Independent Auditors

To the Board of Trustees of
Novant Health, Inc.

We have audited the accompanying consolidated financial statements of Novant Health, Inc. and Affiliates (the "Company"), which comprise the consolidated balance sheets as of December 31, 2020 and 2019, and the related consolidated statements of operations and changes in net assets and of cash flows for the years then ended.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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 consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Novant Health, Inc. and Affiliates as of December 31, 2020 and 2019, and the results of their operations, changes in their 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 consolidated financial statements, the Company changed the manner in which it accounts for leases and the manner in which it accounts for restricted cash in 2019. Our opinion is not modified with respect to this matter.

Pricewaterhouse Coopers LLP

March 29, 2021

Novant Health, Inc. and Affiliates
Consolidated Balance Sheets
December 31, 2020 and 2019

<i>(in thousands of dollars)</i>	2020	2019
Assets		
Current assets		
Cash and cash equivalents	\$ 711,822	\$ 402,536
Accounts receivable, net	670,736	610,470
Short-term investments	330,742	195,619
Current portion of assets limited as to use	42,674	71,021
Receivable for settlement with third-party payors	25,109	16,231
Other current assets	259,254	230,875
Total current assets	2,040,337	1,526,752
Assets limited as to use	234,676	213,478
Long-term investments	2,984,671	2,507,709
Property and equipment, net	2,400,069	2,320,419
Right-of-use assets, net	493,354	493,865
Intangible assets and goodwill, net	310,047	313,974
Investments in affiliates	54,954	79,284
Deferred tax asset	5,317	6,646
Other assets	128,253	113,916
Total assets	\$ 8,651,678	\$ 7,576,043
Liabilities and Net Assets		
Current liabilities		
Current portion of long-term debt	\$ 54,848	\$ 57,119
Short-term borrowings	149,592	88,176
Accounts payable	277,310	207,414
Accrued liabilities	682,673	423,091
Current portion of operating lease liabilities	88,796	88,369
Estimated third-party payor settlements	87,982	36,362
Total current liabilities	1,341,201	900,531
Long-term debt, net of current portion	1,275,987	1,283,939
Deferred tax liability	5,194	5,223
Operating lease liabilities, net of current portion	418,011	422,326
Derivative financial instruments	51,803	43,897
Employee benefits and other liabilities	589,583	333,605
Total liabilities	3,681,779	2,989,521
Commitments and contingencies		
Net assets		
Without donor restrictions - attributable to Novant Health	4,805,811	4,420,971
Without donor restrictions - noncontrolling interests	79,252	80,819
Total net assets without donor restrictions	4,885,063	4,501,790
With donor restrictions	84,836	84,732
Total net assets	4,969,899	4,586,522
Total liabilities and net assets	\$ 8,651,678	\$ 7,576,043

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

Novant Health, Inc. and Affiliates
Consolidated Statements of Operations and Changes in Net Assets
Years Ended December 31, 2020 and 2019

<i>(in thousands of dollars)</i>	2020	2019
Operating revenues and other support		
Net patient service revenues	\$ 5,052,794	\$ 5,055,436
Other revenue	<u>629,981</u>	<u>379,509</u>
Total operating revenues and other support	<u>5,682,775</u>	<u>5,434,945</u>
Operating expenses		
Salaries and employee benefits	3,083,108	3,023,877
Supplies and other	2,073,090	1,910,059
Depreciation and amortization expense	260,051	266,233
Interest expense	<u>78,022</u>	<u>79,292</u>
Total operating expenses	<u>5,494,271</u>	<u>5,279,461</u>
Operating income	188,504	155,484
Non-operating income		
Investment income	201,823	378,547
Loss on extinguishment of debt	(6,208)	-
Income tax expense	(505)	(7,358)
Other net periodic pension costs	<u>(1,459)</u>	<u>(3,191)</u>
Excess of revenues over expenses	<u>\$ 382,155</u>	<u>\$ 523,482</u>
Other changes in net assets without donor restrictions		
Cumulative effect of change in accounting principle	-	20,589
Change in funded status of defined benefit plans	(878)	(2,233)
Unrealized gain on derivative financial instruments	3,180	3,374
Other changes in net assets without donor restrictions	<u>(1,184)</u>	<u>(4,789)</u>
Increase in net assets without donor restrictions	<u>383,273</u>	<u>540,423</u>
Net assets with donor restrictions		
Contributions and investment income	11,740	13,295
Net assets released from restrictions for operations	<u>(11,636)</u>	<u>(6,096)</u>
Increase in net assets with donor restrictions	<u>104</u>	<u>7,199</u>
Increase in total net assets	<u>383,377</u>	<u>547,622</u>
Net assets, beginning of year	<u>4,586,522</u>	<u>4,038,900</u>
Net assets, end of year	<u>\$ 4,969,899</u>	<u>\$ 4,586,522</u>

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

Novant Health, Inc. and Affiliates
Consolidated Statements of Cash Flows
Years Ended December 31, 2020 and 2019

(in thousands of dollars)

	2020	2019
Cash flows from operating activities		
Increase in net assets	\$ 383,377	\$ 547,622
Adjustments to reconcile changes in net assets to net cash provided by operating activities		
Depreciation, amortization and accretion	259,735	266,287
Loss on extinguishment of debt	6,208	-
Gain on sale of consolidated entities	(6,500)	(38,521)
Cumulative effect of change in accounting principle	-	(20,589)
Actuarial loss on pension and postretirement benefits	1,253	936
Change in funded status of defined benefit plans	878	2,233
Share of earnings in affiliates, net of distributions	17,196	4,282
Net realized and unrealized gains on assets limited as to use and investments	(164,305)	(327,494)
Change in fair value of interest rate swaps	7,906	7,527
Contributions restricted for capital	(1,468)	(7,825)
Changes in operating assets and liabilities, net of assets acquired and liabilities assumed		
Accounts receivable	(92,662)	(80,345)
Accounts payable and accrued liabilities	178,105	13,025
Medicare advanced payments	373,718	-
Third-party payor settlements	42,742	(2,176)
Deferred taxes, net	1,300	3,374
Other assets and liabilities, net	15,704	(15,450)
Net cash provided by operating activities	<u>1,023,187</u>	<u>352,886</u>
Cash flows from investing activities		
Capital expenditures	(372,021)	(413,369)
Proceeds from sales of long-term investments	1,910,189	965,892
Purchase of long-term investments	(2,278,671)	(904,147)
Proceeds from sales of short-term investments	341,485	665,036
Purchase of short-term investments	(477,778)	(373,458)
Proceeds from sale of property and equipment	2,821	3,844
Proceeds from sale of consolidated entities	8,500	34,143
Investments in unconsolidated affiliates, net	(2,516)	(21,033)
Other investing activities	(1,388)	(1,715)
Net cash used in investing activities	<u>(869,379)</u>	<u>(44,807)</u>
Cash flows from financing activities		
Principal payments on long-term debt	(288,136)	(268,643)
Proceeds from long-term debt	264,165	-
Net proceeds from issuance of bonds deposited with trustee	-	212,700
Proceeds from repurchase agreements, net	61,124	-
Proceeds from sale of accounts receivable	32,109	40,024
Proceeds from revolving credit facility	675,000	31,800
Payments on revolving credit facility	(675,000)	-
Other financing activities	4,559	7,758
Net cash provided by financing activities	<u>73,821</u>	<u>23,639</u>
Net increase in cash, cash equivalents and restricted cash	<u>227,629</u>	<u>331,718</u>
Cash, cash equivalents and restricted cash		
Beginning of year	<u>634,049</u>	<u>302,331</u>
End of year	<u>\$ 861,678</u>	<u>\$ 634,049</u>

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

Novant Health, Inc. and Affiliates
Consolidated Statements of Cash Flows, continued
Years Ended December 31, 2020 and 2019

(in thousands of dollars)

	2020	2019
Supplemental disclosure of cash flow information		
Interest paid	\$ 74,806	\$ 71,211
Income taxes paid	2,945	2,220
Supplemental disclosure of noncash financing and investing activities		
Property and equipment financed through current liabilities	37,090	59,048

The following table reconciles cash and cash equivalents on the consolidated balance sheets to cash, cash equivalents and restricted cash on the consolidated statements of cash flows:

	2020	2019
Cash and cash equivalents	\$ 711,822	\$ 402,536
Restricted cash included in assets limited as to use:		
Bond proceeds	18,180	48,520
Nonqualified plans	10,791	6,778
Other	12,152	3,492
Cash and cash equivalents included in long-term investments	<u>108,733</u>	<u>172,723</u>
Total cash, cash equivalents and restricted cash shown in the consolidated statements of cash flows	<u>\$ 861,678</u>	<u>\$ 634,049</u>

In July 2019, Novant Health issued Series 2019 A bonds. The following amounts were noncash and investing activities related to this transaction.

Face value of Series 2019 A bonds	\$ 306,985
Premium received on issuance of 2019 A bonds	20,583
Repayment of line of credit	(112,300)
Debt issuance costs	<u>(2,568)</u>
Net proceeds from issuance of bonds deposited with trustee	<u>\$ 212,700</u>

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

Novant Health, Inc. and Affiliates

Notes to Consolidated Financial Statements

December 31, 2020 and 2019

(in thousands of dollars)

1. Reporting Entity

Novant Health, Inc. (“Novant Health” or the “Company”) is a nonprofit, integrated health care network of physician clinics, outpatient facilities and hospitals that serves patients and communities in North Carolina, Virginia and South Carolina. The Novant Health network consists of over 1,600 physicians and 29,000 team members at nearly 700 locations, including 15 medical centers and hundreds of outpatient facilities and physician clinics. Headquartered in Winston-Salem, North Carolina, Novant Health is committed to making healthcare remarkable for patients and communities, serving more than 5 million patients annually. Novant Health and its affiliates serve their communities with programs including health education, home health care, prenatal clinics, community clinics and immunization services.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

Principles of Consolidation

The consolidated financial statements include the accounts of all affiliates controlled by Novant Health. All intercompany transactions and balances have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Significant estimates include, but are not limited to, accounts receivable price concessions, third-party payor settlements, goodwill and intangible asset valuation and subsequent recoverability, useful lives of intangible assets and property and equipment and medical and professional liability and other self-insurance accruals related assumptions.

Fair Value of Financial Instruments

The fair value of financial instruments approximates the carrying amount reported in the consolidated balance sheets for cash and cash equivalents, investments other than alternatives, assets limited as to use and interest rate swaps. More information can be found in Note 9, *Fair Value Measurements*.

Cash and Cash Equivalents

Cash and cash equivalents include highly liquid investments with an original maturity of three months or less, excluding amounts limited as to use by board designation, donors or trustees and certain amounts that are reported as long-term investments.

Novant Health, Inc. and Affiliates

Notes to Consolidated Financial Statements

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(in thousands of dollars)

Restricted Cash

Effective January 1, 2019, the Company adopted Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) 2016-18, “*Statement of Cash Flows (Topic 230)*” using the retrospective transition method. This guidance requires that the consolidated statements of cash flows explain the change during the period in the total of cash, cash equivalents and restricted cash.

Novant Health holds cash that is restricted by the Company to purchase investments, pay participants in the Company’s nonqualified plan and fund expenditures on certain capital projects which were financed by the issuance of the Series 2019 A bonds. Restricted cash balances were \$149,856 and \$231,513 as of December 31, 2020 and 2019, respectively, and are classified as long-term, consistent with the nature of their intended use based on the restrictions.

Accounts Receivable

Accounts receivable consist primarily of amounts owed by various governmental agencies, insurance companies and patients. Novant Health manages these receivables by regularly reviewing the accounts and contracts and by recording appropriate price concessions. Amounts the Company receives for treatment of patients covered by governmental programs and third-party payors as well as directly from patients are subject to both explicit and implicit price concessions. The Company estimates these price concessions using contractual agreements, discount policies and historical experience. Novant Health records price concessions in the period of service based on the analysis and consideration of these factors.

Leases

Effective January 1, 2019, the Company adopted FASB ASU 2016-02, “Leases (Topic 842)” using the modified retrospective transition approach as of the period of adoption. There was a cumulative effect adjustment to net assets without donor restrictions of \$20,589 as a result of the adoption.

Novant Health leases property and equipment under finance and operating leases and determines if an arrangement is a lease at the inception of the contract. Right-of-use assets represent the Company’s right to use the underlying assets for the lease term and lease liabilities represent the Company’s obligation to make lease payments arising from the leases. For leases with terms greater than 12 months, the related right-of-use assets and liabilities are recorded at the present value of lease payments over the term. Many of the Company’s leases include rental escalation clauses and renewal options that are factored into our determination of lease payments when appropriate. The Company uses its estimated incremental borrowing rate, which is derived from information available at the lease commencement date, in determining the present value of the lease payment.

Other Current Assets

Other current assets include inventories (which primarily consist of hospital and medical supplies and pharmaceuticals), prepaid expenses, deferred lease income and other receivables. Inventory costs are determined primarily using the average cost method and are stated at the lower of cost or net realizable value.

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(in thousands of dollars)

Investments

Debt investments are classified as trading securities. All debt investments are designated as trading at the time of acquisition. Unrealized gains and losses on debt and equity investments are included in excess of revenues over expenses, unless the income or loss is restricted by donor or law. Long-term investments are classified as noncurrent assets as the Company does not expect to use these funds to meet its current liabilities.

