

CONSOLIDATED FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION

City of Hope
Years Ended September 30, 2019 and 2018
With Report of Independent Auditors

Ernst & Young LLP



City of Hope

Consolidated Financial Statements and Supplementary Information

Years Ended September 30, 2019 and 2018

Contents

Report of Independent Auditors 1

Consolidated Financial Statements

Consolidated Statements of Financial Position 3

Consolidated Statements of Activities 5

Consolidated Statements of Cash Flows 7

Notes to Consolidated Financial Statements 9

Supplementary Information

Consolidating Statements of Financial Position 59

Consolidating Statements of Activities 61



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Report of Independent Auditors

The Board of Directors
City of Hope

We have audited the accompanying consolidated financial statements of City of Hope, which comprise the consolidated statements of financial position as of September 30, 2019 and 2018, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

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

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

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

Opinion

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

Adoption of ASU No. 2014-09, *Revenue from Contracts with Customers*, and ASU No. 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities*

As discussed in Note 2 to the consolidated financial statements, City of Hope changed its method of revenue recognition in 2019 as a result of the adoption of amendments to the FASB Accounting Standards Codification resulting from Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers*, effective October 1, 2018, and adopted the amendments to the FASB Accounting Standards Codification resulting from Accounting Standards Update No. 2016-14, *Not-for-Profit Entities: Presentation of Financial Statements of Not-for-Profit Entities*, effective September 30, 2019. Our opinion is not modified with respect to these matters.

Supplementary Information

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

Ernst & Young LLP

December 20, 2019

City of Hope

Consolidated Statements of Financial Position
(In Thousands)

	September 30	
	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 238,535	\$ 377,571
Investments	1,927,425	1,526,106
Self-insurance trust funds	3,418	3,765
Patient accounts receivable, net (less allowance for uncollectible accounts of \$10,916 in 2018)	235,989	238,384
Grants and other receivables	158,176	95,981
Due from third-party payors	–	342
Donor-restricted unconditional promises to give, net	24,449	18,576
Prepaid and other	47,151	39,105
Total current assets	<u>2,635,143</u>	<u>2,299,830</u>
Property and equipment, net	977,718	930,236
Other assets:		
Investments held for long-term purposes	237,564	302,822
Board-designated assets	895,110	884,127
Bond trust funds	380,242	–
With donor restrictions:		
Investments	557,136	518,251
Unconditional promises to give, net	45,587	60,741
Contributions receivable from annuity and split-interest agreements, net	15,716	13,182
Other	3,565	9,452
Intangible assets	10,038	10,667
Goodwill	53,160	59,067
Other long-term assets	58,657	47,428
Total other assets	<u>2,256,775</u>	<u>1,905,737</u>
Total assets	<u><u>\$ 5,869,636</u></u>	<u><u>\$ 5,135,803</u></u>

	September 30	
	2019	2018
Liabilities and net assets		
Current liabilities:		
Accounts payable and other accrued liabilities	\$ 198,081	\$ 150,553
Accrued salaries, wages, and employee benefits	107,833	87,473
Long-term debt, current portion	13,492	13,051
Deferred revenue	28,781	28,404
Due to third-party payors	25,675	—
Total current liabilities	<u>373,862</u>	<u>279,481</u>
Long-term debt, net of current portion	1,373,657	1,003,810
Annuity and split-interest agreement obligations	19,068	20,464
Deferred rent	5,904	10,146
Interest rate swaps	19,489	6,549
Other	57,113	60,115
Total liabilities	<u>1,849,093</u>	<u>1,380,565</u>
Net assets:		
Without donor restrictions:		
Controlling interests	3,363,779	3,127,206
Noncontrolling interest	32,298	35,100
With donor restrictions	624,466	592,932
Total net assets	<u>4,020,543</u>	<u>3,755,238</u>
Total liabilities and net assets	<u><u>\$ 5,869,636</u></u>	<u><u>\$ 5,135,803</u></u>

See accompanying notes.

City of Hope

Consolidated Statement of Activities

(In Thousands)

Year Ended September 30, 2019

	Without Donor Restrictions	With Donor Restrictions	Total
Revenues, gains, and other support:			
Net patient service revenues	\$ 1,555,575	\$ –	\$ 1,555,575
Research grants, contracts, and clinical trials	169,314	–	169,314
Contributions	59,250	92,178	151,428
Investment income	206,678	33,324	240,002
Net unrealized loss on investments	(136,280)	(14,190)	(150,470)
Royalty and licensing revenue	384,514	–	384,514
Other revenue	56,458	79	56,537
Total revenues and gains	2,295,509	111,391	2,406,900
Net assets released from restrictions	79,237	(79,237)	–
Total revenues, gains, and other support	2,374,746	32,154	2,406,900
Expenses:			
Salaries, wages, and employee benefits	826,095	–	826,095
Purchased services and professional fees	465,792	–	465,792
Supplies and pharmaceuticals	514,663	–	514,663
Royalty sharing	118,445	–	118,445
Interest, including changes in fair value of swap agreements	59,888	–	59,888
Depreciation and amortization	140,306	–	140,306
Hospital provider fee	15,735	–	15,735
Other expense	85,158	620	85,778
Total expenses	2,226,082	620	2,226,702
Excess of revenues, gains, and other support over expenses	148,664	31,534	180,198
Distribution to noncontrolling interest	(2,037)	–	(2,037)
Cumulative changes in net assets from adoption of new accounting standards	87,144	–	87,144
Changes in net assets	233,771	31,534	265,305
Net assets, beginning of year	3,162,306	592,932	3,755,238
Net assets, end of year	\$ 3,396,077	\$ 624,466	\$ 4,020,543

See accompanying notes.

City of Hope

Consolidated Statement of Activities

(In Thousands)

Year Ended September 30, 2018

	Without Donor Restrictions	With Donor Restrictions	Total
Revenues, gains, and other support:			
Net patient service revenues	\$ 1,375,498	\$ –	\$ 1,375,498
Research grants, contracts, and clinical trials	152,821	–	152,821
Contributions	76,740	86,475	163,215
Investment income	166,039	18,273	184,312
Net unrealized gain on investments	20,794	6,473	27,267
Royalty and licensing revenue	500,370	–	500,370
Other revenue	44,283	283	44,566
Total revenues and gains	2,336,545	111,504	2,448,049
Net assets released from restrictions	62,564	(62,564)	–
Total revenues, gains, and other support	2,399,109	48,940	2,448,049
Expenses:			
Salaries, wages and employee benefits	740,439	–	740,439
Purchased services and professional fees	451,739	–	451,739
Supplies and pharmaceuticals	424,740	–	424,740
Royalty sharing	155,376	–	155,376
Interest, including changes in fair value of swap agreements	32,535	–	32,535
Depreciation and amortization	126,298	–	126,298
Hospital provider fee	40,836	–	40,836
Other expense	91,189	–	91,189
Total expenses	2,063,152	–	2,063,152
Excess of revenues, gains, and other support over expenses	335,957	48,940	384,897
Contributed capital noncontrolling interest	34,911	–	34,911
Cumulative changes in net assets from adoption of new accounting standards	2,945	(2,945)	–
Changes in net assets	373,813	45,995	419,808
Net assets, beginning of year	2,788,493	546,937	3,335,430
Net assets, end of year	<u>\$ 3,162,306</u>	<u>\$ 592,932</u>	<u>\$ 3,755,238</u>

See accompanying notes.

City of Hope

Consolidated Statements of Cash Flows (In Thousands)

	Year Ended September 30	
	2019	2018
Operating activities		
Changes in net assets	\$ 265,305	\$ 419,808
Adjustments to reconcile changes in net assets to net cash used in operating activities:		
Depreciation and amortization	140,306	126,298
Amortization of bond cost, discount and premium	(1,604)	(1,313)
Contributed capital, noncontrolling interest	–	(34,911)
Distribution to noncontrolling interest	2,037	–
Provision for bad debt	–	8,481
Net unrealized loss (gain) on investments	150,470	(27,267)
Change in fair value of interest rate swaps	12,940	(3,718)
Contribution proceeds restricted for endowment	(13,430)	(20,193)
Other	96	(3,646)
Changes in assets and liabilities:		
Patient accounts receivable, net	2,395	(324)
Grants and other receivables	(62,195)	(35,569)
Unconditional promises to give, net	9,281	24,118
Contributions receivable from annuity and split-interest agreements	(2,534)	441
Other assets	(13,670)	(2,351)
Accounts payable and accrued liabilities	40,513	(51,897)
Accrued salaries, wages, and employee benefits	20,361	18,690
Annuity and split-interest agreement obligations	(1,396)	1,884
Other liabilities	30,040	9,078
Net cash provided by operating activities before net purchases of trading investments	578,915	427,609
Net purchases of trading investments	(944,560)	(509,622)
Net cash used in operating activities	(365,645)	(82,013)
Investing activities		
Increase in notes receivable	(150)	(194)
Additions to property and equipment	(180,919)	(110,085)
Cash paid to SCRO noncontrolling interest	–	(23,494)
Proceeds from sale of contributed real property held for sale	407	3,121
Net sales of alternative investments	28,263	73,026
Net cash used in investing activities	(152,399)	(57,626)

City of Hope

Consolidated Statements of Cash Flows (continued) (In Thousands)

	Year Ended September 30	
	2019	2018
Financing activities		
Proceeds from long-term debt borrowing, net	\$ 382,660	\$ 298,555
Principal payments on long-term debt	(13,740)	(15,350)
Bond issuance costs	(1,305)	(1,057)
Working capital contribution, noncontrolling interest	–	2,802
Distribution to noncontrolling interest	(2,037)	–
Contribution proceeds restricted for endowment	13,430	20,193
Net cash provided by financing activities	379,008	305,143
Net (decrease) increase in cash and cash equivalents	(139,036)	165,504
Cash and cash equivalents, beginning of year	377,571	212,067
Cash and cash equivalents, end of year	\$ 238,535	\$ 377,571
Supplemental disclosure of cash flow information		
Interest paid during the year (net of capitalized interest)	\$ 46,324	\$ 36,752
Supplemental disclosure of noncash activity		
Assets constructed by landlord	\$ –	\$ 10,891
Capital lease obligation	\$ 4,278	\$ 48,045
Additions to property and equipment included in accounts payable and accrued liabilities	\$ 25,932	\$ 45,088
Noncash consideration from noncontrolling interest	\$ –	\$ 32,110

See accompanying notes.

City of Hope

Notes to Consolidated Financial Statements

September 30, 2019

1. Organization

City of Hope, a California nonprofit public benefit corporation, with its principal office located in Duarte, California, is the development organization of City of Hope National Medical Center (the Center), City of Hope Medical Foundation (the Foundation), Beckman Research Institute of the City of Hope (the Institute) (collectively, the Obligated Group), The Translational Genomics Research Institute and its Affiliates (TGen), Southern California Radiation Oncology, LLC (SCRO), Access City of Hope, LLC (ACOH) and City of Hope Auxiliaries (the Auxiliaries) (collectively, the Affiliated Group). These entities represent the consolidated City of Hope organization (collectively referred to as City of Hope). City of Hope's management and staff coordinate the fundraising activities of the many volunteers and donors needed to support the patient care and research mission of the City of Hope.