Investments in equity and debt securities with readily determinable fair values are measured at fair value based on prices obtained on active markets or exchanges. The Company also invests in alternative and private equity investments through funds structured as limited partnerships, limited liability companies ("LLC's") and corporations. These investments are recorded using the equity method, with the values provided by the respective partnership, LLC or corporation based on market value or other estimates that require varying degrees of judgment. The Company also has certain investments that are reported at Net Asset Value ("NAV") as permitted under GAAP. Novant Health believes the NAV reported at the end of the period is representative of the price we would receive if we sold the investment. For all of the Company's long-term investments, the related earnings are reported as investment income in the consolidated statements of operations and changes in net assets. At December 31, 2020 and 2019, the Company did not hold any long-term investments that were accounted for at cost less impairment with adjustments made for any observable price changes resulting from an orderly transaction for the identical or a similar investment of the same issuer.

Investments are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term would materially affect the investment balances included in the consolidated financial statements.

Assets Limited as to Use

Assets limited as to use primarily include assets held by trustees and assets designated for specific purposes by the Board of Trustees.

Derivatives

The Company selectively enters into interest rate protection agreements to mitigate changes in interest rates on variable rate borrowings. The notional amounts of such agreements are used to measure the interest to be paid or received and do not represent the amount of exposure to loss. None of these agreements are used for speculative or trading purposes.

Derivatives are recognized on the consolidated balance sheets at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship. The Company formally documents the hedging relationships at inception of the contract for derivative transactions, including identifying the hedge instruments and hedged items, as well as the risk management objectives and strategies for entering into the hedge transaction. At inception and on a quarterly basis thereafter, the Company assesses the effectiveness of derivatives used to hedge transactions. If a cash flow hedge is deemed highly effective, the change in fair value is recorded as a change in net assets without donor restrictions. The change in fair value of derivatives that do not qualify for hedge accounting is recognized in excess of revenues over expenses.

Novant Health, Inc. and Affiliates

Notes to Consolidated Financial Statements

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(in thousands of dollars)

Property and Equipment

Property and equipment are recorded at cost, if purchased, or at fair value at the date of donation, if donated. Depreciation is computed on a straight-line basis over the estimated useful lives of the related assets. Leasehold improvements are amortized over the life of the lease or the useful life of the asset, whichever is shorter.

Following is a summary of the estimated useful lives used in computing depreciation:

Buildings	30–40 years
Machinery and equipment	3–15 years
Software	3–10 years
Furniture and fixtures	7–14 years

Maintenance and repairs of property and equipment are expensed in the period incurred. Replacements or improvements that increase the estimated useful life of an asset are capitalized. The Company also capitalizes the cost of software developed for internal use. Assets that are sold, retired or otherwise disposed of are removed from the respective asset cost and accumulated depreciation accounts and any gain or loss is included in the results of operations.

Under the terms of the 1984 deed in which the Forsyth County Board of County Commissioners conveyed the assets of Forsyth Memorial Hospital (the “Hospital”) to Novant Health, Novant Health is required to operate the Hospital as a community general hospital open to the general public, and if Novant Health is dissolved, a successor nonprofit corporation approved by the Forsyth County Board of County Commissioners must carry out the terms and conditions of this conveyance. If these terms are not met, all ownership rights to the Hospital shall revert to the County, including the buildings and land together with the personal property and equipment associated with the Hospital with a net book value of approximately \$247,160 at December 31, 2020.

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

Goodwill and Other Intangible Assets

Goodwill represents the excess of the purchase price over the fair value of the net assets of acquired companies. Intangible assets generally represent the acquisition date fair value of certain rights or relationships obtained in such business acquisitions.

The Company considers certificates of need, which are required by certain states prior to the acquisition of high cost capital items, to be indefinite-lived intangible assets. The Company also has intangible assets with identifiable useful lives related to business acquisitions. These assets include business relationships and corporate trade names. In accordance with GAAP, the Company amortizes the cost of these intangible assets over their estimated useful lives.

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(in thousands of dollars)

Following is a summary of the estimated useful lives used in computing amortization:

Business relationships	26 years
Corporate trade name	29 years

On an annual basis, Novant Health tests goodwill and indefinite-lived assets for impairment. If it is more likely than not that the indefinite-lived asset is impaired, additional testing for impairment is required. GAAP prescribes that impairment for indefinite-lived intangibles is evaluated by comparing the fair value of the asset with its carrying amount. If the carrying amount exceeds the fair value, an impairment loss is recognized as the amount of that excess.

Impairment tests are performed at the reporting unit level for units that have goodwill. If it is more likely than not that the fair value of the reporting unit exceeds the carrying value of the reporting unit, additional impairment testing is not required. If it is more likely than not that the carrying value of the reporting unit exceeds the fair value of the reporting unit, additional testing for impairment is required. GAAP prescribes a two-step process for testing for goodwill impairments after applying the qualitative assessment. The first step is to determine if the carrying value of the reporting unit with goodwill is less than the related fair value of the reporting unit. The fair value of the reporting unit is determined through use of discounted cash flow methods and/or market based multiples of earnings and sales methods. If the carrying value of the reporting unit is less than the fair value of the reporting unit, the goodwill is not considered impaired. If the carrying value is greater than the fair value, the potential for impairment of goodwill exists. The goodwill impairment is determined by allocating the current fair value of the reporting unit among the assets and liabilities based on a purchase price allocation methodology as if the reporting unit was being acquired in a business combination. The fair value of the goodwill is implied from this allocation and compared to the carrying value with an impairment loss recognized if the carrying value is greater than the implied fair value.

Investments in Affiliates

Investments in entities which Novant Health does not control, but in which it has a substantial ownership interest and can exercise significant influence, are accounted for using the equity method. Investments for which the Company does not have the ability to exercise significant influence are accounted for at fair value or, if fair value is not readily determinable, at cost less impairment with adjustments made for any observable price changes resulting from an orderly transaction for the identical or a similar investment of the same issuer.

Other Assets

Other assets consist of notes and pledges receivable, insurance receivables, deferred rent income, prepaid pension costs and the cash surrender value of insurance policies.

Compensated Absences

The Company's employees earn vacation days at varying rates depending on years of service. Vacation time accumulates up to certain limits, at which time no additional vacation hours can be earned. Provided this hourly limit is not met, employees can continue to accumulate vacation hours and time can be carried over to future years. Accrued vacation time is included in accrued liabilities on the Company's consolidated balance sheets.

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Pension and Postretirement Benefit Plans

Novant Health's defined benefit plans are measured using actuarial techniques that reflect management's assumptions for discount rate, investment returns on plan assets, salary increases, expected retirement, mortality, employee turnover and future increases in healthcare costs. The discount rate (which is required to be the rate at which the projected benefit obligation could be effectively settled as of the measurement date) is determined with the assistance of actuaries, who calculate the yield on a theoretical portfolio of high-grade corporate bonds (rated Aa or better) with cash flows that are designed to match expected benefit payments in future years. The expected rate of return is a judgmental matter which is reviewed on an annual basis and revised as appropriate.

The accounting guidance related to employers' accounting for defined benefit pension and other postretirement plans requires recognition in the consolidated balance sheets of the funded status of these plans. The Company uses mark-to-market accounting and immediately recognizes changes in the fair value of plan assets and actuarial gains or losses in operating results annually in the fourth quarter. The remaining components of pension and postretirement healthcare expense, primarily service and interest costs and the expected return on plan assets, are recorded on a quarterly basis.

Self-Insurance Reserves

The Company is self-insured for certain employee health benefit options, workers' compensation and malpractice. These costs are accounted for on an accrual basis to include estimates of future payments for claims incurred.

Net Assets

Net assets without donor restrictions include undesignated amounts as well as amounts designated by the board for a specific purpose. Net assets with donor restrictions are held by related foundations and consist primarily of amounts contributed to foundations by donors with purpose restrictions. The Company also has net assets with donor restrictions that are perpetual in nature. Earnings on these assets are available for use as specified by the donors.

Contributions Received

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received or the condition is met. The gifts are reported as net assets with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is met, net assets with donor restrictions are reclassified as net assets without donor restrictions and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions, which is included in other operating revenue. Donor-restricted contributions whose restrictions are met within the same year as received are reported as net assets without donor restrictions in the accompanying consolidated financial statements.

Statement of Operations

All activities of Novant Health deemed by management to be ongoing, major and central to the provision of healthcare services are reported as operating revenues and expenses. Other activities are deemed to be non-operating and include investment income, income tax expense and other net periodic pension costs.

Novant Health, Inc. and Affiliates

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December 31, 2020 and 2019

(in thousands of dollars)

Novant Health receives supplemental Medicaid payments from the state of North Carolina through a federally approved disproportionate share program ("Medicaid DSH"). During 2012, the federal government approved an amendment to the Medicaid DSH plan. This amendment, referred to as the Medicaid Gap Assessment Program ("GAP"), provides a new funding model whereby hospitals are assessed an amount based on a percentage of their costs and are then paid supplemental amounts in an effort to reduce Medicaid losses. Novant Health records GAP payments received as net patient service revenue and GAP assessments paid as supplies and other on the consolidated statements of operations and changes in net assets. These supplemental payments are recognized in income when earned, if reasonably estimable and deemed collectible. There can be no assurance that this program will not be discontinued or materially modified. During 2020, Novant Health received \$186,180 and paid \$81,360 for GAP. During 2019, Novant Health received \$154,659 and paid \$79,850 for GAP.

The consolidated statements of operations and changes in net assets include excess of revenues over expenses. Changes in net assets without donor restrictions which are excluded from excess of revenues over expenses include cumulative effect of change in accounting principle, change in funded status of defined benefit plans and unrealized gain on derivative financial instruments that apply hedge accounting.

Other Revenue

Other revenue consists primarily of revenue from CARES Act funds, earnings from investments in affiliates accounted for using the equity method of accounting, retail pharmacy revenue, revenue from management services agreements, revenue from pay-for-performance contracts, gains on sales of consolidated entities and rental income.

Income Taxes

Novant Health is classified as a nonprofit organization pursuant to Section 501(c)(3) of the Internal Revenue Code and is exempt from income taxes on revenue earned from its tax-exempt purposes. Novant Health also operates various for-profit subsidiaries which operate in service lines that are complementary to the Company's tax-exempt purpose. Income from activities that are determined by IRS regulations to be unrelated to the tax-exempt purposes as well as income from activities of for-profit subsidiaries of the Company are subject to federal and state taxation.

The Company provides for income taxes using the asset and liability method. This approach recognizes the amount of federal, state and local taxes payable or refundable for the current year, as well as deferred tax assets and liabilities for the future tax consequences of events recognized in the consolidated financial statements and income tax returns. Deferred income tax assets and liabilities are adjusted to recognize the effects of changes in tax laws or enacted tax rates in the period in which such laws or rates are enacted. A valuation allowance is required when it is more likely than not that some portion of the deferred tax assets will not be realized. Realization is dependent on generating sufficient future taxable income.

Reclassifications

Certain balances in the prior fiscal year have been reclassified to conform to the presentation adopted in the current fiscal year.

Novant Health, Inc. and Affiliates

Notes to Consolidated Financial Statements

December 31, 2020 and 2019

(in thousands of dollars)

3. COVID-19 Pandemic

In December 2019, a novel strain of coronavirus, known as COVID-19, was first detected. The virus spread worldwide and on March 11, 2020, the World Health Organization designated the COVID-19 outbreak as a global pandemic. The spread of COVID-19 and the ensuing response of federal, state and local authorities resulted in a reduction in our patient volumes and also adversely impacted net patient service revenues as well as total operating expenses for the year ended December 31, 2020. Federal, state and local authorities have taken several actions designed to assist healthcare providers in providing care to COVID-19 and other patients to mitigate the adverse economic impact of the COVID-19 pandemic.

In response to the effect of COVID-19 on Novant Health's operating results and in accordance with the provisions of FASB ASC 350 Intangibles— Goodwill and Other and FASB ASC 360 Property, Plant and Equipment, the Company reviewed its long-lived and intangible assets for indicators of impairment. While COVID-19 did adversely impact Novant Health's operating results, the Company does not believe that the effects are significant enough or of a long enough duration to indicate impairment as of and for the year ended December 31, 2020. Novant Health will continue to assess potential indicators of impairment in all future periods.

CARES Act Funding

In response to COVID-19, the Coronavirus Aid, Relief, and Economic Security (CARES) Act, was signed into law on March 27, 2020. The CARES Act provides relief funds to hospitals and other healthcare providers on the front lines of the COVID-19 response. These funds are to be used to support healthcare related expenses or lost revenues attributable to COVID-19. During 2020, Novant Health received \$240,224 of CARES Act funding, of which \$205,924 was recognized as other operating revenue in the consolidated statement of operations and changes in net assets. The remaining \$34,300 is included in estimated third-party payor settlements on the consolidated balance sheet and may be recorded as revenue in future periods or refunded, subject to certain terms and conditions and ongoing regulatory clarifications.

Medicare Accelerated and Advanced Payment Program

In April 2020, the Company requested funds under the Centers for Medicare and Medicaid Services' Accelerated and Advanced Payment ("MAP") Program designed to increase cash flow to Medicare providers and suppliers impacted by COVID-19. The MAP program allows eligible health care facilities to request up to six months of advance Medicare payments for acute care hospitals or up to three months of advance Medicare payments for other health care providers. Novant Health received \$373,718 of MAP payments, with repayment to occur based upon the terms and conditions of the program. These payments are included in accrued liabilities and employee benefits and other liabilities on the consolidated balance sheet as of December 31, 2020.

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Employer Payroll Tax Deferrals

Under the provisions of the CARES Act, employers are allowed to defer payment of the employer share of the Social Security tax they otherwise are responsible for submitting to the federal government with respect to their employees. Employers generally are responsible for paying a 6.2 percent tax on employee wages. The provision required that the deferred employment tax be paid over the following two years, with half of the amount required to be paid by December 31, 2021, and the other half by December 31, 2022. The Company has \$76,318 of payroll tax deferrals that are included in accrued liabilities and employee benefits and other liabilities on the consolidated balance sheet as of December 31, 2020.