The Center, located in Duarte, California, is a California nonprofit public benefit corporation treating primarily cancer and other life-threatening diseases. The Center currently operates a 186-bed tertiary referral center with a licensed capacity of 217 beds. City of Hope is the sole corporate member of the Center.

The Foundation, located in Duarte, California, is a California nonprofit public benefit corporation organized as part of a coordinated health care delivery system to provide teaching, education, and research services in support of the Center and the Institute. The Foundation also owns and/or operates outpatient clinic facilities that provide an extensive range of medical care and treatment. City of Hope is the sole corporate member of the Foundation.

The Foundation has entered into a professional services agreement with the City of Hope Medical Group (COHMG), an unconsolidated medical group. Under the terms of the professional services agreement, COHMG physicians provide exclusive patient care services and academic services, such as teaching, administration, and research to the Foundation. As part of City of Hope's goal of creating greater integration and coordination of City of Hope's patient care, research, and educational services, the Foundation provides for, or arranges for, the provision of certain patient care and on-call coverage services and teaching, administration, and research for the operations and activities of the Center pursuant to an agreement between the Foundation and the Center. The professional fee revenue and expense associated with the contract between the Foundation and the Center are eliminated in consolidation.

City of Hope

Notes to Consolidated Financial Statements (continued)

1. Organization (continued)

Pursuant to the professional services agreement, COHMG assigns to the Foundation the right to bill and collect for professional services rendered by COHMG physicians and other professional employees, and the Foundation contracts directly with payors for the provision of patient care services. Accordingly, net patient service revenues for the Foundation include amounts for services provided by COHMG physicians on behalf of the Foundation.

The Institute, located in Duarte, California, is a California nonprofit public benefit corporation that owns and operates several major research facilities on or near City of Hope's main campus. The Institute conducts basic scientific research in support of, and in conjunction with, the patient care activities of the Center and the Foundation. City of Hope is the sole corporate member of the Institute.

TGen, located in Phoenix, Arizona, is an Arizona nonprofit public benefit corporation that translates genomic discoveries into advances in human health. TGen employs innovative advances arising from the Human Genome Project and applies them to the development of diagnostics. The accounts of TGen include the assets, liabilities, and results of operations of TGen Foundation and certain other controlled entities that were created to support TGen through its various functions. City of Hope is the sole corporate member of TGen (the Affiliation).

SCRO, a California for-profit joint venture, was formed on March 30, 2018, between the Foundation and Vantage Oncology Treatment Centers, LLC (Vantage) to manage and provide services to nine freestanding radiation therapy centers in Southern California. The Foundation owns 50.1%, and Vantage owns 49.9% of SCRO (see Note 7).

ACOH, located in Irwindale, California, is a Delaware single-member, limited liability company that provides or arranges for the provision, to employers and payers throughout the United States, of certain oncology-related consultative, advisory, and support services designed to address the specific cancer needs of patients, improve care outcomes and drive value. City of Hope is the single member of ACOH (see Note 6).

The Auxiliaries, located throughout the United States, are nonprofit public benefit unincorporated associations that coordinate fundraising activities to support the mission of City of Hope.

City of Hope

Notes to Consolidated Financial Statements (continued)

1. Organization (continued)

Principles of Consolidation

The accompanying consolidated financial statements of City of Hope include the accounts of the Obligated Group and the Affiliated Group. All intercompany accounts and transactions have been eliminated in the consolidated financial statements. The consolidated financial statements of City of Hope have been prepared in accordance with U.S. generally accepted accounting principles (GAAP).

2. Summary of Significant Accounting Policies

New Accounting Standards Adopted

Effective October 1, 2018, City of Hope adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*, using the modified retrospective method of transition. ASU 2014-09 consolidated and replaced existing revenue recognition guidance, including industry-specific guidance, and requires revenue to be recognized in an amount that reflects the consideration to which the entity expects to be entitled in an exchange of goods or services. Refer to Note 2 – Royalty and Licensing Revenue for further information.

Effective September 30, 2019, City of Hope adopted ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. ASU 2016-14 changes certain financial statement requirements for not-for-profit entities in an effort to make the information more meaningful to users and reduce reporting complexity. The guidance provides more information in the notes to the consolidated financial statements concerning liquidity, financial performance, and cash flows. The guidance also includes presenting two classes of net assets, those without donor restrictions and those with donor restrictions, and recognition of underwater endowment funds as a reduction in net assets with donor restrictions.

ASU 2016-14 has been applied retrospectively to all periods presented (except for prior-year liquidity and availability of resources to which City of Hope elected to apply the practical expedient and not disclose). As a result of the adoption of ASU 2016-14, City of Hope recorded a net asset adjustment for \$2,945,000 and a reclass of \$1,362,000 from other revenue with donor restrictions to other revenue without donor restrictions for the year ended September 30, 2018. Additionally, net assets released from restrictions was increased by \$1,018,000 to account for net assets released under the placed-in-service approach of ASU 2016-14 for the year ended September 30, 2018.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Effective October 1, 2018, City of Hope adopted ASU 2017-04, *Intangibles – Goodwill and Other*. ASU 2017-04 eliminates Step 2 of the goodwill impairment test and requires a goodwill impairment to be measured as the amount by which the reporting unit's carrying amount exceeds its fair value, not to exceed the carrying amount of its goodwill. City of Hope elected to early adopt ASU 2017-04 for the year ended September 30, 2019.

Additionally, City of Hope has made the election to apply the goodwill accounting alternative in Accounting Standards Codification (ASC) 350, *Intangibles – Goodwill and Other*, and the intangible asset accounting alternative in ASC 805, *Business Combinations*, that were previously only available to private companies. As such, City of Hope began amortizing its goodwill as of October 1, 2018, the beginning of the period of adoption, on a straight-line basis over ten years. City of Hope will perform a one-step impairment test at the reporting unit level when an impairment indicator exists.

Effective October 1, 2018, City of Hope adopted ASU 2018-08, *Not-for-Profit Entities – Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made*. ASU 2018-08 provides a greater framework to determine when a transaction should be accounted for as a contribution or as an exchange transaction, and it provides additional guidance about how to determine whether a contribution is conditional. Grants that are not exchange transactions are now reported in contributions. The adoption of ASU 2018-08 resulted in approximately \$13,000,000 in nonexchange transactions moving from grants, contracts and clinical trials to contributions with or without donor restrictions for the year ended September 30, 2019.

New Accounting Standards Not Yet Adopted

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, which amends the accounting and disclosures of financial instruments, including a provision that requires equity investments (except for investments accounted for under the equity method of accounting) to be measured at fair value, with changes in fair value recognized in current earnings. ASU 2016-01 is effective for interim and annual periods beginning after December 15, 2018. City of Hope is evaluating the effect of this standard on the consolidated financial statements.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which amends the existing accounting standards for lease accounting, including requiring lessees to recognize most leases on their balance sheets and making targeted changes to lessor accounting. The new standard, effective October 1, 2019, requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application, with an option to use certain transition relief. In July 2018, the FASB issued ASU 2018-11, *Leases (Topic 842): Targeted Improvements*, which further amended this standard to allow for a new transition method that provides the option to use the effective date as the date of initial application. This guidance simplifies transition requirements, which allows for an option to apply the transition provisions of the new standard at its adoption date instead of at the earliest comparative period presented in its financial statements. It also provides a practical expedient for the separation of non-lease components from lease components. City of Hope intends to elect the package of practical expedients and the practical expedient to not separate lease and non-lease components. City of Hope also intends to elect the practical expedient to reflect the adoption as of the adoption date as opposed to the earliest period presented in the financial statement period of adoption. The primary effect of adopting the standard will be to record right-of-use assets and the corresponding present value of lease obligations for leases classified as operating leases under current guidance, which will have a material impact on the consolidated statements of financial position and significant incremental disclosures to the notes to the consolidated financial statements. The standard will not have a material impact on City of Hope's consolidated statements of activities or cash flows. City of Hope will adopt the standard on October 1, 2019.

Use of Estimates

The preparation of City of Hope's consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Principal areas requiring the use of estimates include recognition of net patient service revenue, which includes contractual discounts and adjustments, price concessions and charity care; valuation of unconditional promises to give; cost report settlements and amounts due to/from third-party payors; valuation of annuity and split-interest agreement obligations; fair value of interest rate swap agreements; fair value of business combinations; impairment of goodwill and other intangibles; and self-insured liabilities. City of Hope bases its estimates on historical experience and various other assumptions that it believes are reasonable under the particular circumstances. Actual results could differ from those estimates, and the amounts could be material to the consolidated financial statements.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Performance Indicator

Management considers changes in net assets to be the performance indicator.

Reclassifications

Certain reclassifications were made to the accompanying 2018 consolidated financial statements to conform to the 2019 presentation. These reclassifications had no impact on total assets; total liabilities; the changes in net assets; or excess of revenues, gains, and other support over expenses previously reported and are not considered material to the consolidated financial statements of City of Hope.

Cash and Cash Equivalents

Cash and cash equivalents reflect all unrestricted cash and cash equivalents that include highly liquid investments with original or remaining maturities of three months or less from the date of purchase and exclude amounts whose use is limited under contractual or donor agreements.

Cash and cash equivalents that are held as a component of donor restricted assets are reflected in donor-restricted investments on the accompanying consolidated statements of financial position. Cash and cash equivalents are also held as components of investments held for long-term purposes, board-designated assets, and bond trust funds on the accompanying consolidated statements of financial position.

Cash is held in depository accounts at various financial institutions. The combined account balance at any given institution may exceed the Federal Deposit Insurance Corporation (FDIC) insurance coverage of \$250,000, and, as a result, there is a concentration of credit risk related to amounts on deposit over the FDIC insurance coverage. Management believes, based on the quality of the financial institutions, that the risk is not significant.

Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value on the consolidated statements of financial position (see Note 3). These equity and debt securities are designated as trading securities, since the investments are externally managed within the guidelines of City of Hope's investment policy. Fair value is

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

established based on quoted prices from recognized security exchanges. Accordingly, the change in unrealized gains and losses on investments is reported within the excess of revenues, gains, and other support over expenses on the consolidated statements of activities. Management considers the settlement date to be the valuation date when investments are purchased and sold.

Investment income or loss on equity and debt securities included in net assets with donor restrictions (including realized gains and losses on investments, interest, and dividends) is reported in revenues without donor restrictions, unless the income or loss is specifically restricted by the donor or by law.