4. Organizational Changes

Formation of Joint Ventures

In February 2019, the Company purchased 50% of the outstanding units of a company that operates two radiation oncology centers for \$16,600. This investment is being accounted for using the equity method.

In March 2019, the Company contributed its ownership interest in two imaging centers in South Carolina to a new joint venture. In addition to a 20% interest in the new joint venture, Novant Health received cash of \$12,985 and recorded a gain of \$6,731 which is included in other revenue in the consolidated statements of operations and changes in net assets. This investment is being accounted for using the equity method.

In April 2019, Novant Health UVA Health System, a subsidiary of the Company, contributed its ownership interest in two ambulatory surgical centers to a new legal entity and sold 51% of that entity to a third party. In exchange, the Company received cash of \$5,761 and recorded a gain of \$8,488 which is included in other revenue in the consolidated statements of operations and changes in net assets.

Divestiture of Imaging Centers

In December 2020, MedQuest, Inc., a subsidiary of the Company, sold the stock of three imaging centers. In exchange, the Company received cash of \$8,500 and recorded a gain of \$6,500 which is included in other revenue in the consolidated statements of operations and changes in net assets.

Divestiture of Retail Pharmacy Business

In October 2019, Novant Health entered into a retail health care collaboration agreement with Walgreens Co. ("Walgreens"). As part of this transaction, the Company sold its retail pharmacy business to Walgreens. The Company received cash of \$7,407 and recorded a gain of \$4,162 which is included in other revenue in the consolidated statements of operations and changes in net assets.

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Divestiture of Clinical Engineering Business

In December 2019, Novant Health sold its clinical engineering business to TRIMEDX Holdings, LLC ("TRIMEDX"). Novant Health received cash of \$9,650 and a 0.9% interest in TRIMEDX. TRIMEDX assumed existing contracts for clinical engineering and maintenance services for Novant Health. As a result of this transaction, the Company recorded a gain of \$19,140 which is included in other revenue in the consolidated statements of operations and changes in net assets.

5. Revenue Recognition and Accounts Receivable

Net Patient Service Revenue

Net patient service revenue is reported at the amount that reflects the consideration to which Novant Health expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs) and others. Generally, the Company bills the patient and third-party payors several days after the services are performed and/or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

Performance obligations are determined based on the nature of the services provided by the Company. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected or actual charges. Novant Health believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in our hospitals receiving inpatient acute care services. The Company measures the performance obligation from admission into the hospital to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge. Revenue for performance obligations satisfied at a point in time is recognized when goods or services are provided and the Company does not believe it is required to provide additional goods or services to the patient.

Because all of its performance obligations relate to contracts with a duration of less than one year, the Company has elected to apply the practical expedient provided in FASB ASC 606-10-50-14(a) and, therefore, is not required to disclose the aggregate amounts of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. These performance obligations are primarily related to inpatient acute care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

Novant Health determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with Novant Health's policies and/or implicit price concessions provided to uninsured patients. The Company determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies and historical experience. The Company determines its estimate of implicit price concessions based on historical collection experience.

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Agreements with third-party payors typically provide for payments at amounts less than established charges. For services provided under Medicare and Medicaid programs, inpatient acute care services rendered to program beneficiaries are paid at prospectively determined rates per diagnosis. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Inpatient non-acute services, certain outpatient services and defined capital and medical education costs related to beneficiaries are paid based on a cost reimbursement methodology. Outpatient services are paid at a prospectively determined rate. Physician services are paid based upon established fee schedules. Novant Health is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by Novant Health and audits thereof by the fiscal intermediary. Payment arrangements with commercial insurance carriers include prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to interpretation. Compliance with such laws and regulations may also be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge Novant Health's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon the Company. In addition, the contracts the Company has with commercial payors also provide for retroactive audit and review of claims.

Cost report settlements under reimbursement agreements with Medicare and Medicaid for retroactive adjustments due to audits, reviews or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor and the Company's historical experience. Estimated settlements are adjusted in future periods as final settlements are determined. There is a reasonable possibility that recorded estimates will change by a material amount in the near term. Adjustments arising from a change in the transaction price were not significant in 2020 and 2019.

Generally patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. Novant Health also provides services to uninsured patients. The transaction price for both uninsured patients as well as insured patients with deductibles and coinsurance is estimated based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to net patient service revenue in the period of the change. For the years ended December 31, 2020 and 2019, additional revenue of \$25,900 and \$33,000, respectively, was recognized due to changes in estimates of implicit price concessions, discounts and contractual adjustments for performance obligations satisfied in prior years. Subsequent changes that are determined to be the results of an adverse change in the patient's ability to pay are recorded as bad debt expense. Bad debt expense is reported as a component of supplies and other in the consolidated statements of operations and changes in net assets and was not significant for the years ended December 31, 2020 and 2019.

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

	December 31, 2020		
	Acute Care Facilities	Outpatient Locations	Total
Medicare	\$ 1,089,219	\$ 440,236	\$ 1,529,455
Medicaid	392,724	86,309	479,033
Managed care	1,882,339	962,752	2,845,091
Other	112,754	37,764	150,518
Self-pay	23,425	25,272	48,697
Total	\$ 3,500,461	\$ 1,552,333	\$ 5,052,794

	December 31, 2019		
	Acute Care Facilities	Outpatient Locations	Total
Medicare	\$ 1,055,759	\$ 443,436	\$ 1,499,195
Medicaid	356,830	81,944	438,774
Managed care	1,934,796	991,300	2,926,096
Other	108,717	35,137	143,854
Self-pay	17,960	29,557	47,517
Total	\$ 3,474,062	\$ 1,581,374	\$ 5,055,436

Novant Health has elected the practical expedient allowed under FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Company's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, the Company does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Novant Health has a program of factoring certain patient receivables with recourse to a third-party. Novant Health is obligated to repurchase factored receivables upon occurrence of certain conditions of the program. Accordingly, the Company accounts for the factoring as a secured borrowing. The factored receivables are recorded at their estimated net realizable value and are shown as other assets in the consolidated balance sheets. An offsetting liability, representing Novant Health's potential recourse for these receivables, is part of employee benefits and other liabilities in the consolidated balance sheets. As of December 31, 2020, the factored notes and the related liabilities were \$54,001 and \$67,548, respectively. As of December 31, 2019, the factored notes and the related liabilities were \$54,761 and \$68,594, respectively.

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Other Revenue

In addition to net patient service revenue, Novant Health also recognizes revenue related to other, non-patient related transactions. These transactions primarily include revenue from CARES Act funds, retail pharmacy revenue, revenue from management services agreements, revenue from pay-for-performance contracts, gains on sales of consolidated entities and rental income. Revenue from these transactions is recognized when obligations under the terms of the respective contract are satisfied and is measured as the amount of consideration the Company expects to receive from those services. The Company recognizes rental income in accordance with GAAP on a straight-line basis over the lease term.

6. Charity Care and Community Benefit

In accordance with Novant Health's mission to improve the health of its communities one person at a time, Novant Health facilities accept patients regardless of their ability to pay. At acute facilities, uninsured patients qualify for a full write-off of their bills if their household income is at or below 300% of the federal poverty level. Novant Health also offers a catastrophic discount for patients with an account balance greater than \$5, flexible payment plans, and discounts for uninsured patients who do not qualify for the charity care program. In addition to these programs for hospitals, Novant Health physician groups and outpatient centers also have charity care programs to assist patients in need. The Company's approximate cost of providing care to indigent patients was \$179,072 and \$152,295 for the years ended December 31, 2020 and 2019, respectively. Novant Health estimates the costs of providing traditional charity care using each facility's estimated ratio of costs to charges. Funds received from gifts or grants to subsidize charity services provided were \$3,596 and \$2,111 for the years ended December 31, 2020 and 2019, respectively.

7. Other Current Assets

Other current assets consist of the following at December 31:

	2020	2019
Inventory	\$ 118,718	\$ 92,335
Prepays	54,157	48,632
Other receivables	86,379	89,908
	<u>\$ 259,254</u>	<u>\$ 230,875</u>

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8. Assets Limited as to Use and Investments

Short-Term Investments

Novant Health holds certain investments that are short-term in nature and have original maturity dates ranging from three to twelve months. Short-term investments consist of the following at December 31:

	2020	2019
Certificates of deposit	\$ 10,619	\$ 10,550
Fixed income - corporate and other	10,967	-
Fixed income - government securities	<u>309,156</u>	<u>185,069</u>
	<u>\$ 330,742</u>	<u>\$ 195,619</u>

Assets Limited as to Use

The designation of assets limited as to use at December 31 is as follows:

	<u>2020</u>		<u>2019</u>	
	<u>Current Portion</u>	<u>Long-Term Portion</u>	<u>Current Portion</u>	<u>Long-Term Portion</u>
Under general and professional liability funding arrangement held by trustee	\$ 12,645	\$ 22,140	\$ 11,125	\$ 39,099
Held by bond trustee	18,180	-	48,520	-
Designated by board to service benefit plans	<u>11,849</u>	<u>212,536</u>	<u>11,376</u>	<u>174,379</u>
	<u>\$ 42,674</u>	<u>\$ 234,676</u>	<u>\$ 71,021</u>	<u>\$ 213,478</u>

Assets limited as to use are invested primarily in cash and cash equivalents and corporate, U.S. government and U.S. agency debt obligations.

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Long-Term Investments

Investments are reported at either fair value, the equity method of accounting or at NAV as a practical expedient. The composition of long-term investments is as follows:

	December 31, 2020			
	At Fair Value	On Equity Method	At NAV	Total
Cash and cash equivalents	\$ 108,733	\$ -	\$ -	\$ 108,733
U.S. equities	124,134	-	582,987	707,121
International equities	17,878	-	413,327	431,205
Fixed income - government securities	574,936	-	-	574,936
Fixed income - corporate and other	5,448	94,326	-	99,774
Hedge funds	-	422,110	-	422,110
Private equity	-	152,126	-	152,126
Emerging markets	33,370	-	199,253	232,623
Real estate and other	57,469	198,574	-	256,043
	\$ 921,968	\$ 867,136	\$ 1,195,567	\$ 2,984,671

	December 31, 2019			
	At Fair Value	On Equity Method	At NAV	Total
Cash and cash equivalents	\$ 172,723	\$ -	\$ -	\$ 172,723
U.S. equities	501,509	14,449	113,756	629,714
International equities	315,949	-	99,741	415,690
Fixed income - government securities	251,315	-	-	251,315
Fixed income - corporate and other	12,343	77,585	-	89,928
Hedge funds	-	420,336	-	420,336
Private equity	-	80,236	-	80,236
Emerging markets	2,499	-	184,853	187,352
Real estate and other	70,832	189,583	-	260,415
	\$ 1,327,170	\$ 782,189	\$ 398,350	\$ 2,507,709

Long-term investments carried at NAV may be redeemed or liquidated only after giving notice to the fund manager. The notice period ranges from daily to 120 days. These investments have been reported at NAV by each fund as a practical expedient to estimate their fair value. Novant Health has the ability to redeem its interests at or within 120 days of the financial statement date.

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The Company's investments in hedge funds include funds structured as limited partnerships, LLCs and corporations. These funds are domiciled in the U.S. and foreign jurisdictions and are managed by investment managers subject to oversight by various countries' regulators. The underlying assets of the hedge funds vary widely in risk and liquidity. Overall, the hedge fund holdings of the Company are expected to provide improved diversification to the Company's broader portfolio.

The Company's investments in hedge funds represent 14.1% and 16.8% of total long-term investments held at December 31, 2020 and 2019, respectively. These instruments may contain elements of both credit and market risk. Such risks include, but are not limited to, limited liquidity, absence of oversight, dependence upon key individuals, emphasis on speculative investments (both derivatives and nonmarketable investments) and nondisclosure of portfolio composition.

Novant Health is obligated under certain investment agreements to periodically advance additional funding up to specified levels. As of December 31, 2020 and 2019, Novant Health had future commitments of \$343,566 and \$286,635, respectively, for which capital calls had not been exercised.

Investment income for assets limited as to use and investments is comprised of the following for the years ended December 31:

	2020	2019
Income		
Interest and dividend income	\$ 37,518	\$ 51,053
Net realized gains	37,347	70,638
Net unrealized gains	<u>126,958</u>	<u>256,856</u>
	<u>\$ 201,823</u>	<u>\$ 378,547</u>

Investment income is shown net of related expenses on the consolidated statements of operations and changes in net assets. Investment related administrative expenses were \$7,629 and \$8,474 for the years ended December 31, 2020 and 2019, respectively.

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Liquidity and Availability

As of December 31, 2020 and 2019, Novant Health has working capital of \$699,136 and \$626,221, respectively.

Financial assets at year-end:	2020	2019
Cash and cash equivalents	\$ 711,822	\$ 402,536
Accounts receivable, net	670,736	610,470
Short-term investments	330,742	195,619
Assets limited as to use	277,350	284,499
Receivable for settlement with third-party payors	25,109	16,231
Other current assets	86,379	89,908
Long-term investments	2,984,671	2,507,709
Other assets	37,665	36,384
Total financial assets	\$ 5,124,474	\$ 4,143,356
Less amounts not available:		
Long-term investments with liquidity horizons greater than one year	459,562	364,292
Assets limited as to use	277,350	284,499
Donor restricted funds	84,836	84,732
Financial assets not available to be used within one year	\$ 821,748	\$ 733,523
Financial assets available to meet general expenditures within one year	\$ 4,302,726	\$ 3,409,833

As part of the Company's liquidity management plan, cash in excess of daily requirements is invested in either money market funds, short-term investments or long-term investments. Investment decisions are made based on anticipated liquidity needs, such that financial assets are available as general expenditures, liabilities and other obligations come due. Additionally, Novant Health maintains a \$950,000 line of credit, as discussed in Note 16, *Long-Term Debt*. As of December 31, 2020, \$950,000 was available on the line of credit. As of December 31, 2020, the Company was in compliance with financial covenants as discussed in Note 16, *Long-Term Debt*.