City of Hope's alternative investments consist of limited partnerships and limited liability companies that seek to limit the effect of downward market swings on the portfolio and are not restricted to any particular asset class. Some alternative investments invest in other similar partnerships or funds and employ a "fund of funds" strategy, while other alternative investments have specific industry focus in their investment assets. At an investment manager's direction, these alternative investments may invest in both registered and non-registered securities in the U.S. and globally, with exposure to both emerging and developed markets. These entities employ a range of investment strategies, including, but not limited to, long or short equity positions, derivatives, forward and futures contracts, and currency hedges.

City of Hope's alternative investments include equity commingled funds that invest primarily in marketable securities. These funds are subject to certain notice requirements but can be liquidated at least monthly.

City of Hope's hedge fund investments consist of direct and multimanager hedge fund "fund of funds" investments, which implement a range of alternative investment strategies, including, but not limited to, long or short equity, credit, and other strategies. Investments in hedge funds have limited liquidity, since shares or interests in the hedge funds are not freely transferable and are subject to various lockup periods, redemption fees, and notice requirements. In addition, the hedge funds typically reserve the right to reduce or suspend redemptions (gating event) and to satisfy redemptions by making distributions in kind, under certain circumstances. Additionally, hedge funds may hold, directly or indirectly, side-pocket investments where no redemptions are permitted until such investments are liquidated or deemed realized. Redemption clauses range from monthly to quarterly and annually with various notice requirements between 30 and 90 days.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

City of Hope's private equity investments consist of direct and private equity fund of funds investments, including private equity buyout, venture capital, mezzanine, and secondary private equity funds. These private equity investments typically have investment terms greater than ten years. City of Hope may not withdraw, sell, assign, or transfer its interests in the private equity funds, except under very limited circumstances, subject to consent by the general partners of the funds.

City of Hope's public and private real asset investments consist of funds that invest in timberland properties, global real estate investment trusts securities, real estate operating company securities, distressed real estate, energy funds, fund of funds, and master limited partnerships. The investment terms of these investment funds are typically greater than ten years and City of Hope may not withdraw or sell, assign, or transfer its interests in these funds except in certain very limited circumstances, subject to consent by the general partners of the funds.

City of Hope invests in private equity and private real asset funds that may be structured as drawdown funds, to which City of Hope has committed to fund future capital calls as the investment opportunities develop over the initial investment period established by the fund managers. Based upon the most recent available information, the outstanding unfunded commitments as of September 30 totaled (amounts in thousands):

	<u>2019</u>	<u>2018</u>
Private equity	\$ 239,300	\$ 244,300
Private real assets:		
Real estate	138,300	103,600
Natural resources	33,700	40,500
Total unfunded commitments	<u>\$ 411,300</u>	<u>\$ 388,400</u>

City of Hope accounts for its ownership interests in alternative investments at fair value, under which the net asset value (NAV) is used as a practical expedient to fair value on the accompanying consolidated statements of financial position and its changes in fair value and share of earnings are included in net unrealized gain or loss on investments on the consolidated statements of activities. Ownership interest in these funds ranges between .004% and 33.01% as of September 30, 2019.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Patient Accounts Receivable and Patient Service Revenue

The Center and the Foundation receive payments for services rendered to patients from federal and state governmental programs, mainly Medicare and Medi-Cal, privately sponsored managed care programs (including Medicare and Medi-Cal managed care) for which payment is made based on terms defined under formal contracts, and other payors. City of Hope recognizes that revenues and receivables from government agencies are significant to its operations, but it does not believe there are significant credit risks associated with these government agencies. City of Hope does not believe there are any other significant concentrations of revenues and receivables from any particular payor that would subject City of Hope to any significant credit risks in the collection of accounts receivable. Changes in general economic conditions, patient accounting operations, payor mix, or federal or state governmental health care coverage could affect the collection of accounts receivable, cash flows, and results of operations. The following table summarizes the percentages of gross accounts receivable from patients and third-party payors as of September 30:

	<u>2019</u>	<u>2018</u>
Medicare	22%	24%
Medi-Cal	13	13
Managed care (including Medicare and Medi-Cal managed care	63	61
Indemnity, self-pay, and other	2	2
	<u>100%</u>	<u>100%</u>

Net patient service revenues are reported at the amount that reflects the consideration to which the Center and the Foundation expect to be entitled in exchange for providing patient care. These amounts, representing transaction price, are due from patients, third-party payors (including health insurers and government programs), and others and includes variable consideration for retroactive revenue adjustments due to settlement of third-party payor audits or reviews. Patients and third-party payors are billed after the services are performed and/or the patient is discharged from the facility. The Center and the Foundation recognize revenue as performance obligations are satisfied.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Performance obligations are determined based on the nature of the services provided by the Center and the Foundation. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to the total expected. The Center and the Foundation believe this method provides a reasonable depiction of the transfer of services over the term of the performance obligation based on the inputs necessary to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in the Center receiving inpatient care services. The Center measures the performance obligation from admission to the hospital to the point when it is no longer required to provide goods or services to the patient for that admission, which is generally at the time of discharge.

Substantially all performance obligations relate to contracts with a duration of less than one year; as such, the Center and the Foundation have elected to apply the optional exemption provided in ASC 606-10-50-14(a) and are not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations are primarily related to inpatient care services whose performance obligation for these contracts are generally completed when the patients are discharged, which often occurs within weeks of the end of the reporting period.

Transaction prices are determined based on standard charges for goods and services provided to patients and are reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with the Center's and the Foundation's charity policies, and/or implicit price concessions based on historical collection experience.

City of Hope's policy includes the evaluation of a patient's ability to pay. The allowances for contractual discounts and uncollectible accounts have been determined based on historical collection data and other factors, including changes to contract terms. As a result of certain changes required by ASU 2014-09, the majority of City of Hope's provision for uncollectible accounts is recorded as a direct reduction to net patient service revenue instead of being presented as a component of expenses on the consolidated statements of activities for the year ended September 30, 2019. The adoption of ASU 2014-09 had no material impact on City of Hope's patient receivables.

The Center and the Foundation have agreements with third-party payors that provide for payments to the Center and the Foundation at amounts different from established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

charges, per diem payments, case rates, and specialized fee schedules. Estimated retroactive adjustments under the Medicare and Medi-Cal programs are also reflected in patient service revenues. Net patient service revenues for the years ended September 30 are as follows (amounts in thousands):

	<u>2019</u>	<u>2018</u>
Medicare	\$ 317,497	\$ 269,817
Medi-Cal	133,617	205,364
Managed care (including Medicare and Medi-Cal managed care)	1,082,963	878,091
Indemnity, self-pay, and other	21,498	22,226
Patient service revenues	<u>\$ 1,555,575</u>	<u>\$ 1,375,498</u>

The Center and the Foundation are reimbursed for services provided to patients under certain programs administered by governmental agencies. Laws and regulations governing the Medicare and Medi-Cal programs are complex and subject to interpretation. Compliance with such laws and regulations can be subject to future governmental review and interpretation, as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medi-Cal programs. The Center and the Foundation believe they are in compliance with all applicable laws and regulations, and they are not aware of any pending or threatened investigations involving allegations of potential wrongdoing.

Medicare reimburses the Center for cost-reimbursable items at an interim rate, and final settlements are determined after an audit of the Center's related annual cost reports by the Medicare fiscal intermediary. Estimated provisions to approximate the full expected settlements after review by the intermediary are included on the accompanying consolidated financial statements.

Expected settlement amounts are included in due to and due from third-party payors on the consolidated statements of financial position. Estimation differences between final settlements and amounts accrued in previous years are reported as adjustments of the current year's patient service revenues. In the opinion of management, adequate provision has been made for any adjustments that might result from this review. During 2019 and 2018, the Center received information requiring changes in its estimates of settlements due for certain open cost report years and appeals. Based on this information, the Center recorded a reduction to net patient service revenues totaling \$9,428,000 and \$7,761,000 for the years ended September 30, 2019 and 2018, respectively.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

During the year ended September 30, 2019, the Center and the Foundation recorded \$59,693,000 in additional net patient service revenues resulting from a change in estimate related to the collectability of patient service revenues earned prior to October 1, 2018, due to the implementation of an electronic medical record system in December 2017. This change in estimate represented additional cash collected during the year ended September 30, 2019, on the reserves for collectability on accounts receivable as of September 30, 2018.

Patient Charity Care

The Center and the Foundation approve charity care for patients meeting financial eligibility and clinical criteria at the time of admission or provision of service. A patient is classified as a charity patient by reference to certain established policies of the Center and the Foundation. Essentially, these policies define charity care as those services provided that are medically necessary but are never expected to result in cash receipts. Benefits for the indigent include services provided to persons who cannot afford health care because of inadequate resources or who are uninsured or underinsured. Also, certain medically necessary services provided to Medi-Cal patients that are not reimbursed by the Medi-Cal program have been included in the estimated cost of patient charity care. This amount is not included in net patient service revenues on the consolidated statements of activities.

The estimated cost for both patient charity care and Medi-Cal patients represents total direct and indirect cost calculated at the medical procedure level and pertains specifically to the respective charity and Medi-Cal patient populations. Procedure-level cost includes the direct costs, such as labor and supplies, involved in providing the specific service, as well as an applicable allocation of departmental overhead (e.g., departmental management) and institutional overhead (e.g., administration, depreciation, and utilities). For the years ended September 30, 2019 and 2018, these components of charity care costs totaled \$4,991,000 and \$3,351,000, respectively.

See Note 8 for additional disclosure related to benefits for the broader community and support of governmental health care programs.

California Hospital Fee Program

The State of California enacted legislation for a hospital fee program to fund certain Medi-Cal coverage expansions. The program charges hospitals a quality assurance fee that is used to obtain federal matching funds for Medi-Cal with the proceeds redistributed as supplemental payments to

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

California hospitals that treat Medi-Cal patients. There are two hospital fee programs that had activity during 2018 and 2019; a 36-month hospital fee program covering the period from January 1, 2014, through December 31, 2016, and a 30-month hospital fee program covering the period from January 1, 2017, through June 30, 2019.

The Center also entered into various enforceable pledge agreements with the California Health Foundation and Trust (CHFT), agreeing to make contributions to the CHFT based on a pre-described calculation methodology. These funds will be used by CHFT to support charitable activities at various independent hospitals and hospital/health systems in California, including measures to alleviate distortions, interruptions, and disparities potentially resulting from short-term changes in government health care reimbursement programs, including the hospital fee to be imposed on hospitals under the hospital fee program.

The Center recognized \$67,989,000 and \$149,981,000 in net patient service revenues on the accompanying consolidated statements of activities for the years ended September 30, 2019 and 2018, respectively. Additionally, the Center recognized \$15,735,000 and \$40,836,000 as expenses for the years ended September 30, 2019 and 2018, respectively, which has been reflected in hospital provider fee expense on the accompanying consolidated statements of activities.