9. Fair Value Measurements

Novant Health categorizes, for disclosure purposes, assets and liabilities measured at fair value in the consolidated financial statements based upon whether the inputs used to determine their fair values are observable or unobservable. Observable inputs are inputs which are based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about pricing the asset or liability, based on the best information available in the circumstances.

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In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement of the asset or liability. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

Novant Health follows the three-level fair value hierarchy to categorize these assets and liabilities recognized at fair value at each reporting period, which prioritizes the inputs used to measure such fair values. Level inputs are defined as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities on the reporting date. Investments classified in this level generally include exchange traded equity securities, futures, pooled short-term investment funds, options and exchange traded mutual funds.

Level 2: Inputs other than quoted market prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability. Investments classified in this level generally include fixed income securities, including fixed income government obligations; asset-backed securities; certificates of deposit; derivatives; as well as certain U.S. and international equities which are not traded on an active exchange.

Level 3: Pricing inputs are generally unobservable for the assets and liabilities and include situations where there is little, if any, market activity for the investment. The inputs into the determination of the fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities.

Assets and liabilities classified as Level 1 are valued using unadjusted quoted market prices for identical assets or liabilities in active markets. Novant Health uses techniques consistent with the market approach and income approach for measuring the fair value of its Level 2 assets and liabilities. The market approach is a valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities. The income approach generally converts future amounts (cash flows or earnings) to a single present value amount (discounted).

The degree of judgement exercised in determining fair value is greatest for securities categorized in Level 3. Inputs used in estimating the fair value of Level 3 investments include earnings metrics and a valuation multiple. Assumptions used, due to lack of observable inputs, may significantly impact the fair value of the investment.

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As of December 31, 2020 and 2019, the Level 1 and Level 2 assets and liabilities listed in the fair value hierarchy tables below utilize the following valuation techniques and inputs:

Certificates of deposit

The fair value of certificates of deposit is based on cost plus accrued interest. Significant observable inputs include security cost, maturity and relevant short-term interest rates.

U.S. equities, international equities, emerging markets and other exchange traded funds

The fair value of investments in U.S. equities, international equities, emerging markets and other exchange traded funds are primarily determined using either quoted prices in active markets or the calculated net asset value. The values for underlying investments are fair value estimates determined by external fund managers based on operating results, balance sheet stability, growth and other business and market sector fundamentals. The investments in Level 2 may be redeemed or liquidated on a daily basis with no notice.

Fixed income and debt securities

The fair value of investments in fixed income and debt securities is primarily determined using techniques that are consistent with the market approach. Significant observable inputs include benchmark yields, reported trades, observable broker/dealer quotes, issuer spreads and security specific characteristics, such as early redemption options.

Derivatives

The fair value of derivative contracts is primarily determined using techniques consistent with the market approach. Significant observable inputs to valuation models include interest rates, credit spreads, volatilities and maturity.

During 2020 and 2019, there were no transfers between Level 1 and 2.

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The following table summarizes fair value measurements, by level, at December 31, 2020 for all financial assets and liabilities measured at fair value on a recurring basis in the consolidated financial statements:

	Fair Value Measurements at Reporting Date Using			Total
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
Assets				
Short-term investments:				
Certificates of deposit	\$ -	\$ 10,619	\$ -	\$ 10,619
Fixed income - corporate and other	-	10,967	-	10,967
Fixed income - government securities	-	309,156	-	309,156
Total short-term investments	-	330,742	-	330,742
Assets limited as to use:				
Cash and cash equivalents	41,123	-	-	41,123
U.S. equities	176,795	-	-	176,795
International equities	6,306	-	-	6,306
Fixed income - government securities	18,474	22,701	-	41,175
Fixed income - corporate and other	564	11,387	-	11,951
Total assets limited as to use	243,262	34,088	-	277,350
Long-term investments:				
Cash and cash equivalents	108,733	-	-	108,733
U.S. equities	111,772	-	12,362	124,134
International equities	17,878	-	-	17,878
Fixed income - government securities	-	574,936	-	574,936
Fixed income - corporate and other	5,243	205	-	5,448
Emerging markets	33,370	-	-	33,370
Other exchange traded funds	57,469	-	-	57,469
Total long-term investments	334,465	575,141	12,362	921,968
Total assets at fair value	\$ 577,727	\$ 939,971	\$ 12,362	\$ 1,530,060
Liabilities				
Accrued liabilities	\$ 11,654	\$ -	\$ -	\$ 11,654
Derivative financial instruments	-	51,803	-	51,803
Deferred compensation liabilities	198,519	-	-	198,519
Total liabilities at fair value	\$ 210,173	\$ 51,803	\$ -	\$ 261,976

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The following table summarizes fair value measurements, by level, at December 31, 2019 for all financial assets and liabilities measured at fair value on a recurring basis in the consolidated financial statements:

	Fair Value Measurements at Reporting Date Using			Total
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
Assets				
Short-term investments:				
Certificates of deposit	\$ -	\$ 10,550	\$ -	\$ 10,550
Fixed income - government securities	-	185,069	-	185,069
Total short-term investments	-	195,619	-	195,619
Assets limited as to use:				
Cash and cash equivalents	58,790	-	-	58,790
U.S. equities	153,694	-	-	153,694
International equities	5,698	-	-	5,698
Fixed income - government securities	16,102	34,924	-	51,026
Fixed income - corporate and other	884	14,407	-	15,291
Total assets limited as to use	235,168	49,331	-	284,499
Long-term investments:				
Cash and cash equivalents	172,723	-	-	172,723
U.S. equities	501,509	-	-	501,509
International equities	314,943	1,006	-	315,949
Fixed income - government securities	-	251,315	-	251,315
Fixed income - corporate and other	10,101	2,242	-	12,343
Emerging markets	2,499	-	-	2,499
Other exchange traded funds	70,832	-	-	70,832
Total long-term investments	1,072,607	254,563	-	1,327,170
Total assets at fair value	\$ 1,307,775	\$ 499,513	\$ -	\$ 1,807,288
Liabilities				
Accrued liabilities	\$ 11,182	\$ -	\$ -	\$ 11,182
Derivative financial instruments	-	43,897	-	43,897
Deferred compensation liabilities	169,355	-	-	169,355
Total liabilities at fair value	\$ 180,537	\$ 43,897	\$ -	\$ 224,434

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The table below sets forth a summary of the changes in the fair value of the Level 3 investment for the year ended December 31, 2020:

	U.S. Equities
Balance at December 31, 2019	\$ -
Transfer in of Level 3 investment	9,650
Unrealized gain	<u>2,712</u>
Balance at December 31, 2020	<u>\$ 12,362</u>

During 2020, the Company transferred \$9,650 from investments in affiliates to long-term investments as it was determined that the investment was to be held for the long-term and our primary objective is capital appreciation of the preferred stock.

10. Property and Equipment

Property and equipment consists of the following at December 31:

	2020	2019
Land and land improvements	\$ 409,302	\$ 394,550
Leasehold improvements	267,520	229,822
Buildings and building improvements	2,388,551	2,170,658
Equipment	2,101,953	1,999,027
Software	539,339	530,326
Construction-in-progress	<u>155,046</u>	<u>254,306</u>
	5,861,711	5,578,689
Less: Accumulated depreciation	<u>(3,461,642)</u>	<u>(3,258,270)</u>
	<u>\$ 2,400,069</u>	<u>\$ 2,320,419</u>

Novant Health reviews long-lived assets for recoverability as required when events and changes in circumstances indicate that its carrying value may not be recoverable. No impairment charges were recorded in 2020 or 2019.

Depreciation expense for the years ended December 31, 2020 and 2019 was \$257,293 and \$263,471, respectively. Construction contracts of approximately \$324,209 exist for the expansion of existing hospitals and facility renovations. At December 31, 2020, the remaining commitment on these contracts was \$66,810.

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11. Leases

Novant Health leases property and equipment under non-cancellable agreements. The following table presents the components of our right-of-use assets and liabilities related to leases and their classification as of December 31:

Component of Lease Balances	Classification in Consolidated Balance Sheets	2020	2019
Assets:			
Operating lease assets		\$ 486,099	\$ 493,405
Finance lease assets		7,255	460
Total leased assets		<u>\$ 493,354</u>	<u>\$ 493,865</u>
Liabilities:			
Operating lease liabilities			
Current		\$ 88,796	\$ 88,369
Long-term		418,011	422,326
Total operating lease liabilities		<u>506,807</u>	<u>510,695</u>
Finance lease liabilities			
Current	Current portion of long-term debt	857	147
Long-term	Long-term debt, net of current portion	6,467	283
Total finance lease liabilities		<u>7,324</u>	<u>430</u>
Total lease liabilities		<u>\$ 514,131</u>	<u>\$ 511,125</u>

Novant Health's operating leases are primarily for real estate, including off-campus outpatient facilities, medical office buildings and corporate and other administrative offices, as well as medical and office equipment. Novant Health's finance leases consist of a real estate lease and several medical equipment leases. Real estate lease agreements typically have initial terms of five to ten years and equipment lease agreements typically have initial terms of three years. Leases with an initial term of 12 months or less ("short-term leases") are not recorded in the consolidated balance sheets.

Real estate leases may include one or more options to renew, with renewals that can extend the lease term from five to ten years. The exercise of lease renewal options is at the Company's sole discretion. In general, renewal options are not considered to be reasonably likely to be exercised, therefore, renewal options are generally not recognized as part of right-of-use assets and lease liabilities. Certain leases also include options to purchase the leased property. The useful lives of assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise. The majority of medical equipment leases have terms of three years with a bargain purchase option that is reasonably certain of exercise; therefore, these assets are depreciated over their useful life, typically ranging from five to seven years.

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Certain lease agreements for real estate include payments based on actual common area maintenance expenses and/or include rental payments adjusted periodically for inflation. These variable lease payments are recognized in supplies and other in the consolidated statements of operations and changes in net assets but are not included in the right-of-use asset or liability balances in our consolidated balance sheets. Lease agreements do not contain any material residual value guarantees, restrictions or covenants.

Novant Health has elected the practical expedient that allows lessees to choose to not separate lease and non-lease components by class of underlying asset and are applying this expedient to all asset classes.

The following table presents certain information related to lease expense for finance and operating leases for the years ended December 31:

	<u>2020</u>	<u>2019</u>
Operating leases ⁽¹⁾	\$ 106,690	\$ 100,556
Variable lease expense ⁽¹⁾	11,735	10,354
Finance lease expense:		
Amortization of leased assets	492	174
Interest on lease liabilities	47	24
	<u>\$ 118,964</u>	<u>\$ 111,108</u>

⁽¹⁾ Expenses are included in supplies and other in the consolidated statements of operations and changes in net assets.

The following table presents supplemental cash flow information for the years ended December 31:

	<u>2020</u>	<u>2019</u>
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows for operating leases	\$ 102,015	\$ 96,147
Operating cash flows for finance leases	441	201
Financing cash flows for finance leases	47	24

The Company entered into agreements to obtain right-of-use assets that created lease liabilities which resulted in noncash operating activities of \$59,384 and noncash financing and investing activities of \$7,288 for the year ended December 31, 2020.

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Future maturities of lease liabilities at December 31, 2020 are presented in the following table:

	<u>Operating Leases</u>	<u>Finance Leases</u>	<u>Total</u>
2021	\$ 97,860	\$ 957	\$ 98,817
2022	90,463	892	91,355
2023	79,118	895	80,013
2024	66,250	857	67,107
2025	56,317	860	57,177
Thereafter	<u>171,191</u>	<u>3,270</u>	<u>174,461</u>
Total lease payments	561,199	7,731	568,930
Less: Imputed interest	<u>(54,392)</u>	<u>(407)</u>	<u>(54,799)</u>
Total lease obligations	506,807	7,324	514,131
Less: Current obligations	<u>(88,796)</u>	<u>(857)</u>	<u>(89,653)</u>
Long-term lease obligations	<u>\$ 418,011</u>	<u>\$ 6,467</u>	<u>\$ 424,478</u>

At December 31, 2020, the weighted average remaining lease term for operating leases is 7.2 years and the weighted average discount rate is 2.6%. For finance leases, the weighted average remaining lease term is 8.6 years and the weighted average discount rate is 1.5%.

Novant Health is also a lessor and sublessor of real estate under operating leases. At December 31, 2020 and 2019, \$12,283 and \$11,572, respectively, of deferred rent was recorded in the consolidated balance sheets as a component of other assets. Lease income for the years ended December 31, 2020 and 2019 was \$11,106 and \$10,331, respectively, which is included in other revenue in the consolidated statements of operations and changes in net assets. Most of the Company's leases include operating expenses such as utilities and maintenance costs in rent charges. However, variable rent income is not material. The Company has elected the practical expedient that allows lessors to not separate lease and non-lease components by class of underlying asset for all asset classes. The combined component is accounted for under lease accounting guidance.

At December 31, 2020 and 2019, land and buildings with a net book value of \$14,888 and \$16,623, respectively, were leased to various unrelated health care organizations, with terms ranging from six months to five years. These assets are included in property and equipment, net on the consolidated balance sheets.

Although the Company leases and subleases a small amount of building space to non-affiliated medical practices, the significant leases consist of long-term ground leases classified as operating leases with remaining terms from 42 years with options to extend for the additional terms of five years each to 64 years with no options to extend.

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The future undiscounted cash flows to be received from these leases are as follows:

Years Ending December 31

2021	\$	7,982
2022		7,124
2023		4,892
2024		3,326
2025		2,697
Thereafter		129,778
	<u>\$</u>	<u>155,799</u>

12. Intangible Assets and Goodwill

Intangible assets consist of the following at December 31:

	<u>Gross Intangible</u>	<u>Accumulated Amortization</u>	<u>Net Intangible</u>
Balance at December 31, 2020			
Unamortized intangible assets			
Certificates of need	\$ 67,311	\$ -	\$ 67,311
Total unamortized intangible assets	67,311	-	67,311
Amortized intangible assets			
Business relationships	44,840	(22,550)	22,290
Corporate trade name and other intangibles	25,724	(8,713)	17,011
Total amortized intangible assets	70,564	(31,263)	39,301
Total intangible assets	<u>\$ 137,875</u>	<u>\$ (31,263)</u>	<u>\$ 106,612</u>
Balance at December 31, 2019			
Unamortized intangible assets			
Certificates of need	\$ 67,363	\$ -	\$ 67,363
Total unamortized intangible assets	67,363	-	67,363
Amortized intangible assets			
Business relationships	45,181	(20,776)	24,405
Corporate trade name and other intangibles	25,624	(7,451)	18,173
Total amortized intangible assets	70,805	(28,227)	42,578
Total intangible assets	<u>\$ 138,168</u>	<u>\$ (28,227)</u>	<u>\$ 109,941</u>

Amortization expense related to intangible assets was \$2,728 and \$2,733 for the years ended December 31, 2020 and 2019, respectively. Estimated annual amortization expense for intangible assets for the years 2021 through 2023 is \$2,728 per year and \$2,715 for 2024 and 2025.

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The following table summarizes the changes in the carrying amount of goodwill for the years ended December 31:

	2020	2019
As of January 1		
Goodwill, net of accumulated amortization	\$ 241,596	\$ 244,587
Accumulated impairment losses	<u>(37,563)</u>	<u>(37,563)</u>
	204,033	207,024
Disposals	<u>(598)</u>	<u>(2,991)</u>
	<u>203,435</u>	<u>204,033</u>
As of the end of the period		
Goodwill, net of accumulated amortization	240,540	241,596
Accumulated impairment losses	<u>(37,105)</u>	<u>(37,563)</u>
	<u>\$ 203,435</u>	<u>\$ 204,033</u>

Novant Health reviews long-lived assets for recoverability as required when events and changes in circumstances indicate that its carrying value may not be recoverable. The Company tests goodwill and indefinite-lived assets for impairment on an annual basis. No impairment charges to amortizable intangible assets were recorded as a result of this review in 2020 or 2019. Impairment tests presume stable or improving results at certain Novant Health reporting units which are based on the implementation of programs and initiatives that are designed to achieve projected results. If these projections are not met, or in the future negative trends occur which would impact our future outlook, further impairments of goodwill and other intangible assets may occur. Future restructuring of our markets that could potentially change our reporting units could also result in future impairments of goodwill.

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13. Investments in Affiliates

Novant Health has noncontrolling interests in eighteen healthcare related entities. The Company's ownership interests in the entities range from 8.0% to 51.0%. These investments are accounted for using either the equity method or a measurement alternative.

A summary of investments, ownership percentages, investment amounts and the Company's share of earnings for the years ended December 31, 2020 and 2019 is as follows:

Investee	% Ownership		Investment Balance		Share of Earnings of Investee	
	2020	2019	2020	2019	2020	2019
Advanced Services	23%	23%	\$ 5,253	\$ 25,405	\$ 10,697	\$ 1,926
Radiation Oncology Centers of the Carolinas LLC	50%	50%	15,981	16,217	3,014	2,169
Novant Health Rehabilitation Hospital	50%	50%	15,626	13,416	2,210	128
Providence Plaza LLC	30%	30%	4,636	4,596	280	259
Provider-Lead Patient-Centered Care of NC	9%	9%	1,600	1,600	-	-
Other	Various	Various	11,858	18,050	1,484	(2,357)
			<u>\$ 54,954</u>	<u>\$ 79,284</u>	<u>\$ 17,685</u>	<u>\$ 2,125</u>

The following table presents summarized financial information related to investments in the above noncontrolled entities as of December 31:

	2020	2019
Assets	\$ 194,936	\$ 901,009
Liabilities	106,797	722,570
Equity	88,139	178,439
Total revenue	141,066	245,401
Total expenses	82,328	240,501
Net income	58,738	4,900
Novant Health's share of net income	17,685	2,125

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14. Other Assets

Other assets consist of the following at December 31:

	2020	2019
Notes receivable and other	\$ 70,764	\$ 56,320
Cash surrender value of insurance policies	32,681	28,914
Deferred rent income	12,283	11,572
Pledges receivable	4,984	7,470
Reinsurance receivables	7,541	8,660
Prepaid pension costs	-	980
	<u>\$ 128,253</u>	<u>\$ 113,916</u>

15. Accrued Liabilities

Accrued liabilities consist of the following at December 31:

	2020	2019
Accrued compensation	\$ 335,863	\$ 289,969
Medicare advanced payments, current portion	173,385	-
Payroll taxes and withholdings	39,754	5,467
Interest	6,562	8,303
Postretirement benefit liability	1,267	1,450
Pension liability	-	321
Other accrued liabilities	80,650	72,542
Self-insurance		
Employee medical claims liability	27,472	29,001
Malpractice and workers' compensation liability	17,720	16,038
	<u>\$ 682,673</u>	<u>\$ 423,091</u>

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16. Long-Term Debt

Following is a summary of long-term debt at December 31:

	2020	2019
Tax-exempt revenue bonds	\$ 775,575	\$ 1,059,390
Taxable revenue bonds	<u>250,000</u>	<u>250,000</u>
Total bonds	1,025,575	1,309,390
Taxable term loan	264,165	-
Finance lease obligations and other notes payable	<u>19,648</u>	<u>15,901</u>
	1,309,388	1,325,291
Unamortized premium or discount, net	27,622	24,809
Unamortized debt issuance costs, net	<u>(6,175)</u>	<u>(9,042)</u>
	1,330,835	1,341,058
Less: Current maturities	<u>(54,848)</u>	<u>(57,119)</u>
	<u>\$ 1,275,987</u>	<u>\$ 1,283,939</u>

Tax-Exempt Revenue Bonds

Novant Health has tax-exempt financing agreements through conduit issuers. These bonds are comprised of the following at December 31:

	2020	2019
Series 2019 A Current Interest Term Bonds, bearing interest at rates ranging from 3.1% to 4.0% payable semi-annually with mandatory redemption beginning in 2047	\$ 306,985	\$ 306,985
Series 2013 A and B Current Interest Term Bonds and Serial Bonds, bearing interest at rates ranging from 3.125% to 5.0% payable semi-annually and maturing through 2046; principal payments began in 2014	256,495	263,675
Series 2010 A Current Interest Term Bonds and Serial Bonds, bearing interest at rates ranging from 4.0% to 5.3% payable semi-annually and maturing through 2043; principal payments begin in 2023	-	264,165
Series 2008 A, B and C Variable Rate Demand Bonds, bearing interest at variable rates payable monthly and maturing through 2028; principal payments began in 2009	77,095	89,565
Series 2004 A and B Variable Rate Demand Bonds, bearing interest at variable rates payable monthly and maturing through 2034; principal payments begin in 2025	<u>135,000</u>	<u>135,000</u>
	<u>\$ 775,575</u>	<u>\$ 1,059,390</u>

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In 2003, Novant Health entered into a new Master Trust Indenture (the “Agreement”). The Agreement authorizes the creation of a Combined Group, which consists of the members of the Obligated Group and the Restricted Affiliates. Novant Health and two of its affiliates that operate tertiary care hospitals, Novant Health Forsyth Medical Center and Novant Health Presbyterian Medical Center, are the members of the Obligated Group. The members of the Obligated Group are jointly and severally liable for the payment of all obligations under the Agreement. The Company’s Restricted Affiliates, which include certain other subsidiaries of the Company, are not directly obligated to pay obligations under the Agreement, but the members of the Obligated Group have covenanted in the Agreement to cause the Restricted Affiliates to provide funds to the members of the Obligated Group to pay obligations under the Agreement. All bonds issued by Novant Health are collateralized by the Obligated Group.

The bond agreements provide for early redemption periods of the bonds prior to mandatory redemption, subject to a premium, generally ranging from 0.0% to 2.0%, as defined in the agreements. In accordance with the bond indenture agreements, the bonds are general, unsecured obligations of Novant Health. The bond indentures require Novant Health to cause the Restricted Affiliates to comply with certain covenants, including the maintenance of a minimum debt service coverage ratio and a minimum number of days cash on hand. As of December 31, 2020 and 2019, Novant Health is in compliance with these bond covenants.

The Series 2004 A and B Variable Rate Demand Bonds are collateralized by a standby purchase agreement (“SBPA”) issued by JP Morgan Chase Bank National Association. The SBPA expires April 1, 2025. If the SBPA should be used to fund tenders due to a failed remarketing, repayment in quarterly installments over three years is required. As a result, the Company has classified \$36,818 of the 2004 bonds as current at December 31, 2020 and 2019.

In March 2011, the documents related to the Series 2008 A, B and C Variable Rate Demand Bonds were amended to allow the conversion of the bonds to bank direct purchase index floating rate bonds. In December 2017, the Series 2008 A, B, and C Variable Rate Demand Bonds were refinanced. Subsequent to the refinancing, the direct purchase agreements have a term of seven years and will expire in December 2024.

In July 2019, Novant Health issued \$306,985 of Series 2019 A bonds through the North Carolina Medical Care Commission. Proceeds of the bonds were used to refund outstanding balances on the revolving credit facility, pay expenses of issuing the bonds and to finance and reimburse Novant Health for expenses related to constructing and equipping additions and renovations to several acute care facilities and constructing a new acute care facility, Novant Health Mint Hill Medical Center.

On November 1, 2020, Novant Health called the Series 2010 A bonds and repaid them at face value using the proceeds of the Taxable Term Loan.

Taxable Revenue Bonds

On September 23, 2009, Novant Health issued \$350,000 of taxable fixed rate bonds (the “2009 A Bonds”). \$250,000 of these bonds bore interest at a rate of 5.85% and matured in 2019. The remaining \$100,000 of these bonds matured in 2014. Proceeds of the 2009 A Bonds were used to refinance a portion of the Company’s revolving credit facility in January 2010.

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On April 23, 2013, Novant Health issued \$250,000 of taxable fixed rate bonds (the “2013 C Bonds”). The 2013 C Bonds bear interest at a rate of 4.37% and mature in 2043. Proceeds of the 2013 C Bonds were used for eligible purposes, including the refinancing of long-term debt.

The taxable revenue bonds are subject to the same covenant requirements that are included in the bond agreements for the tax-exempt revenue bonds.

Taxable Term Loan

In March 2020, Novant Health entered into an agreement to borrow \$264,165. The loan bears interest at a fixed rate with principal payments due annually beginning in 2023 through the maturity date of April 1, 2030.

Other Long-Term Debt

Other long-term debt consists of a promissory note related to the redemption of a membership interest and various loans and notes on buildings and finance leases, bearing interest at rates ranging from 0.81% to 12.15%.

Scheduled maturities of all long-term debt are as follows:

Years Ending December 31

2021	\$ 18,030
2022	20,330
2023	26,514
2024	25,639
2025	21,132
Thereafter	<u>1,197,743</u>
	<u>\$ 1,309,388</u>

Novant Health capitalized \$5,437 and \$3,795 of interest in 2020 and 2019, respectively.

Revolving Credit Facility

On June 13, 2013, Novant Health entered into a \$200,000 Senior Revolving Credit Facility. In March 2017, the Senior Revolving Credit Facility was amended and is available through March 27, 2022. At December 31, 2019, \$200,000 was available for borrowing. In April 2020, the Senior Revolving Credit Facility was terminated. On April 1, 2020, Novant Health entered into a \$950,000 Revolving Credit Agreement which is available until September 30, 2021. Borrowings bear interest at variable rates. At December 31, 2020, \$950,000 was available for borrowing.

Debt Issuance Costs

Unamortized debt issuance costs are presented in the consolidated balance sheets as a direct deduction from the carrying value of the associated debt. Debt issuance costs are amortized using the effective interest method over the life of the related debt agreements and instruments.

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17. Short-Term Borrowings

Short-term borrowings consist primarily of securities repurchase transactions. Securities repurchase transactions are conducted by the Company under a standardized securities industry master agreement, amended to suit the specificities of each respective counter-party. These agreements generally provide detail as to the nature of the transaction, including provisions for payment netting, established parameters concerning the ownership and custody of the collateral securities, including the right to substitute collateral during the term of the agreement, and provide for remedies in the event of default by either party. The Company's securities repurchase agreements are accounted for as a secured borrowing and are reported in the consolidated balance sheets as short-term borrowings. The Company posts collateral in the form of U.S. treasury, agency securities and treasury inflation protected securities and receives an amount equal to approximately 98% of the fair value of the securities to be repurchased during January 2021 at interest rates ranging from 0.25% to 3.00%. At December 31, 2020 and 2019, the fair value amounts outstanding were \$149,592 and \$88,176, respectively. The interest rate on the outstanding balances at December 31, 2020 is 0.22%. The maturity dates of the agreements are under two weeks.