As of September 30, 2019 and 2018, \$19,875,000 and \$47,306,000, respectively, is included in grants and other receivables and \$6,606,000 and \$9,478,000, respectively, is included in accounts payable and other accrued liabilities on the accompanying consolidated statements of financial position.

Supplies Inventory

Inventories, consisting of materials, pharmaceuticals, and medical supplies for use in program services provided by City of Hope, are stated at the lower of cost or market using the first-in, first-out method. Inventories are included in prepaid and other current assets on the consolidated statements of financial position and totaled \$22,662,000 and \$23,583,000 at September 30, 2019 and 2018, respectively.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Property and Equipment

Property and equipment are stated at cost when purchased or at fair market value on the contribution date in the case of a donation. When property and equipment are sold or otherwise disposed of, the cost and related accumulated depreciation and amortization are removed from the accounts, and any resulting gain or loss is included in other expense on the accompanying consolidated statement of activities. The costs of normal maintenance, repairs, and minor replacements are charged to expense when incurred.

City of Hope provides for depreciation and amortization using the straight-line method over the following estimated useful lives:

Buildings and improvements	7 to 40 years
Equipment and furniture	5 to 10 years
Software	3 to 5 years

Leasehold improvements are amortized on a straight-line basis over the term of the lease or estimated useful life, whichever is shorter. Leases that have been capitalized are amortized over the life of the lease. Capital lease amortization is included with depreciation and amortization expense.

A summary of the cost and accumulated depreciation and amortization of property and equipment as of September 30 is as follows (amounts in thousands):

	2019	2018
Land	\$ 17,911	\$ 17,175
Buildings and improvements	789,739	770,571
Equipment and furniture	599,576	545,598
Software	268,365	332,458
Leased capital assets	89,509	88,081
	1,765,100	1,753,883
Accumulated depreciation and amortization	(951,639)	(905,926)
	813,461	847,957
Construction in progress	164,257	82,279
Total property and equipment, net	\$ 977,718	\$ 930,236

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Total accumulated amortization for leased capital assets totaled \$22,152,000 and \$18,578,000 as of September 30, 2019 and 2018, respectively.

City of Hope reviews long-lived assets for impairment when events or changes in business conditions indicate that their carrying value may not be recoverable. Impairment is considered when the associated expected undiscounted cash flows are less than the carrying value and the assets will be written down to fair value at that time. Fair value is the present value of the associated cash flows. As of September 30, 2019, no long-lived assets are considered impaired.

Interest and Capitalized Interest

Total interest cost incurred on all financing vehicles (excluding changes in fair value of interest rate swap agreements) totaled \$49,382,000 and \$38,597,000 in 2019 and 2018, respectively. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Interest cost capitalized totaled \$2,434,000 and \$2,344,000 in 2019 and 2018, respectively.

Intangible Assets and Goodwill

Intangible assets subject to amortization is comprised of certain trade names, electronic medical records, and favorable leasehold interests totaling \$11,173,000 as of September 30, 2019 and 2018.

Goodwill resulted from the acquisition of SCRO during fiscal year 2018 and totaled \$59,067,000. City of Hope elected to begin amortizing its goodwill on October 1, 2018, the beginning of the period in which ASU 2019-06 is applicable. Amortization is applied on a straight-line basis over a period of ten years.

The accumulated amortization for intangible assets subject to amortization, including goodwill, totaled \$15,642,000 and \$9,106,000 as of September 30, 2019 and 2018, respectively. City of Hope has recorded \$6,536,000 and \$1,139,000 of amortization and rent expense for intangible assets during the years ended September 30, 2019 and 2018, respectively. Intangible assets are amortized on a straight-line basis between seven and ten years or, in the case of leasehold interests, the remaining life of the lease.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Future amortization of intangible assets subject to amortization is reflected below (amounts in thousands):

	Goodwill	Intangible Assets
2020	\$ 5,907	\$ 491
2021	5,907	304
2022	5,907	113
2023	5,907	111
2024	5,907	27
Thereafter	23,625	392
	\$ 53,160	\$ 1,438

Intangible assets not subject to amortization include certain trade names and intellectual property, research and development that resulted from the Affiliation with TGen and totaled \$8,600,000 as of September 30, 2019 and 2018. Under ASU Topic 350, *Intangibles – Goodwill and Other (ASU Topic 350)*, these intangibles are subject to an annual impairment assessment, or more frequently if significant indicators of impairment exist. A qualitative review for impairment of intangible assets was performed on the annual measurement date of July 1, and there was no indication of an impairment in value as of September 30, 2019.

Deferred Revenue

City of Hope defers recognition of revenue received in advance of certain performance objectives, including fundraising events, research grants, and other agreements prior to such funds being earned. The following is a summary of deferred revenue as of September 30 (amounts in thousands):

	2019	2018
Fundraising events and other efforts	\$ 3,493	\$ 3,896
Donor restricted conditional contributions	1,095	1,481
Royalty revenue	–	558
Grants revenue	24,193	22,469
Total deferred revenue	\$ 28,781	\$ 28,404

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Net Assets Without Donor Restrictions

A rollforward of controlling interest and noncontrolling interest net assets without donor restrictions for the years ended September 30, 2019 and 2018, is as follows (amounts in thousands):

	Controlling Interests	Noncontrolling Interest	Total
Beginning balance at September 30, 2017	\$ 2,788,493	\$ –	\$ 2,788,493
Excess of revenues, gains, and other support over expenses	335,768	189	335,957
Contributed capital	–	34,911	34,911
Other changes in net assets	2,945	–	2,945
Balance at September 30, 2018	3,127,206	35,100	3,162,306
Excess of revenues, gains, and other support over expenses	149,429	(765)	148,664
Other changes in net assets	87,144	–	87,144
Distributions to noncontrolling interest	–	(2,037)	(2,037)
Balance September 30, 2019	\$ 3,363,779	\$ 32,298	\$ 3,396,077

Contributions

All contributions are considered without donor restrictions, unless specifically restricted by the donor. Amounts received that are designated for future periods or are restricted by the donor for specific purposes are reported as contributions with donor restrictions.

Net assets with donor restrictions consist of assets that are subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity in a true endowment. All other contributions without donor restrictions are considered net assets without donor restrictions.

Restricted monetary gifts are held in net assets with donor restrictions until the designation is met. When the donor designation is met, a stipulated time restriction ends, or a purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

restrictions and reported on the consolidated statements of activities as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same fiscal period as the contributions are received are also reflected as net assets released from restrictions on the accompanying consolidated statements of activities.

City of Hope is the beneficiary under various wills and trust agreements of which the total realizable amount is not readily determinable at the date of gift. In the case of wills, such amounts are recognized as contributions when the will is declared valid by a probate court and the proceeds are measurable. For the years ended September 30, 2019 and 2018, valid will and trust agreement amounts that became measurable totaled \$24,314,000 and \$39,173,000, respectively, and are included in contributions on the accompanying consolidated statements of activities.

City of Hope reports unconditional promises to give as contributions with donor restrictions. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on these amounts are computed using risk-free interest rates approximating the U.S. Treasury Note rate when the unconditional promise is made. The rates used in 2019 and 2018 were between 1.2% and 2.82%.

Net unconditional promises to give in the accompanying consolidated statements of financial position consist of the following as of September 30 (amounts in thousands):

	<u>2019</u>	<u>2018</u>
Unconditional promises to give	\$ 80,268	\$ 90,029
Less:		
Discounts	(4,361)	(4,885)
Allowance for uncollectible promises to give	(5,871)	(5,827)
Total unconditional promises to give, net	<u>70,036</u>	<u>79,317</u>
Less current portion	(24,449)	(18,576)
	<u>\$ 45,587</u>	<u>\$ 60,741</u>

The allowance for uncollectible promises to give has been determined based on historical collection experience. Changes in the allowance for uncollectible promises to give and the amortization of pledge discounts is included in contribution revenue to the extent previously recognized when collected. Subsequent changes in the collectability of promises to give are included in other expense on the accompanying consolidated statements of activities.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

At September 30, 2019, future cash flows anticipated from unconditional promises to give are as follows (amounts in thousands):

2020	\$	24,449
2021		13,455
2022		10,872
2023		7,528
2024		5,371
Thereafter		18,593
		<u>80,268</u>
Discounts		(4,361)
Allowance for uncollectible promises to give		<u>(5,871)</u>
	\$	<u>70,036</u>

City of Hope reports conditional promises to give as contribution revenue when the conditions stipulated by the donor are met, at which time the conditional promise becomes unconditional. Prior to September 30, 2019, City of Hope received a conditional promise in the amount of \$35,000,000. There are specific project goals and milestones that must be met to receive the payments under the agreement. City of Hope recorded \$4,167,000 and \$5,000,000 for the years ending September 30, 2019 and 2018, respectively, which has been recorded in contribution revenue, in recognition of attaining project goals and milestones. The remaining \$8,333,000 of this conditional promise as of September 30, 2019, has not been recognized in contribution revenue due to certain project goals and milestones still subject to completion by City of Hope. Cash payments in advance of meeting specific project goals and milestones totaled \$1,095,000 and \$1,481,000 as of September 30, 2019 and 2018, respectively, which is included in deferred revenue on the accompanying consolidated statements of financial position.

Split-Interest Agreements

City of Hope receives contributions from various types of split-interest agreements, including charitable gift annuities, charitable remainder annuity trusts, and charitable remainder unitrusts. City of Hope may be named as a trustee or a co-trustee, or a financial institution may be named as the trustee.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Under a charitable gift annuity arrangement, City of Hope recognizes the agreement in the period in which the contract is executed. The assets from the donor are recognized at fair value, and the liabilities designated by the donor to various beneficiaries are recognized at the present value of the estimated future payments to be distributed by City of Hope to such beneficiaries. The amount of the contribution revenue with donor restrictions is the difference between these assets and liabilities.

Some states have laws that mandate certain requirements regarding gift annuity reserves. These laws can be based on where the nonprofit entity is located or where the gift annuity donor resides. As of September 30, 2019, City of Hope has state-mandated reserves above the actuarial annuity reserves in the amount of \$290,000. Additionally, City of Hope has voluntary reserves in the amount of \$5,876,000 that are to protect the reserve fund against unexpected market fluctuations and actuarial changes. These voluntary reserves are included in investments and net assets without donor restrictions on the accompanying consolidated statements of financial position.

Under charitable trust arrangements in which City of Hope is not the trustee or is a co-trustee, City of Hope recognizes, in the period the agreement is executed, donor restricted long-term contribution receivables and contribution revenues at the present value of the estimated future benefits to be received when the trust assets are expected to be distributed. Trust distributions are recorded as a reduction in receivables, while adjustments to the receivables to reflect amortization of the discount and changes in actuarial assumptions during the term of the trust are recorded as donor restricted contributions on the accompanying consolidated statements of activities. Receivables totaling \$15,716,000 as of September 30, 2019, are to be collected over the next 28.6 years and have an average remaining life of 15.1 years.