18. Interest Rate Swaps

As of August 18, 2008, concurrent with the 2008 bond issuance, Novant Health entered into two interest rate swap agreements to hedge the variable interest rates of the 2008 bonds. The swaps are based on an aggregate notional amount of \$77,095. Novant Health receives a variable rate which is tied to 68% of LIBOR, and pays a fixed rate of 3.679% and 3.621% for the \$56,100 and \$20,995 notional amounts, respectively. The swaps have been designated as cash flow hedges and are carried on the consolidated balance sheets at fair value. In the fourth quarter of 2018, the hedging relationship ceased to be highly effective and hedge accounting was discontinued.

In July 2006, Novant Health entered into a floating-to-fixed swap agreement with a notional amount of \$135,000 and a term of 28 years to hedge the floating rate 2004 bonds. Novant Health receives a variable rate which is tied to 64.8% of LIBOR plus 12 basis points and pays a fixed interest rate of 3.8%. The swap has been designated as a cash flow hedge and is carried on the consolidated balance sheets at fair value. In the first quarter of 2019, the hedge relationship ceased to be highly effective and hedge accounting was discontinued.

Novant Health records interest rate swaps at fair value. These swaps are presented as derivative financial instruments in the consolidated balance sheets.

The following table summarizes the expense for derivatives after hedge accounting was discontinued. This expense is included in interest expense in the consolidated statements of operations and changes in net assets for the years ended December 31:

	2020	2019
Change in fair value of non-hedged interest rate swaps	\$ (7,906)	\$ (7,527)
Reclassification of net assets into earnings	(3,180)	(3,374)
	<u>\$ (11,086)</u>	<u>\$ (10,901)</u>

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19. Employee Benefits and Other Liabilities

Employee benefits and other liabilities consist of the following at December 31:

	2020	2019
Medicare advanced payments	\$ 200,333	\$ -
Deferred compensation liabilities	198,519	169,355
Employee benefits and other	119,796	83,388
Self-insurance malpractice and workers' compensation, net of current portion	44,139	54,545
Deferred gains	3,451	3,531
Postretirement benefit liability, net of current portion	20,955	20,518
Pension liability, net of current portion	2,390	2,268
	<u>\$ 589,583</u>	<u>\$ 333,605</u>

20. Income Taxes

The provision for federal and state income taxes is as follows:

	2020	2019
Current tax expense (benefit)		
Federal	\$ (892)	\$ 5,286
State	97	1,450
	<u>(795)</u>	<u>6,736</u>
Deferred tax expense (benefit)		
Federal	1,422	767
State	(122)	(145)
	<u>1,300</u>	<u>622</u>
	<u>\$ 505</u>	<u>\$ 7,358</u>

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The components of deferred taxes are as follows:

	2020	2019
Deferred tax assets		
Loss carryforwards	\$ 16,493	\$ 17,757
Deferred charge for intercompany transfer	5,329	6,655
Allowance for doubtful accounts	954	1,056
Accrued expenses	3,748	3,525
Future deductions- operating leases	3,360	2,639
Total deferred tax assets	<u>29,884</u>	<u>31,632</u>
Deferred tax liabilities		
Intangible assets	(5,840)	(6,141)
Property and equipment	(564)	(1,070)
Right-of-use assets	(3,295)	(2,579)
Other	(1,087)	-
Total deferred tax liabilities	<u>(10,786)</u>	<u>(9,790)</u>
Valuation allowance	<u>(18,975)</u>	<u>(20,419)</u>
Net deferred tax asset	<u>\$ 123</u>	<u>\$ 1,423</u>

GAAP requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences are deductible. In making this determination, management considers all available positive and negative evidence affecting specific deferred tax assets, including the Company's past and anticipated future performance, reversal of deferred tax liabilities, length of carryback and carryforward periods and implementation of tax planning strategies.

Objective positive evidence is necessary to support a conclusion that a valuation allowance is not needed for all or a portion of deferred tax assets when significant negative evidence exists. Cumulative losses in recent years are the most compelling form of negative evidence considered by management in this determination. For the years ended December 31, 2020 and 2019, management has determined that based on all available evidence, a valuation allowance of \$18,975 and \$20,419, respectively, is appropriate.

As of December 31, 2020, the Company had approximately \$73,426 of federal and \$54,585 of state loss carryforwards available to reduce taxable income. \$66,943 of the loss carryforwards expire through 2038 and the remainder do not expire. In addition, at December 31, 2020, the Company had approximately \$11,030 of federal and \$2,815 of state contribution carryforwards available to reduce taxable income.

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Income tax expense (benefit) reported in the consolidated statements of operations and changes in net assets is shown below:

	2020	2019
Federal taxes	\$ 530	\$ 6,053
State income taxes	(25)	1,305
	<u>\$ 505</u>	<u>\$ 7,358</u>

The Company is required to evaluate uncertain tax positions. This evaluation includes a quantification of tax risk in areas such as unrelated business taxable income and the taxation of our for-profit subsidiaries. This evaluation did not have a material effect on the Company's consolidated statements of operations and changes in net assets for the years ended December 31, 2020 and 2019.

21. Employee Benefit Plans and Other Postretirement Benefit Plans

Certain Novant Health affiliates participate in the Pension Restoration Plan of Novant Health, Inc. (the "Novant Plan"), a noncontributory defined benefit pension plan covering substantially all the affiliates' employees of record as of December 1998. Participation is limited to vested employees as of December 31, 1998. Effective January 1, 2008, and July 1, 2009, the Company assumed two noncontributory defined benefit plans, the Pension Plan for the Employees of Rowan Regional Medical Center (the "Rowan Plan") and the Prince William Hospital Corporation Cash Balance Pension Plan (the "Prince William Plan"), respectively. Participation in the Rowan Plan was closed to new entrants and the accrued benefits were frozen as of December 31, 2003. Participation in the Prince William Plan was closed to new entrants and the accrued benefits were frozen as of April 1, 2010. The assets of the plans are primarily invested in fixed income securities (both U.S. government and corporate debt) and cash and cash equivalents.

In 2018, the Novant Health Board of Trustees decided to terminate the Novant Plan, the Rowan Plan and the Prince William Plan. During 2019, all assets were transferred from the plans as either lump sum payments to participants or to an insurance company for current and future annuity payments. As a result of the termination, the Company recorded an additional expense in other net periodic pension costs in the consolidated statements of operations and changes in net assets of \$2,480. Also during 2019, the Company provided additional funding of \$16,146 to the plans.

Certain Novant Health affiliates have supplemental retirement income plans covering highly compensated employees. These are nonqualified plans which are not subject to ERISA funding requirements. As such, Novant Health intends only to fund the plans in amounts equivalent to the plans' annual benefit payments. During 2013, the Company implemented a new supplemental retirement income plan that covers certain highly compensated employees. This plan acts as a defined contribution plan and annual funding requirements are determined under provisions of the plan. Some of these plans are nonqualified deferred compensation plans which provide certain individuals meeting specific criteria with the ability to defer compensation. The assets of these plans, along with the associated liabilities, are recorded as current and long-term assets limited as to use, accrued liabilities, and employee benefits and other liabilities on the consolidated balance sheets.

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

(in thousands of dollars)

Novant Health also provides fixed dollar amounts for health care and life insurance benefits to certain retired employees. Covered employees may become eligible for these benefits if they meet minimum age and service requirements, and if they are eligible for retirement benefits. Novant Health has the right to modify or terminate these benefits.

Information regarding benefit obligations, plan assets, funded status, expected cash flows and net periodic benefit cost follows within this footnote.

	Defined Benefit Plans		Postretirement Healthcare Benefit Plans	
	2020	2019	2020	2019
Change in benefit obligations				
Projected benefit obligation at beginning of year	\$ 2,589	\$ 282,482	\$ 21,968	\$ 20,140
Service cost	22	20	89	83
Interest cost	62	5,647	623	791
Actuarial (gain) loss	(35)	17,989	727	1,688
Assumption changes	-	(496)	4	4
Settlements	-	(290,901)	-	-
Benefits paid	(248)	(12,152)	(1,189)	(738)
Projected benefit obligation at end of year	<u>\$ 2,390</u>	<u>\$ 2,589</u>	<u>\$ 22,222</u>	<u>\$ 21,968</u>

The assumption changes for 2020 and 2019 are primarily due to changes in the discount rate.

The weighted-average assumptions used to determine end of year benefit obligations are as follows:

	Defined Benefit Plans		Postretirement Healthcare Benefit Plans	
	2020	2019	2020	2019
Discount rate	1.85% - 2.25%	2.80% - 3.00%	1.70% - 2.35%	2.70% - 3.10%
Health care cost trend on covered charges	N/A	N/A	6.75% in 2021 grading to 4.50% in 2026	7.25% in 2020 grading to 4.50% in 2026

Assumed health care cost trend rates may have an impact on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would not have a significant effect on the amounts reported as of December 31, 2020.

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

(in thousands of dollars)

	Defined Benefit Plans		Postretirement Healthcare Benefit Plans	
	2020	2019	2020	2019
Change in plan assets				
Fair value of plan assets at beginning of year	\$ 980	\$ 267,511	\$ -	\$ -
Actual return on plan assets	-	23,695	-	-
Employer contributions	248	16,333	1,189	738
Settlements	(980)	(290,901)	-	-
Benefits paid	(248)	(12,152)	(1,189)	(738)
Plan expenses	-	(3,506)	-	-
Fair value of plan assets at end of year	<u>\$ -</u>	<u>\$ 980</u>	<u>\$ -</u>	<u>\$ -</u>

At December 31, 2019, all of the Company's pension plan assets are cash and were valued using Level 1 measurements.

Funded Status

The funded status of the plans recognized in the consolidated balance sheets and the amounts recognized in net assets without donor restrictions as of December 31 are as follows:

	Defined Benefit Plans		Postretirement Healthcare Benefit Plans	
	2020	2019	2020	2019
End of Year				
Fair value of plan assets at end of year	\$ -	\$ 980	\$ -	\$ -
Benefit obligation at end of year	2,390	2,589	22,222	21,968
Funded status	<u>\$ (2,390)</u>	<u>\$ (1,609)</u>	<u>\$ (22,222)</u>	<u>\$ (21,968)</u>

Amount recognized in the balance sheets

Prepaid benefit cost at measurement date	\$ -	\$ 980	\$ -	\$ -
Accrued benefit cost	(1,884)	(2,066)	(24,084)	(21,000)
Change in net assets without donor restrictions	(506)	(523)	1,862	(968)
	<u>\$ (2,390)</u>	<u>\$ (1,609)</u>	<u>\$ (22,222)</u>	<u>\$ (21,968)</u>

Amounts recognized in net assets

Net actuarial loss (gain)	\$ 506	\$ 523	\$ (1,862)	\$ 968
	<u>\$ 506</u>	<u>\$ 523</u>	<u>\$ (1,862)</u>	<u>\$ 968</u>

Other changes in plan assets and benefit

Net (gain) loss	\$ (36)	\$ 378	\$ 727	\$ 1,688
Amortization of net loss	19	72	168	95
Total recognized in net assets	<u>\$ (17)</u>	<u>\$ 450</u>	<u>\$ 895</u>	<u>\$ 1,783</u>

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
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At the end of 2020 and 2019, the projected benefit obligation, accumulated benefit obligation and fair value of plan assets within the defined benefit pension plans were as follows:

	2020	2019
Projected benefit obligation	\$ 2,390	\$ 2,589
Accumulated benefit obligation	2,390	2,589
Fair value of plan assets	-	980

Cash Flows

The Company does not plan to make any contributions to its defined benefit pension plans in 2021. The Company expects to make contributions to the supplemental retirement income plans of approximately \$4,086 for the 2021 fiscal year.

The following assumed benefit payments, which reflect expected future service, as appropriate, and were used in the calculation of projected benefit obligations, are estimated to be paid as follows:

	Defined Benefit Plans	Postretirement Healthcare Benefit Plans
Expected benefit payments		
2021	\$ 188	\$ 1,266
2022	410	1,227
2023	176	1,253
2024	164	1,269
2025	158	1,276
2026–2030	656	6,204

The components of net periodic benefit cost as of December 31 are as follows:

	Defined Benefit Plans		Postretirement Healthcare Benefit Plans	
	2020	2019	2020	2019
Service cost	\$ 22	\$ 20	\$ 89	\$ 83
Interest cost	62	5,647	623	791
Estimated return on plan assets	-	(4,179)	-	-
Recognized net actuarial loss (gain)	942	1,027	(168)	(95)
Net periodic benefit cost	<u>\$ 1,026</u>	<u>\$ 2,515</u>	<u>\$ 544</u>	<u>\$ 779</u>
Total recognized in net periodic benefit cost and net assets without donor restrictions	<u>\$ 1,009</u>	<u>\$ 2,965</u>	<u>\$ 1,439</u>	<u>\$ 2,562</u>

The components of net periodic pension and postretirement benefit costs other than the service component are included in non-operating income on the consolidated statements of operations and changes in net assets.