In-Kind Contributions

In-kind contributions are reflected at their estimated fair market value on the date of the donation. City of Hope reports gifts of land, buildings, equipment, and other nonmonetary contributions as contributions without donor restrictions, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how and how long the donated assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as contributions with donor restrictions. Absent explicit donor stipulations about how long those long-lived assets must be maintained, City of Hope reports expirations of donor restrictions as net assets released from restrictions when the donated or acquired long-lived assets are placed in service.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

There are no amounts recorded for contributed services on the accompanying consolidated statements of activities.

Research Grants, Contracts, and Clinical Trials Revenue

Research grants, contracts, and clinical trials revenue includes federal, state, and local jurisdiction awards and other exchange transactions. An exchange transaction is one in which there is reciprocal benefit where each party receives approximate commensurate value. Research grants, contracts, and clinical trials revenue is recognized in the period it is earned based on when the applicable project expenses have been incurred and project milestones are achieved. Payments received in advance of related project expenses are recorded in deferred revenue on the accompanying consolidated statements of financial position.

Royalty and Licensing Revenue

City of Hope receives royalties from Genentech based on sales of its own drugs, as well as from royalties and other amounts paid by its licensees. During 2019 and 2018, City of Hope recognized royalty and licensing revenue totaling \$384,514,000 and \$500,370,000, respectively, primarily from sales of drugs by Genentech and other licensees of monoclonal antibodies, including Rituxan, Herceptin, Avastin, Humira, and others using technology developed at the Institute and covered by the Cabilly patents. The Cabilly patents, as further defined in Note 12, expired during the first quarter of fiscal year 2019, with some royalty revenue anticipated to continue into fiscal year 2020.

Previously under Accounting Standard Codification 605, *Revenue Recognition* (ASC 605), revenue related to royalties was reported on a lag because it was not fixed and determinable in the period of reporting; as such City of Hope recognized revenue from royalties in the period the related payment for royalties was received, generally one quarter in arrears from the period in which the underlying sales occurred.

Under ASU 2014-09, which was effective for City of Hope on October 1, 2018, an entity is required to recognize estimated royalty revenue in the same period the sales occur. City of Hope adopted ASU 2014-09 using the modified retrospective approach, which required the recognition of the first quarter of fiscal year 2019 cash basis royalty revenue to be recognized as a component of the cumulative changes in net assets along with the related royalty sharing expenses from adoption of the new accounting standard. The cumulative adjustment of \$87,144,000 increased City of Hope's net assets without donor restrictions and in accordance with the modified

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

retrospective approach of adoption, is not included in the royalty and licensing revenues for the year ended September 30, 2019. As of and for the year ended September 30, 2019, City of Hope's royalty revenue and royalty sharing expense is reported on an accrual basis to match the period of related sales that generate the royalties.

The table below summarizes the impact of the implementation of ASU 2014-09 to the consolidated statement of activities and the consolidated statement of financial position as of and for the year ended September 30, 2019:

	As Reported	Balance Before Adoption of ASU 2014-09	Effect of Change Increase (Decrease)
Consolidated Statement of Activities			
Revenues, gains and other support:			
Royalty and licensing revenue	\$ 384,514	\$ 451,732	\$ (67,218)
Expenses:			
Royalty sharing	\$ 118,445	\$ 139,169	<u>\$ (20,724)</u>
Net impact to excess of revenues, gains, and other support over expenses			<u><u>\$ (46,494)</u></u>

	As Reported	Balance Before Adoption of ASU 2014-09	Effect of Change Increase (Decrease)
Consolidated Statement of Financial Position			
Current assets:			
Grants and other receivables	\$ 158,176	\$ 99,403	\$ 58,773
Current liabilities:			
Accounts payable and other accrued liabilities	\$ 198,081	\$ 179,959	<u>\$ 18,122</u>
Net assets without donor restrictions:			
Controlling interest	\$ 3,363,779	\$ 3,323,128	<u><u>\$ 40,651</u></u>

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Royalty revenues are expected to decline over the coming year due to the expiration of the Cabilly patents in December 2018, however the ultimate date of when the royalties from the Cabilly patents will completely cease cannot be determined at this time.

City of Hope has entered into various licensing agreements whereby equity interests in the licensee is received as compensation. The stock and membership units related to these agreements are recorded at fair value.

Workers' Compensation Program

City of Hope, the Center, the Foundation, and the Institute have elected to self-insure their workers' compensation liability. Reinsurance has been obtained for this program to cover claims that exceed \$250,000 between 1991 and 2002, \$500,000 in 2003, and \$1,000,000 per individual claim beginning in 2004. An estimated liability of \$23,195,000 and \$21,164,000 has been recorded as of September 30, 2019 and 2018, respectively. The estimated current portion of the liability, totaling \$4,234,000 and \$3,889,000 as of September 30, 2019 and 2018, respectively, is included in accrued salaries, wages, and employee benefits on the consolidated statements of financial position and the estimated long-term portion of the liability, totaling \$18,961,000 and \$17,275,000 as of September 30, 2019 and 2018, respectively, is included in other long-term liabilities on the consolidated statements of financial position. Accruals for uninsured claims and claims incurred but not reported are estimated by an actuary based on prior claims experience. The estimated liability was recorded using a 1.65% and 2.85% discount factor as of September 30, 2019 and 2018, respectively.

Insurance recoveries related to workers' compensation totaling \$4,237,000 and \$3,679,000 as of September 30, 2019 and 2018, respectively, have been reflected on the accompanying consolidated statements of financial position in other assets.

Workers' compensation expense charged to operations totaled \$6,763,000 and \$7,022,000 in 2019 and 2018, respectively.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Professional Liability Insurance

The Center, the Foundation, and the Institute maintain professional liability insurance under a claims-made program, which provides coverage for claims arising out of incidents that have occurred from November 1, 1997 to September 30, 2015, with limits up to \$50,000,000 and a deductible of \$100,000 through June 30, 2014, and \$250,000 between July 1, 2014 and September 30, 2019. Accruals for uninsured claims and claims incurred but not reported are estimated by an actuary based on prior claims experience. Such accruals were recorded using a 2.85% discount factor as of September 30, 2019 and 2018. An estimated liability of \$1,595,000 as of September 30, 2019 and 2018, is included in other current and long-term liabilities on the consolidated statements of financial position.

The Center, the Foundation, and the Institute recorded insurance recoveries related to professional liability totaling \$443,000, as of September 30, 2019 and 2018, which have been reflected on the accompanying consolidated statements of financial position in other assets.

SCRO maintains health care professional liability insurance that provides coverage for claims arising that occurred from March 31, 2018, through September 30, 2019, with limits up to \$10,000,000 per occurrence and a deductible of \$10,000 for each claim.

The professional liability insurance expense charged to operations amounted to \$1,798,000 and \$1,242,000 in 2019 and 2018, respectively.

Retirement Plans

City of Hope, the Center, the Foundation, and the Institute participate in the City of Hope Defined Contribution Plan (the Plan). The Plan was established in 1989 to provide benefits to eligible employees as defined in the plan document and covers substantially all employees. Contributions range between 2% and 10%, depending on years of service and salary, and are calculated on an employee's biweekly base salary up to and above the annual Social Security Taxable wage base, not to exceed the maximum covered compensation of \$280,000 in 2019. Employees are eligible to participate in the Plan upon the completion of one year of service in which they have worked at least 1,000 hours. They may direct these contributions into various funds offered through the Plan.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

The Center and the Institute also participate in the City of Hope Research Staff Organization (RSO) Tax Deferred Annuity Plan (the RSO TDA Plan), which was established in 1983 to provide benefits to eligible members of the City of Hope RSO as defined in the plan document. Employer contributions of 15% of each participant's biweekly eligible salary are made up to a defined annual maximum base salary of \$280,000 in 2019. The participants have the option to direct these contributions into various funds offered through the RSO TDA Plan.

TGen has a defined contribution Profit Sharing Plan (the PSP Plan) that covers all employees who are 21 years of age and who have completed one month of service. Under the terms of the PSP Plan, employees may make voluntary contributions, subject to Internal Revenue Service limitations. TGen matches employee contributions up to 4% of the employee's annual compensation, subject to certain eligibility criteria as stated in the plan document.

SCRO has a Defined Contribution Plan (the DC Plan) that covers all employees who are 21 years of age and who have completed six months of service. Under the terms of the DC Plan, employees may make voluntary contributions subject to Internal Revenue Service limitations. SCRO matches 100% of employee contributions up to 3% of the employee's eligible compensation and then matches 50% of the next 2% of the employee's eligible compensation subject to certain eligibility criteria as stated in the plan document.

Contribution expense for the plans defined above totaled \$27,023,000 and \$24,678,000 in 2019 and 2018, respectively.

Derivative and Hedging Instruments

City of Hope recognizes all derivatives at fair value on the consolidated statements of financial position. At September 30, 2019 and 2018, derivative instruments consisted of two interest rate swap agreements with a total notional amount of \$65,000,000 (see Note 5). Interest rate swap agreements are used to manage interest rate risk. The derivatives are not designated as effective hedges and are adjusted to fair value on the consolidated statements of activities, above the performance indicator.

City of Hope

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Income Taxes

City of Hope is exempt from federal income tax under Section 501(c)(3) of the U.S. Internal Revenue Code. City of Hope, the Center, the Foundation, and the Institute are exempt from California state franchise and income tax under Section 23701d of the California Revenue and Taxation Code.

TGen is exempt from Arizona corporate income tax under Section 43-1201(A) of the Arizona Revised Statutes (A.R.S.).

ACOH and the 100% wholly owned entities of TGen are single-member, limited liability companies and are considered disregarded entities for tax purposes.

SCRO is treated as a partnership for federal and state income tax purposes where all taxable income is allocated to the partners in accordance with the respective partnership agreement; accordingly, federal and state taxes on income are the responsibility of the joint partners individually.

FASB ASC 740, *Income Taxes*, clarifies the accounting for income taxes by prescribing a minimum recognition threshold that a tax position is required to meet before being recognized in the financial statements. ASC 740 also provides guidance on de-recognition, measurement, classification, interest and penalties, disclosure, and transition. The guidance contained in ASC 740 is applicable to pass-through entities and tax-exempt organizations. City of Hope has no significant uncertain tax positions or tax liability for tax benefits, interest, or penalties accrued at September 30, 2019 and 2018.