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

(in thousands of dollars)

Amounts expected to be amortized from net assets without donor restrictions into net periodic benefit cost during the year ending December 31, 2021 are as follows:

	Defined Benefit Plans	Postretirement Healthcare Benefit Plans
Actuarial net loss	\$ 30	\$ 128

The weighted-average assumptions used to determine net periodic benefit cost were as follows:

	Defined Benefit Plans		Postretirement Healthcare Benefit Plans	
	2020	2019	2020	2019
Discount rate	2.80% - 3.00%	3.90% - 4.16%	2.70% - 3.10%	3.85% - 4.15%
Expected return on plan assets	N/A	3.00%	N/A	N/A
Health care cost trend on covered charges	N/A	N/A	7.25% in 2020 grading to 4.50% in 2026	8.0% in 2019 grading to 5.0% in 2025

In developing the expected return on plan assets, the Company considers the plan assets' historical actual return, targeted asset allocations and the anticipated future economic environment and long-term performance of individual asset classes, based on the Company's investment strategy. While appropriate consideration is given to recent and historical investment performance, the assumption represents management's best estimate of the long-term prospective return.

In addition to these plans, Novant Health sponsors a number of defined contribution plans. Contributions are determined under various formulas. Costs related to such plans amounted to \$87,444 and \$91,159 in 2020 and 2019, respectively.

Certain Novant Health consolidated affiliates participate in cafeteria plans which provide certain benefits, including basic medical and dental coverage, long-term disability benefits, reimbursement of supplemental dependent care expenses and group life insurance benefits. The affiliates contribute predetermined amounts for each full-time and part-time employee, which is allocated to the various benefit options in accordance with the participant's election. Affiliate contributions to these plans were approximately \$282,126 in 2020 and \$291,370 in 2019.

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

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22. Net Assets without Donor Restrictions

The following table reconciles the carrying amounts of the Company's controlling interest and the noncontrolling interests for net assets without donor restrictions:

	<u>Total</u>	<u>Controlling Interest</u>	<u>Noncontrolling Interests</u>
Balance at January 1, 2019	\$ 3,961,367	\$ 3,877,651	\$ 83,716
Excess of revenues over expenses	523,482	522,280	1,202
Cumulative effect of change in accounting principle	20,589	20,589	-
Change in funded status of defined benefit plans	(2,233)	(2,233)	-
Unrealized gain on derivative financial instruments	3,374	3,374	-
Other changes in net assets without donor restrictions	(4,789)	(690)	(4,099)
Balance at December 31, 2019	4,501,790	4,420,971	80,819
Excess (deficit) of revenues over expenses	382,155	382,401	(246)
Change in funded status of defined benefit plans	(878)	(878)	-
Unrealized gain on derivative financial instruments	3,180	3,180	-
Other changes in net assets without donor restrictions	(1,184)	137	(1,321)
Balance at December 31, 2020	\$ 4,885,063	\$ 4,805,811	\$ 79,252

23. Net Assets with Donor Restrictions

Donor restricted net assets are available for the following purposes as of December 31:

	2020	2019
Buildings and equipment	\$ 41,777	\$ 44,801
Clinical care, research and academic	27,651	25,271
Charity care	6,841	5,263
Other	8,567	9,397
	<u>\$ 84,836</u>	<u>\$ 84,732</u>

Novant Health, Inc. and Affiliates
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(in thousands of dollars)

24. Professional and General Liability Insurance Coverage

Novant Health is self-insured for professional and general liability exposures up to certain limits. The Company has umbrella policies in place above those limits. The provision for estimated medical malpractice claims includes estimates of the ultimate costs for reported claims and claims incurred but not reported. Novant Health also participates in a self-insured program for workers' compensation and is self-insured for certain health benefits options. A portion of these self-insured professional liabilities is funded through a revocable trust fund operated by Novant Health. This fund was converted to claims-made status on January 1, 2020, and prior reported liabilities under this coverage were placed in run-off. Effective January 1, 2020, funding for self-insured professional liabilities are insured by Novant Health Casualty, LLC a North Carolina domiciled insurance captive. Coverage terms and umbrella policies of the same or higher limits are in place for the captive. At December 31, 2020 and 2019, undiscounted professional and general liability loss reserves of \$61,859 and \$70,583, respectively, are included in current liabilities and employee benefits and other liabilities on the consolidated balance sheets. Expenses related to these plans amounted to \$19,181 and \$19,208 in 2020 and 2019, respectively.

25. Commitments and Contingencies

The Company and its affiliates are presently involved in various personal injury, regulatory investigations, tort actions and other claims and assessments arising out of the normal course of business. The Company establishes separate legal reserves when such matters, other than those covered under the Company's self-insured programs, present loss contingencies that are both probable and estimable. Management believes that Novant Health has adequate legal defenses, self-insurance reserves and/or insurance coverage for these asserted claims, as well as any unasserted claims and does not believe these claims will have a material effect on the Company's operations or financial position. The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services and Medicare and Medicaid fraud and abuse. In recent years, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

(in thousands of dollars)

At December 31, 2020, the Company had guarantees for payment of the indebtedness and lease agreements of certain equity method investees. The maximum potential amount of future payments under these agreements was approximately \$29,545. These guarantees extend until October 2026 based on the payment schedule of the underlying agreements. At December 31, 2020, \$985 has been recorded in the consolidated balance sheet for the Company's obligations under these guarantees.

26. Concentrations of Credit Risk

Novant Health provides services primarily to the residents of various counties within North Carolina, South Carolina and Virginia without collateral or other proof of ability to pay. Most patients are local residents who are insured partially or fully under third-party payor arrangements.

The mix of receivables from patients and third-party payors at December 31 is as follows:

	2020	2019
Medicare	28.8%	25.2%
Medicaid	4.7%	4.9%
Other third-party payors	62.3%	65.1%
Patients	4.2%	4.8%
	<u>100.0%</u>	<u>100.0%</u>

Novant Health places the majority of its cash and investments with corporate and financial institutions. Novant Health maintains cash balances in excess of FDIC insured limits; however, the Company has not experienced any losses on such deposits.

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
December 31, 2020 and 2019

(in thousands of dollars)

27. Functional Expenses

Novant Health provides general health care services to residents within its geographic region. Novant Health's financial statements report certain expense categories that are attributable to more than one health care service or support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including depreciation, amortization and interest and other occupancy costs, are allocated to a function based on a square footage or units of service basis. Allocated health care services costs not allocated on a units of service basis are generally allocated based on revenue. Expenses relating to providing these services are as follows:

	December 31, 2020			
	Health Care Services		Support Services	
	Acute Care Facilities	Outpatient Locations	General & Administrative	Total
Salaries and employee benefits	\$ 1,414,131	\$ 1,333,086	\$ 335,891	\$ 3,083,108
Supplies and other	1,332,862	595,005	145,223	2,073,090
Depreciation and amortization expense	147,261	46,507	66,283	260,051
Interest expense	62,744	8,390	6,888	78,022
Other non-operating expenses	(42)	2,349	5,865	8,172
Total expenses	\$ 2,956,956	\$ 1,985,337	\$ 560,150	\$ 5,502,443

	December 31, 2019			
	Health Care Services		Support Services	
	Acute Care Facilities	Outpatient Locations	General & Administrative	Total
Salaries and employee benefits	\$ 1,405,372	\$ 1,341,217	\$ 277,288	\$ 3,023,877
Supplies and other	1,299,805	484,741	125,513	1,910,059
Depreciation and amortization expense	147,450	41,930	76,853	266,233
Interest expense	55,729	8,855	14,708	79,292
Other non-operating expenses	(38)	2,017	8,570	10,549
Total expenses	\$ 2,908,318	\$ 1,878,760	\$ 502,932	\$ 5,290,010

Novant Health, Inc. and Affiliates
Notes to Consolidated Financial Statements
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(in thousands of dollars)

28. Subsequent Events

On February 1, 2021, a wholly owned subsidiary of Novant Health, Inc. purchased substantially all of the assets of New Hanover Regional Medical Center located in Wilmington, NC as well as certain assets of New Hanover County used by New Hanover Regional Medical Center in the delivery of health care services. The purchased assets also include ownership interest or board control of the subsidiaries of New Hanover Regional Medical Center, most significantly, its physician practices which provide patient care at 55 locations. New Hanover Regional Medical Center includes 800 licensed beds and is the primary referral hospital in the region, with specialty centers in cardiac, cancer, obstetrics, trauma, vascular surgery, intensive care, rehabilitation and psychiatry. The total purchase price paid for the acquisition was \$1,500,000, plus adjustments for cash and working capital. In order to finance the transaction, on January 29, 2021, Novant Health amended its Revolving Credit Agreement to increase the borrowing limit to \$1,600,000 and extend the maturity date to July 29, 2022. The Revolving Credit Agreement is fully drawn as of the date these financial statements were issued. The purchase price allocation for this acquisition has not been finalized.

In January 2021, Novant Health signed a non-binding letter of intent with The Rector and Visitors of the University of Virginia, on behalf of its Medical Center. The purpose of the letter of intent is to proceed with discussing a potential sale of Novant Health's 60% ownership interest in Novant Health UVA Health System. The terms of the potential transaction have not yet been finalized.

The Company evaluated subsequent events and transactions for potential recognition or disclosure in the consolidated financial statements through March 29, 2021, the day the consolidated financial statements were issued.

29. Significant Recent Accounting Pronouncements

In January 2017, the FASB issued ASU 2017-04, *Simplifying the Test for Goodwill Impairment*. The new guidance eliminates the requirement to calculate the implied fair value of goodwill (i.e., Step 2 of the current goodwill impairment test) to measure a goodwill impairment charge. Instead, entities will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value (i.e., measure the charge based on the current Step 1). This guidance is effective for Novant Health on January 1, 2022. The adoption of this guidance would only impact Novant Health's consolidated financial statements in situations where there is impairment of a reporting unit.

Novant Health, Inc. and Affiliates
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(in thousands of dollars)

In August 2018, the FASB issued ASU 2018-15, *Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40), Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract*. This guidance aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). The guidance also requires that the capitalized costs be expensed over the term of the hosting arrangement and that the expense and cash flows of the capitalized expense be presented in the same place on the statements of operations and statements of cash flows, respectively. Similarly, the capitalized costs are required to be presented on the balance sheets in the same line item that a prepayment of the fees of the associated hosting arrangement would be presented. This guidance was effective for Novant Health on January 1, 2020 and is being applied prospectively to all implementation costs incurred after the date of adoption. Implementation of this guidance did not have a significant impact on the consolidated financial statements of Novant Health.

In May 2019, the FASB issued ASU 2019-06, *Intangibles - Goodwill and Other (Topic 350), Business Combinations (Topic 805), and Not-for-Profit Entities (Topics 958)*. This guidance extends certain private company alternatives to not-for-profit entities, allowing the amortization of goodwill on a straight-line basis over ten years or less. If this accounting alternative is elected, an accounting policy election must also be made to test goodwill at either the entity level or the reporting unit level. Goodwill is required to be tested for impairment when a triggering event occurs that indicates that the fair value of the entity may be below its carrying amount. An election is also allowed on a prospective basis to subsume into goodwill and amortize customer-related intangible assets that are not capable of being sold or licensed independently and all noncompete agreements. If this election is adopted, the election to amortize goodwill must also be adopted. Novant Health has not elected these alternatives at this time.

In March 2020, the FASB issued ASU 2020-04, *Reference Rate Reform (Topic 848)* and has subsequently issued supplemental and/or clarifying ASUs (collectively “ASC 848”). This guidance provides relief from the application of certain guidance during the transition to alternative reference rates. Optional expedients are provided for contract modification that replace a reference rate affected by reference rate reform and related contemporaneous modifications. Exceptions are provided for changes to the critical terms of a hedging relationship due to reference rate reform. Expedients are provided for cash flow hedging relationships and fair value hedging relationships. These provisions are available until December 31, 2022. Novant Health is currently evaluating the effect of reference rate reform on its contracts, but the availability of these expedients and exceptions is expected to reduce the impact of reference rate reform on the consolidated financial statements of Novant Health.

Other Financial Information



Report of Independent Auditors

To the Board of Trustees of
Novant Health, Inc.

We have audited the consolidated financial statements of Novant Health, Inc. and its affiliates as of December 31, 2020 and for the year then ended and our report thereon appears on pages 1 and 2 of this document. That audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The accompanying consolidating information as of and for the year ended December 31, 2020 and the supplemental schedule of cost of community benefit programs for the year ended December 31, 2020 appearing on pages 54 – 60 (collectively referred to herein as the “information”) are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. The information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information, excluding the schedule of cost of community benefit programs information marked “unaudited,” has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information, excluding the schedule of costs of community benefit programs information marked “unaudited,” is fairly stated, in all material respects, in relation to the consolidated financial statements taken as a whole. The consolidating information is not intended to present the financial position, results of operations and cash flows of the individual companies, and accordingly, we do not express an opinion on the financial position, results of operations and cash flows of the individual companies. The schedule of costs of community benefit programs information marked “unaudited” has not been subjected to the auditing procedures applied in the audit of the consolidated financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

PricewaterhouseCoopers LLP

March 29, 2021

Novant Health, Inc. and Affiliates
Schedule of Cost of Community Benefit Programs (unaudited)
December 31, 2020

In addition to providing charity care to uninsured patients, Novant Health also provides services to beneficiaries of public programs and various other community health services intended to improve the health of the communities in which the Company operates. Novant Health uses the following four categories to identify the resources utilized for the care of persons who are underserved and for providing community benefit programs to the needy:

- Traditional charity care, which includes the cost of services provided to persons who cannot afford health care because of inadequate resources and who are uninsured.
- Unpaid cost of Medicare, which represents the unpaid cost of services provided to persons through the government program for individuals age 65 and older as well as those that qualify for federal disability benefits.
- Unpaid cost of Medicaid, which represents the unpaid cost of services provided to persons covered by the government program for medically indigent patients.
- Community benefit programs, which consist of the unreimbursed costs of certain programs and services for the general community, mainly for indigent patients but also for people with chronic health risks. Examples of these programs include health promotion and education, free clinics and screenings and other community services.