3. Fair Value of Financial Instruments

The consolidated statements of financial position include the following financial instruments: cash and cash equivalents, patient accounts receivable, grants and other receivables, short- and long-term investments, prepaid and other, accounts payable and other accrued liabilities, estimated amounts due to/from third-party payors, interest rate swaps, annuity and split-interest agreement obligations, and long-term debt. City of Hope considers the carrying amounts of current assets and liabilities (except for investment securities, which are carried at fair value, as described in Note 2) on the consolidated statements of financial position to approximate the fair value of these financial instruments, because of the relatively short period of time between origination of the instruments and their expected realization. The carrying amount of tax-exempt and taxable long-term financing

City of Hope

Notes to Consolidated Financial Statements (continued)

3. Fair Value of Financial Instruments (continued)

for City of Hope was \$1,260,000,000 and \$932,301,000, with a total fair value of \$1,529,000,000 and \$997,970,000 as of September 30, 2019 and 2018, respectively (Level 2 in the fair value hierarchy).

As defined by ASC 820, *Fair Value Measurement*, fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. To increase consistency and comparability in fair value measurements, a fair value hierarchy was established that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

- Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.
- Level 2: Observable prices that are based on inputs not quoted on active markets but can be corroborated by market data.
- Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

Assets and liabilities measured at fair value are based on one or more of three valuation techniques as identified in the tables below. Where more than one technique is noted, individual assets or liabilities were valued using one or more of the noted techniques. The valuation techniques are as follows:

- (a) *Market approach*. Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.
- (b) *Cost approach*. Amount that would be required to replace the service capacity of an asset (replacement cost).
- (c) *Income approach*. Techniques to convert future amounts to a single present amount based on market expectations (including present value techniques, option-pricing, and excess earnings models).

City of Hope

Notes to Consolidated Financial Statements (continued)

3. Fair Value of Financial Instruments (continued)

In determining fair value, City of Hope utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, as well as considers counterparty credit risk, in its assessment of fair value. The fair value of annuity and split-interest obligations has been determined using present value techniques based on mortality tables and discount rates that are consistent with Internal Revenue Service published rates and the American Council on Gift Annuities.

City of Hope uses interest rate swaps to manage interest rate risk associated with floating-rate debt. The valuation of these instruments is determined using widely accepted valuation techniques, including discounted cash flow analysis on the expected cash flows of each derivative. This analysis reflects the contractual terms of the derivatives, including the period of maturity, and uses observable market-based inputs, including interest rate curves and implied volatilities. The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments and the discounted expected variable cash receipts. The variable cash receipts are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves. City of Hope incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements.

City of Hope

Notes to Consolidated Financial Statements (continued)

3. Fair Value of Financial Instruments (continued)

City of Hope's assets and liabilities, measured at fair value on a recurring basis as of September 30 aggregated by the level in the fair value hierarchy, are included in cash equivalents, investments, other long-term assets, annuity and split-interest agreement obligations, and interest rate swaps on the consolidated statements of financial position and are as follows (amounts in thousands):

2019	Investments at Fair Value				Investments at Net		Valuation Technique (a,b,c)
	Level 1	Level 2	Level 3	Fair Value	Asset Value	Total	
Investments							
U.S. government and agency obligations	\$ -	\$ 157,835	\$ -	\$ 157,835	\$ -	\$ 157,835	a,b
Corporate obligations	-	410,441	-	410,441	-	410,441	a,b
Asset-backed obligations	-	206,939	-	206,939	-	206,939	a,b
Mortgage-backed obligations	-	175,146	-	175,146	-	175,146	a,b
Marketable securities	864,536	-	-	864,536	-	864,536	a
Public real assets	146,707	-	-	146,707	-	146,707	a
Municipal obligations	-	1,710	-	1,710	-	1,710	a
Preferred stock	-	-	612	612	-	612	c
Hedge funds	-	-	-	-	254,788	254,788	
Equity commingled funds	-	-	-	-	869,639	869,639	
Private equity funds	-	-	-	-	266,797	266,797	
Private real assets	-	-	-	-	169,029	169,029	
Certificates of deposit	-	363,000	-	363,000	-	363,000	a,b
Cash equivalents	211,045	-	-	211,045	-	211,045	a
Total investments	\$ 1,222,288	\$ 1,315,071	\$ 612	\$ 2,537,971	\$ 1,560,253	\$ 4,098,224	
Other long-term assets							
Marketable securities	\$ 29,124	\$ -	\$ -	\$ 29,124	\$ -	\$ 29,124	a
Cash equivalents	\$ 472	\$ -	\$ -	\$ 472	\$ -	\$ 472	a
Total investments and other long-term assets	\$ 1,251,884	\$ 1,315,071	\$ 612	\$ 2,567,567	\$ 1,560,253	\$ 4,127,820	
Liabilities at fair value							
Annuity and split-interest obligations			Level 1	Level 2	Level 3	Total	
			\$ -	\$ -	\$ 19,068	\$ 19,068	c
Interest rate swaps			-	19,489	-	19,489	a,b
Total liabilities			\$ -	\$ 19,489	\$ 19,068	\$ 38,557	

City of Hope

Notes to Consolidated Financial Statements (continued)

3. Fair Value of Financial Instruments (continued)

2018	Investments at Fair Value				Investments at Net		Valuation Technique (a,b,c)
	Level 1	Level 2	Level 3	Fair Value	Asset Value	Total	
Investments							
U.S. government and agency obligations	\$ -	\$ 80,996	\$ -	\$ 80,996	\$ -	\$ 80,996	a,b
Corporate obligations	-	264,026	-	264,026	-	264,026	a,b
Asset-backed obligations	-	150,633	-	150,633	-	150,633	a,b
Mortgage-backed obligations	-	125,779	-	125,779	-	125,779	a,b
Marketable securities	740,032	-	-	740,032	-	740,032	a
Public real assets	231,812	-	-	231,812	-	231,812	a
Municipal obligations	-	1,766	-	1,766	-	1,766	a
Preferred stock	-	-	612	612	-	612	c
Hedge funds	-	-	-	-	297,046	297,046	
Equity commingled funds	-	-	-	-	891,365	891,365	
Private equity funds	-	-	-	-	202,391	202,391	
Private real assets	-	-	-	-	174,586	174,586	
Cash equivalents	256,917	-	-	256,917	-	256,917	a
Total investments	\$ 1,228,761	\$ 623,200	\$ 612	\$ 1,852,573	\$ 1,565,388	\$ 3,417,961	
Other long-term assets							
Marketable securities	\$ 25,855	\$ -	\$ -	\$ 25,855	\$ -	\$ 25,855	a
Cash equivalents	\$ 454	\$ -	\$ -	\$ 454	\$ -	\$ 454	a
Total investments and other long-term assets	\$ 1,255,070	\$ 623,200	\$ 612	\$ 1,878,882	\$ 1,565,388	\$ 3,444,270	
Liabilities at fair value							
Annuity and split-interest obligations							
			Level 1	Level 2	Level 3	Total	
Interest rate swaps			\$ -	\$ -	\$ 20,464	\$ 20,464	c
Total liabilities			\$ -	\$ 6,549	\$ -	\$ 6,549	a,b
			\$ -	\$ 6,549	\$ 20,464	\$ 27,013	

Other long-term assets consist of 457(b) Plans that are funded by plan participants of City of Hope.

City of Hope

Notes to Consolidated Financial Statements (continued)

3. Fair Value of Financial Instruments (continued)

The table below sets forth a summary of changes in fair value of the Level 3 assets and liabilities for the years ended September 30, 2019 and 2018 (amounts in thousands):

	<u>Assets</u>	<u>Liabilities</u>
Beginning balance at September 30, 2017	\$ 62	\$ 18,580
Additions	550	3,739
Investment activity, adjustments, and maturities	—	605
Distributions	—	(1,355)
Change in fair value	—	(1,105)
Beginning balance at September 30, 2018	612	20,464
Additions	—	1,377
Investment activity, adjustments, and maturities	—	750
Distributions	—	(1,307)
Change in fair value	—	(2,216)
Ending balance at September 30, 2019	<u>\$ 612</u>	<u>\$ 19,068</u>

The following reconciles fair value amounts to the consolidated statements of financial position as of September 30 (amounts in thousands):

	<u>2019</u>	<u>2018</u>
Cash and cash equivalents	\$ 238,535	\$ 377,571
Investments, current	1,927,425	1,526,106
Self-insurance trust funds	3,418	3,765
Investments held for long-term purposes	237,564	302,822
Board-designated assets	895,110	884,127
Bond trust funds	380,242	—
Donor-restricted investments	557,136	518,251
	<u>4,239,430</u>	<u>3,612,642</u>
Less investment at net asset value	(1,560,253)	(1,565,388)
Less amounts held in operating cash	(141,206)	(194,681)
Plus amounts in other long-term assets	29,596	26,309
Investments at fair value	<u>\$ 2,567,567</u>	<u>\$ 1,878,882</u>

City of Hope

Notes to Consolidated Financial Statements (continued)

4. Liquidity and Availability

City of Hope's financial assets available for general expenditure within one year of September 30, 2019, include the following (amounts in thousands):

Cash and cash equivalents	\$ 238,535
Investments	1,927,425
Patient accounts receivable	235,989
Grants and other receivables	158,176
Board-designated assets	895,110
	<u>\$ 3,455,235</u>

As part of City of Hope's liquidity management plan, cash in excess of any daily requirement is invested in long-term investments. The long-term investment portfolio contains liquid investments that can be drawn upon if necessary to meet liquidity needs.

Board-designated assets include funds set aside to function as institutionally designated endowments as established by the Board of Directors for future research, program services, and capital expenditures for City of Hope. Board-designated assets can be used for liquidity purposes related to research, program services, and capital expenditures upon the approval of the Board of Directors.

City of Hope invests in alternative investments to increase the investment portfolio's diversification. The nature of alternative investments generally restricts the liquidity and availability of these investments to be available for the general expenditures of City of Hope within one year of the consolidated statements of financial position. These investments and those assets limited as to use included in self-insurance trust funds, investments held for long-term purposes, bond trust funds, and donor restricted funds have not been included in the amounts above.

Line of Credit

City of Hope maintains a consolidated unsecured revolving bank line of credit in the amount of \$50,000,000, which expires on June 30, 2020, and is available to meet unanticipated liquidity needs. Interest is charged at the London Interbank Offered Rate (LIBOR) plus 0.75%. There was no outstanding balance on the line of credit as of September 30, 2019 and 2018.

Additionally, City of Hope maintains standby letters of credit as required by various agencies to which City of Hope is a party.

City of Hope

Notes to Consolidated Financial Statements (continued)

5. Long-Term Debt

The following is a summary of City of Hope's long-term debt as of September 30 (amounts in thousands):

	2019	2018
City of Hope, 3.75% to 5.00% fixed rate Tax-Exempt Revenue Bonds Series 2012A, originally \$234,635, issued through the California Health Facilities Financing Authority, with varying maturities annually through November 15, 2039. Interest payable semiannually on May 15 and November 15 (Series 2012A Revenue Bonds).	\$ 207,425	\$ 213,400
City of Hope, 5.623% fixed rate Taxable Direct Obligation Notes, originally \$350,000. Interest payable semiannually on May 15 and November 15, principal payment due in full on November 15, 2043 (Series 2013 Notes).	350,000	350,000
City of Hope, Tax-Exempt Variable Rate Revenue Notes Series 2017A, originally \$32,680, issued through the California Health Facilities Financing Authority. Interest payable monthly, principal payments annually beginning on November 15, 2039, through November 15, 2042 (Series 2017A Revenue Notes).	32,680	32,680
City of Hope, Tax-Exempt Variable Rate Revenue Notes Series 2017B, originally \$32,680, issued through the California Health Facilities Financing Authority. Interest payable monthly, principal payments annually beginning on November 15, 2039, through November 15, 2042 (Series 2017B Revenue Notes).	32,680	32,680
City of Hope, 4.378% fixed rate Taxable Direct Obligation Notes, originally \$300,000. Interest payable semiannually on February 15 and August 15, principal payment due in full on August 15, 2048 (Series 2018 Notes).	300,000	300,000

City of Hope

Notes to Consolidated Financial Statements (continued)

5. Long-Term Debt (continued)

	<u>2019</u>	<u>2018</u>
City of Hope, 4%–5% fixed rate Tax-Exempt Revenue Bonds Series 2019, originally \$334,905, issued through the California Health Facilities Financing Authority. Interest payable semiannually on May 15 and November 15, principal payments annually beginning on November 15, 2024, through November 15, 2049 (Series 2019 Revenue Bonds).	\$ 334,905	\$ –
TGen, 3.27%-4.22% fixed rate notes. Principal and interest payable monthly through April 2020 (TGen Notes).	934	2,241
TGen, 2% fixed rate notes. Principal and interest payable annually through 2022 (TGen Notes).	1,000	1,300
Capital lease obligations:		
Equipment	4,903	2,270
Facilities	66,320	70,832
	<u>1,330,847</u>	<u>1,005,403</u>
Less current maturities of long-term debt and capital lease obligations	(13,492)	(13,051)
Less unamortized bond issue costs	(4,072)	(2,934)
Less unamortized discount	(6,911)	(5,313)
Plus unamortized premium	67,285	19,705
	<u>\$ 1,373,657</u>	<u>\$ 1,003,810</u>

Long-term debt maturities and capital lease obligations as of September 30, 2019, and payments for the subsequent years are as follows (amounts in thousands):

2020	\$ 13,492
2021	13,269
2022	13,651
2023	14,026
2024	14,222
Thereafter	1,262,187
	<u>\$ 1,330,847</u>

City of Hope

Notes to Consolidated Financial Statements (continued)

5. Long-Term Debt (continued)

Series 2012 Revenue Bonds (Tax-Exempt) – In November 2012, City of Hope, as representative of the Obligated Group, issued \$234,635,000 of Tax-Exempt Series 2012A fixed rate Revenue Bonds, \$32,500,000 of Tax-Exempt Series 2012B Variable Rate Revenue Bonds, and \$32,500,000 of Tax-Exempt Series 2012C Variable Rate Revenue Bonds through the California Health Facilities Financing Authority. The Series 2012A Revenue Bonds were issued at a premium totaling \$29,887,000. The Series 2012 Revenue Bonds are secured by a gross receivables pledge.

Series 2013 Notes (Taxable) – In July 2013, City of Hope, as representative of the Obligated Group, issued \$350,000,000 of Series 2013 fixed rate Direct Obligation Notes. The proceeds from the Series 2013 Notes are used for the Obligated Group's capital needs in furtherance of the implementation of the Obligated Group's strategic plan. The Series 2013 Notes are secured by a gross receivables pledge.

Series 2017 Revenue Notes (Tax-Exempt) – In February 2017, City of Hope, as representative of the Obligated Group, refunded the Series 2012B Variable Rate Revenue Bonds in the amount of \$32,500,000 and Series 2012C Variable Rate Revenue Bonds in the amount of \$32,500,000 with two new issues through the California Health Facilities Financing Authority, Variable Rate Revenue Notes Series 2017A Variable Rate Revenue Notes in the amount of \$32,680,000 and Series 2017B Variable Rate Revenue Notes in the amount of \$32,680,000. The Series 2017 Revenue Notes were directly purchased by a commercial bank and have the same maturity and approximate principal amortization as the refunded Series 2012B and Series 2012C Revenue Bonds and bear interest based on 70% of one-month of LIBOR plus a spread. The Series 2017 Revenue Notes are secured by a gross receivables pledge.

Series 2018 Notes (Taxable) – In May 2018, City of Hope as representative of the Obligated Group, issued \$300,000,000 of Series 2018 Notes. The proceeds from the Series 2018 Notes are used for the Obligated Group's capital needs in furtherance of the implementation of the Obligated Group's strategic plan, including geographic expansion, addressing patient capacity, informatics, developing precision medicine, and funding research to support the development of innovative treatments. The Series 2018 Notes are secured by a gross receivables pledge.

Series 2019 Revenue Bonds (Tax-Exempt) – In July 2019, City of Hope, as representative of the Obligated Group issued \$334,905,000 of Series 2019 Revenue Bonds through the California Health Facilities Financing Authority. The proceeds from the Series 2019 Revenue Bonds are being used for the construction and equipping of an outpatient clinic, a parking structure to support the outpatient clinic and balance parking requirements across the campus, and the construction of

City of Hope

Notes to Consolidated Financial Statements (continued)

5. Long-Term Debt (continued)

a building that will provide accommodations for patients, family members, and guests. The Series 2019 Revenue Bonds were issued at a premium totaling \$49,624,000 and are secured by a gross receivables pledge.

TGen Notes – TGen Notes are comprised of notes payable with a bank for laboratory equipment and a promissory note for the purchase of the outstanding 50% interest in a subsidiary company. The TGen Notes for laboratory equipment are secured by the equipment financed.

Capital Lease Obligations – City of Hope has entered into various capital lease agreements for equipment and program and administrative facilities. Assets are capitalized using interest rates commensurate with City of Hope's incremental borrowing rate.

On October 3, 2017, TGen entered into a long-term capital lease agreement to purchase the building where its primary operations are conducted in Phoenix, Arizona, through a subsidiary limited liability company (the TGen LLC). The aggregate lease payments that the TGen LLC will be obligated to make under the agreement are approximately \$67,500,000 beginning October 2017 through April 2037. Additionally, under the lease agreement, the TGen LLC will receive future sublease income from tenants in the amount of \$14,896,000 through December 2034.

To secure its obligation under the long-term capital lease agreement, the TGen LLC purchased an irrevocable standby letter of credit in the amount of up to \$25,000,000 for the benefit of the lessor. The standby letter of credit is guaranteed by City of Hope and it will renew annually based on a pre-agreed amortization schedule, unless terminated with a 60-day notice prior to the annual anniversary date by the lender. Unless it has expired earlier, this letter of credit shall finally expire on October 1, 2035.

Interest Rate Swap Transactions – In November 2012, the Obligated Group entered into two interest rate swap contracts to synthetically convert the Series 2012B and Series 2012C Revenue Bonds from a variable rate to a fixed rate of 2.715% and 2.720%, respectively. The Obligated Group receives a floating rate equal to 70% of the USD-LIBOR-BBA for both Series 2012B and Series 2012C Revenue Bonds. The swaps were not designated as cash flow hedges, so the changes in fair value are recorded within interest expense on the accompanying consolidated statements of activities, totaling an increase in fair value of the interest rate swap liability of \$12,940,000 for the year ended September 30, 2019, and a decrease in fair value of the interest rate swap liability of \$3,718,000 for the year ended September 30, 2018. The effect of counterparty payments and receipts on interest expense was an expense increase of \$670,000 and \$976,000 for the years ended September 30, 2019 and 2018, respectively.

City of Hope

Notes to Consolidated Financial Statements (continued)

5. Long-Term Debt (continued)

Financial Covenants – Under the Series 2012 Revenue Bonds, the Series 2013 Notes, the Series 2017 Revenue Notes, the Series 2018 Notes, and the Series 2019 Revenue Bonds, the Obligated Group was in compliance with its financial covenants as of September 30, 2019.

TGen was in compliance with its financial covenants related to its TGen Notes and its capital lease obligations as of September 30, 2019.

6. Formation of Access City of Hope, LLC

On August 20, 2019, the Board of Directors of City of Hope authorized and approved the formation of a new subsidiary to focus on City of Hope's employer and payer services business. Access City of Hope LLC (ACOH) was formed on August 21, 2019, as a Delaware single-member, limited liability company, with City of Hope as its sole member. ACOH, located in Irwindale, California, will provide or arrange for the provision to employers and payers and other parties that provide services to the employer market throughout the United States, of certain oncology-related consultative, advisory, and support services designed to address the specific cancer needs of patients, improve care outcomes and drive value.

Subsequently, on October 27, 2019, City of Hope and the Foundation entered into a Contribution and Assignment and Assumption Agreement (Contribution Agreement) with ACOH pursuant to which City of Hope and the Foundation contributed certain assets to ACOH necessary for the operation of the employer and payer services business, including an initial cash contribution by City of Hope in the amount of \$35,000,000 and the assignment of existing customer contracts and consulting agreements related to the employer and payer services business to ACOH. Concurrently with the Contribution Agreement, City of Hope, the Foundation, and City of Hope National Medical Center also entered into a Shared Services Agreement (SSA) with ACOH to, among other matters, provide ACOH with certain shared services support, including with respect to operational, human resources, marketing and financial services in exchange for the service fees set forth in the SSA.

7. Acquisitions and Affiliations

City of Hope accounts for acquisitions and affiliations in accordance with ASC 958-805, *Not-for-Profit Entities Business Combinations*, in determining the appropriate accounting treatment for acquisitions and affiliations. Under ASC 958-805, business combinations are classified as either a merger or an acquisition, which results in differing accounting treatment.

City of Hope

Notes to Consolidated Financial Statements (continued)

7. Acquisitions and Affiliations (continued)

Effective March 30, 2018, the Foundation closed a transaction with Vantage Oncology Treatment Centers, LLC and certain of its affiliates (Vantage) and Valley Radiotherapy Associates Medical Group, Inc. (VRA) related to nine freestanding radiation therapy centers in Southern California that were managed by Vantage and operated by VRA prior to the closing. The Foundation and Vantage formed a new joint venture company, Southern California Radiation Oncology, LLC (SCRO) (owned 50.1% by the Foundation and 49.9% by Vantage), to manage and provide services to the nine centers. The Foundation evaluated the transaction under ASU 958-810, *Not-for-Profit Entities – Consolidation*, and determined the Foundation has significant and substantive participating rights in the operations of SCRO. The rights of Vantage are substantively protective rights. SCRO contracts with various Vantage affiliates to provide most of these services. As the provider and operator of the centers, the Foundation has retained responsibility for providing certain categories of services at the centers. As part of the transaction, approximately 27 VRA physicians who provide services at the centers and at four hospital-based radiation oncology programs in Los Angeles and Orange counties joined the COHMG. Vantage contributed tangible and intangible assets, including facility leases and equipment with a fair value of \$55,603,000 and initial working capital of \$2,802,000. The Foundation contributed a previous investment in a 40% holding with a fair value of \$8,745,000 and initial working capital of \$2,813,000. The Foundation also contributed \$23,494,000 in cash consideration to obtain a controlling interest in the joint venture. At the close of the transaction, the cash consideration was immediately distributed by SCRO to Vantage.