The net cost of providing care to indigent patients and community benefit programs is as follows:

	2020
Traditional charity care	\$ 179,072
Unpaid cost of Medicare	649,878
Unpaid cost of Medicaid	136,041
Community benefit programs	<u>53,442</u>
	<u>\$ 1,018,433</u>

As discussed in Note 2 in the accompanying consolidated financial statements, Novant Health received supplemental Medicaid payments during 2020. These amounts are included in the community benefit amount for 2020.

Novant Health, Inc. and Affiliates
Consolidating Balance Sheet
December 31, 2020

<i>(in thousands of dollars)</i>	Combined Group	Unrestricted Affiliates	Eliminations	Total
Assets				
Current assets				
Cash and cash equivalents	\$ 556,179	\$ 155,643	\$ -	\$ 711,822
Accounts receivable, net	580,439	90,297	-	670,736
Short-term investments	330,582	160	-	330,742
Current portion of assets limited as to use	30,029	12,645	-	42,674
Receivable for settlement with third-party payors	21,129	3,980	-	25,109
Other current assets	234,386	42,033	(17,165)	259,254
Total current assets	1,752,744	304,758	(17,165)	2,040,337
Assets limited as to use	203,681	30,995	-	234,676
Long-term investments	2,640,842	343,829	-	2,984,671
Property and equipment, net	2,059,045	341,024	-	2,400,069
Operating lease right-of-use assets, net	520,722	57,319	(84,687)	493,354
Intangible assets and goodwill, net	61,164	248,883	-	310,047
Investments in affiliates	95,496	28,597	(69,139)	54,954
Deferred tax asset	-	5,317	-	5,317
Other assets	114,987	14,067	(801)	128,253
Total assets	<u>\$ 7,448,681</u>	<u>\$ 1,374,789</u>	<u>\$ (171,792)</u>	<u>\$ 8,651,678</u>
Liabilities and Net Assets				
Current liabilities				
Current portion of long-term debt	\$ 53,968	\$ 880	\$ -	\$ 54,848
Short-term borrowings	149,300	292	-	149,592
Accounts payable	257,409	31,387	(11,486)	277,310
Accrued liabilities	592,148	93,854	(3,329)	682,673
Operating lease liabilities	86,057	11,857	(9,118)	88,796
Estimated third-party payor settlements	78,411	9,571	-	87,982
Due to (from) related organizations	(247,392)	247,392	-	-
Total current liabilities	969,901	395,233	(23,933)	1,341,201
Long-term debt, net of current portion	1,262,576	13,411	-	1,275,987
Deferred tax liability	-	5,194	-	5,194
Operating lease liabilities, net of current portion	449,276	45,038	(76,303)	418,011
Derivative financial instruments	51,803	-	-	51,803
Employee benefits and other liabilities	548,888	40,695	-	589,583
Total liabilities	3,282,444	499,571	(100,236)	3,681,779
Net assets				
Without donor restrictions - attributable to Novant Health	4,164,059	769,155	(127,403)	4,805,811
Without donor restrictions - noncontrolling interests	-	23,405	55,847	79,252
Total net assets without donor restrictions	4,164,059	792,560	(71,556)	4,885,063
With donor restrictions	2,178	82,658	-	84,836
Total net assets	4,166,237	875,218	(71,556)	4,969,899
Total liabilities and net assets	<u>\$ 7,448,681</u>	<u>\$ 1,374,789</u>	<u>\$ (171,792)</u>	<u>\$ 8,651,678</u>

See accompanying notes to consolidating supplemental schedules.

Novant Health, Inc.
Consolidating Statement of Operations
Year Ended December 31, 2020

<i>(in thousands of dollars)</i>	Combined Group	Unrestricted Affiliates	Eliminations	Total
Operating revenues and other support				
Net patient service revenues	\$ 4,498,761	\$ 554,033	\$ -	\$ 5,052,794
Other revenue	<u>433,191</u>	<u>269,259</u>	<u>(72,469)</u>	<u>629,981</u>
Total operating revenues and other support	<u>4,931,952</u>	<u>823,292</u>	<u>(72,469)</u>	<u>5,682,775</u>
Operating expenses				
Salaries and employee benefits	2,770,074	319,369	(6,335)	3,083,108
Supplies and other	1,670,067	473,352	(70,329)	2,073,090
Depreciation and amortization expense	215,959	44,092	-	260,051
Interest expense	<u>68,688</u>	<u>9,334</u>	<u>-</u>	<u>78,022</u>
Total operating expenses	<u>4,724,788</u>	<u>846,147</u>	<u>(76,664)</u>	<u>5,494,271</u>
Operating income (loss)	207,164	(22,855)	4,195	188,504
Non-operating income (expense)				
Investment income	181,492	20,331	-	201,823
Loss on extinguishment of debt	(6,208)	-	-	(6,208)
Income tax (expense) benefit	1,782	(2,287)	-	(505)
Other net periodic pension costs	<u>(1,466)</u>	<u>7</u>	<u>-</u>	<u>(1,459)</u>
Excess (deficit) of revenues over expenses	<u>\$ 382,764</u>	<u>\$ (4,804)</u>	<u>\$ 4,195</u>	<u>\$ 382,155</u>

See accompanying notes to consolidating supplemental schedules.

Novant Health, Inc.
Combined Group Combining Balance Sheet
December 31, 2020

<i>(in thousands of dollars)</i>	Obligated Group	Restricted Affiliates	Eliminations	Combined Group Total
Assets				
Current assets				
Cash and cash equivalents	\$ 486,401	\$ 69,778	\$ -	\$ 556,179
Accounts receivable, net of allowance for doubtful accounts	488,177	92,262	-	580,439
Short-term investments	330,582	-	-	330,582
Current portion of assets limited as to use	30,029	-	-	30,029
Receivable for settlement with third-party payors	9,016	12,113	-	21,129
Other current assets	177,893	56,493	-	234,386
Total current assets	1,522,098	230,646	-	1,752,744
Assets limited as to use	202,985	696	-	203,681
Long-term investments	2,640,842	-	-	2,640,842
Property and equipment, net	1,482,695	576,350	-	2,059,045
Operating lease right-of-use assets, net	267,190	253,532	-	520,722
Intangible assets and goodwill, net	49,242	11,922	-	61,164
Investments in affiliates	186,667	(4,518)	(86,653)	95,496
Other assets	107,694	23,952	(16,659)	114,987
Total assets	\$ 6,459,413	\$ 1,092,580	\$ (103,312)	\$ 7,448,681
Liabilities and Net Assets				
Current liabilities				
Current portion of long-term debt	\$ 50,731	\$ 3,237	\$ -	\$ 53,968
Short-term borrowings	149,300	-	-	149,300
Accounts payable	235,397	22,012	-	257,409
Accrued liabilities	396,944	195,204	-	592,148
Operating lease liabilities	41,776	44,281	-	86,057
Estimated third-party payor settlements	49,728	28,683	-	78,411
Due to (from) related organizations	(538,654)	291,262	-	(247,392)
Total current liabilities	385,222	584,679	-	969,901
Long-term debt, net of current portion	1,120,766	158,469	(16,659)	1,262,576
Operating lease liabilities, net of current portion	234,241	215,035	-	449,276
Derivative financial instruments	51,803	-	-	51,803
Employee benefits and other liabilities	466,491	82,397	-	548,888
Total liabilities	2,258,523	1,040,580	(16,659)	3,282,444
Net assets				
Without donor restrictions - attributable to Novant Health	4,200,890	49,822	(86,653)	4,164,059
With donor restrictions	-	2,178	-	2,178
Total net assets	4,200,890	52,000	(86,653)	4,166,237
Total liabilities and net assets	\$ 6,459,413	\$ 1,092,580	\$ (103,312)	\$ 7,448,681

See accompanying notes to consolidating supplemental schedules.

Novant Health, Inc.
Combined Group Combining Statement of Operations
Year Ended December 31, 2020

<i>(in thousands of dollars)</i>	Obligated Group	Restricted Affiliates	Eliminations	Combined Group Total
Operating revenues and other support				
Net patient service revenues	\$ 2,734,776	\$ 1,763,985	\$ -	\$ 4,498,761
Other revenue	292,073	169,197	(28,079)	433,191
Total operating revenues and other support	<u>3,026,849</u>	<u>1,933,182</u>	<u>(28,079)</u>	<u>4,931,952</u>
Operating expenses				
Salaries and employee benefits	1,531,409	1,238,665	-	2,770,074
Supplies and other	1,065,513	632,633	(28,079)	1,670,067
Depreciation and amortization expense	134,344	81,615	-	215,959
Interest expense	44,372	24,316	-	68,688
Total operating expenses	<u>2,775,638</u>	<u>1,977,229</u>	<u>(28,079)</u>	<u>4,724,788</u>
Operating income (loss)	251,211	(44,047)	-	207,164
Non-operating income (expense)				
Investment income	181,421	71	-	181,492
Loss on extinguishment of debt	(6,208)	-	-	(6,208)
Income tax benefit	1,778	4	-	1,782
Other net periodic pension costs	(325)	(1,141)	-	(1,466)
Excess (deficit) of revenues over expenses	<u>\$ 427,877</u>	<u>\$ (45,113)</u>	<u>\$ -</u>	<u>\$ 382,764</u>

See accompanying notes to consolidating supplemental schedules.

Novant Health, Inc.
Notes to Consolidating or Combining Supplemental Schedules
December 31, 2020

1. Consolidated Financial Statements Reporting Entity

Novant Health, Inc. (“Novant Health” or the “Company”) is a nonprofit, integrated health care network of physician clinics, outpatient facilities and hospitals that serves patients and communities in North Carolina, Virginia and South Carolina. Novant Health consists of over 1,600 physicians and 29,000 team members at nearly 700 locations, including 15 medical centers and hundreds of outpatient facilities and physician clinics. Headquartered in Winston-Salem, North Carolina, Novant Health is committed to making healthcare remarkable for patients and communities, serving more than 5 million patients annually. Novant Health and its affiliates serve their communities with programs including health education, home health care, prenatal clinics, community clinics and immunization services.

2. Basis of Presentation and Summary of Significant Accounting Policies

Novant Health, Inc. Consolidating Balance Sheet and Consolidating Statement of Operations (which Combines the Information of the Combined Group and Unrestricted Affiliates)

The Total column reconciles to the consolidated financial statements of Novant Health, Inc. and includes the accounts of all affiliates controlled by Novant Health, Inc. The Total is comprised of the Combined Group (as described below, which is comprised of the Obligated Group and Restricted Affiliates) and the Unrestricted Affiliates, which represent affiliates not meeting the definition of the Obligated Group or Restricted Affiliates as defined below.

The Eliminations column represents the elimination of intercompany transactions and balances between the Combined Group and the Unrestricted Affiliates.

The consolidating balance sheet and consolidating statement of operations are otherwise prepared in accordance with accounting policies described in the accompanying notes to the consolidated financial statements. These schedules are not intended to be a presentation in accordance with accounting principles generally accepted in the United States of America, as a result of the exclusion of all required disclosures.

Combined Group Combining Balance Sheet and Statement of Operations

As noted in Note 16 to the consolidated financial statements, the Company is subject to a Master Trust Indenture (the “Agreement”) which authorizes the creation of a Combined Group, which consists of the members of the Obligated Group and the Restricted Affiliates.

The members of the Obligated Group are jointly and severally liable for the payment of all obligations under the Agreement. The members of the Obligated Group are Novant Health and its two affiliates that operate tertiary care hospitals, Forsyth Memorial Hospital, Inc. d/b/a Novant Health Forsyth Medical Center and The Presbyterian Hospital d/b/a Novant Health Presbyterian Medical Center, both of which are North Carolina nonprofit corporations. In the accompanying Combined Group combining balance sheet and combining statement of operations, the Obligated Group column presents information of the aforementioned entities.

Novant Health, Inc.
Notes to Consolidating or Combining Supplemental Schedules
December 31, 2020

Restricted Affiliates represent entities that are not directly obligated to pay obligations under the Agreement, but the members of the Obligated Group have covenanted in the Agreement to cause the Restricted Affiliates to provide funds to the members of the Obligated Group to pay obligations under the Agreement. The Company has designated twelve of its affiliates as Restricted Affiliates. Seven of these Restricted Affiliates, Medical Park Hospital, Inc. d/b/a Novant Health Medical Park Hospital, Community General Health Partners, Inc. d/b/a Novant Health Thomasville Medical Center, Presbyterian Medical Care Corp. d/b/a Novant Health Matthews Medical Center, Brunswick Community Hospital d/b/a Novant Health Brunswick Medical Center, Mint Hill Medical Center, LLC d/b/a Novant Health Mint Hill Medical Center, Prince William Hospital Corporation d/b/a Novant Health UVA Prince William Medical Center, and Prince William Health System, operate, or maintain a significant investment in, hospitals. The other five Restricted Affiliates, Carolina Mediacorp Enterprises, Inc., Forsyth Medical Group, LLC, Foundation Health Systems Corp., Novant Medical Group, Inc. f/k/a Presbyterian Regional Healthcare Corp. and Salem Health Services, Inc., provide, or invest in subsidiaries or joint ventures which provide health care and ancillary services. All of the members of the Combined Group, except Salem Health Services, Inc., are exempt from federal and state income taxation.

The Eliminations column represents the elimination of intercompany transactions and balances between the Obligated Group and the Restricted Affiliates.

The Combined Group combining balance sheet and combining statement of operations are otherwise prepared in accordance with accounting policies described in the accompanying notes to the consolidated financial statements. These schedules are not intended to be a presentation in accordance with accounting principles generally accepted in the United States of America, as a result of the exclusion of all required disclosures.