The tangible and intangible assets acquired as part of the transaction to form the joint venture were recorded as follows (amounts in thousands):

Cash and cash equivalents (initial working capital)	\$	5,615
Prepaid and other assets		388
Property and equipment		3,703
Trade name		430
Favorable leasehold interests		690
Goodwill		59,067
Other long-term assets		70
Total identifiable tangible and intangible assets	\$	<u>69,963</u>

City of Hope

Notes to Consolidated Financial Statements (continued)

8. Community Benefit Expense (Unaudited)

City of Hope supports a variety of programs and services that provide a direct benefit to its patients, as well as to the broader community. The primary categories of community benefit are as follows:

- Benefits for the Broader Community – Clinical Research
- Benefits for the Broader Community – Support of Basic Science Research
- Public Information and Education

City of Hope supports a variety of clinical and basic science research activities focused on finding cures and treatments for cancer and other life-threatening diseases and the development of diagnostics for which research grants, contracts, and clinical trial funding is not available. The cost of these institutionally funded research efforts is considered a benefit to the broader community. In addition, the cost of providing public information and education is also considered a community benefit.

The Center and the Foundation accept all patients who are covered by governmental subsidized programs – primarily Medi-Cal and Medicare fee for service, and who meet certain clinical criteria. These programs typically remit payments substantially less than charges and below the cost of providing the services. The Center and the Foundation have estimated the costs of treating patients less payments received for these costs. The residual amount of costs in excess of payments has been included as a component of community benefit.

City of Hope

Notes to Consolidated Financial Statements (continued)

8. Community Benefit Expense (Unaudited) (continued)

The following is a summary of the estimated benefits for the broader community through internally funded research support and Support of Governmental Health Care Programs – Medi-Cal and Medicare expense, at cost, in terms of service to the indigent for the years ended September 30 (amounts in thousands):

	<u>2019</u>	<u>2018</u>
Benefits for the Broader Community – Support for Research (unaudited)		
Estimated institutionally supported research costs, net of grants received of \$169,314 and \$152,821 in 2019 and 2018, respectively:		
Center	\$ 120,308	\$ 108,550
Institute	188,339	172,247
TGen	<u>42,808</u>	<u>26,460</u>
Total estimated benefits for the broader community, at cost	<u>351,455</u>	307,257
Support of Governmental Health Care Programs (unaudited)		
Estimated unreimbursed cost of the Medi-Cal Program, less net impact of the California hospital fee program of \$52,254 and \$109,145 in 2019 and 2018, respectively	31,033	9,508
Estimated unreimbursed cost of the Medicare Program	<u>144,483</u>	<u>146,586</u>
	<u>175,516</u>	156,094
Total estimated benefits for the broader community and unreimbursed costs to governmental health care programs	<u>\$ 526,971</u>	<u>\$ 463,351</u>

9. Endowment

City of Hope’s endowment consists of approximately 124 individual funds established for a variety of purposes. The endowments include both donor-restricted “true” endowment funds, which are classified as net assets with donor restrictions, and funds designated by the Board to function as an endowment, which are classified as net assets without donor restrictions. City of Hope’s endowment is invested in an investment pool.

City of Hope

Notes to Consolidated Financial Statements (continued)

9. Endowment (continued)

Interpretation of Relevant Law

ASC 958 provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). City of Hope classifies donor-restricted true endowment funds to include (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) changes to the permanent endowment made in accordance with the direction of the applicable donor gift instrument. Also included in net assets with donor restrictions is the accumulated appreciation on donor restricted true endowment funds, which are available for expenditure in a manner consistent with the standard of prudence prescribed by UPMIFA, and any deficiencies associated with investments where the value of the fund has fallen below the original value of the gift.

In accordance with UPMIFA, City of Hope considers the following factors when appropriating or accumulating donor-restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the donor-restricted endowment fund
- General economic conditions
- The possible effects of inflation and deflation
- The expected total return from income and appreciation of investments
- Other resources of City of Hope
- The investment policies of City of Hope

City of Hope

Notes to Consolidated Financial Statements (continued)

9. Endowment (continued)

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor restricted true endowment funds may fall below the level that the donor or UPMIFA requires to be retained as a fund of perpetual duration. Deficiencies of this nature are reported in donor restricted true endowment net assets. As of September 30, 2019 and 2018, seven funds and six funds with an original gift value of \$10,459,000 and \$7,779,000 were underwater by \$761,000 and \$407,000, respectively.

Return Objectives and Risk Parameters

City of Hope's financial objective is to achieve a long-term rate of return that will enhance and preserve the real (inflation-adjusted) purchasing power of the corpus without subjecting the investment portfolio to large investment losses. Assets are invested in a manner that is intended to produce results that exceed the respective benchmark while assuming a moderate level of investment risk. Actual returns in any given year may vary from this amount.

Strategies and Endowment Payout

City of Hope relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). City of Hope targets a diversified asset allocation to achieve its long-term return objectives within prudent risk constraints. In accordance with City of Hope's total return objective, up to 5% of the annual fair value as measured on January 1 each year is available for expenditure in the form of endowment payout for expenditures or purposes as defined by the endowment agreements.

City of Hope

Notes to Consolidated Financial Statements (continued)

9. Endowment (continued)

Changes in the fair value of City of Hope’s endowment investments and other endowment net assets by type of fund for the years ended September 30, 2019 and 2018, are as follows (amounts in thousands):

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, September 30, 2017	\$ 815,638	\$ 233,762	\$ 1,049,400
Investment income	12,923	3,686	16,609
Net appreciation	56,616	15,431	72,047
Contributions	–	4,710	4,710
Appropriation for expenditures	(1,050)	(5,702)	(6,752)
Endowment net assets, September 30, 2018	884,127	251,887	1,136,014
Investment income	15,074	4,155	19,229
Net appreciation	(3,482)	1,014	(2,468)
Contributions	–	15,735	15,735
Appropriation for expenditures	(609)	(7,293)	(7,902)
Endowment net assets, September 30, 2019	\$ 895,110	\$ 265,498	\$ 1,160,608
Donor-restricted true endowment:			
Historical gift value	\$ –	\$ 188,055	\$ 188,055
Appreciation	–	77,443	77,443
Board designated funds functioning as an endowment	895,110	–	895,110
Endowment net assets, September 30, 2019	\$ 895,110	\$ 265,498	\$ 1,160,608

City of Hope

Notes to Consolidated Financial Statements (continued)

10. Net Assets with Donor Restrictions

Net assets with donor restrictions are available to fund the following purposes as of September 30 (amounts in thousands):

	2019	2018
Time-restricted under annuity and split-interest obligations and other	\$ 88,437	\$ 91,527
Patient care	32,490	30,362
Education	29,493	30,960
Research	458,673	430,471
Medical equipment and buildings	15,373	9,612
Total net assets with donor restrictions	\$ 624,466	\$ 592,932

Net assets were released from donor restrictions by satisfying the following restricted purposes in the years ended September 30 (amounts in thousands):

	2019	2018
Time-restricted under annuity and split-interest obligations and other	\$ 5,347	\$ 3,791
Patient care	1,621	513
Education	2,331	2,012
Research	67,055	54,244
Equipment and buildings	2,883	2,004
Total donor restricted net assets released from restrictions	\$ 79,237	\$ 62,564

11. Functional Classification of Expenses

City of Hope's primary program services consist of patient care, research, and public information and education. Expenses in general support of the program services of City of Hope are considered support services and include administrative and fundraising activities. Natural expenses that are attributable to more than one functional expense category are allocated using a variety of cost allocation methodologies, including headcount, square footage, and time and effort.

City of Hope

Notes to Consolidated Financial Statements (continued)

11. Functional Classification of Expenses (continued)

The expenses reported on the consolidated statements of activities supported the following programs and functions for the years ended September 30, 2019 and 2018 (amounts in thousands):

	Patient Care	Research	Public Information and Education	Administrative	Fundraising	Total
2019						
Salaries, wages, and employee benefits	\$ 361,481	\$ 222,476	\$ 7,562	\$ 220,315	\$ 14,261	\$ 826,095
Purchased services and professional fees	231,227	80,352	13,934	128,085	12,194	465,792
Supplies and pharmaceuticals	434,268	60,568	396	17,200	2,231	514,663
Royalty sharing	19	118,426	-	-	-	118,445
Interest, including changes in fair value of swap agreement	34,081	17,746	441	7,620	-	59,888
Depreciation and amortization	70,005	36,181	782	32,880	458	140,306
Hospital provider fee	15,735	-	-	-	-	15,735
Other expense	30,738	26,609	586	25,973	1,872	85,778
Total expenses	<u>\$ 1,177,554</u>	<u>\$ 562,358</u>	<u>\$ 23,701</u>	<u>\$ 432,073</u>	<u>\$ 31,016</u>	<u>\$ 2,226,702</u>

	Patient Care	Research	Public Information and Education	Administrative	Fundraising	Total
2018						
Salaries, wages, and employee benefits	\$ 324,367	\$ 197,744	\$ 10,446	\$ 193,435	\$ 14,447	\$ 740,439
Purchased services and professional fees	192,783	70,650	11,594	169,254	7,458	451,739
Supplies and pharmaceuticals	362,053	45,366	669	14,454	2,198	424,740
Royalty sharing	16	155,360	-	-	-	155,376
Interest, including changes in fair value of swap agreement	19,236	7,343	370	5,586	-	32,535
Depreciation and amortization	65,203	31,036	1,208	28,380	471	126,298
Hospital provider fee	40,836	-	-	-	-	40,836
Other expense	30,327	30,581	604	27,480	2,197	91,189
Total expenses	<u>\$ 1,034,821</u>	<u>\$ 538,080</u>	<u>\$ 24,891</u>	<u>\$ 438,589</u>	<u>\$ 26,771</u>	<u>\$ 2,063,152</u>

City of Hope

Notes to Consolidated Financial Statements (continued)

12. Commitments and Contingencies

Leases

City of Hope has noncancelable operating leases for office space and equipment that expire on various dates through 2072. As of September 30, 2019, future minimum payments required under these operating leases are as follows (amounts in thousands):

2020	\$	14,805
2021		14,271
2022		11,835
2023		9,532
2024		8,305
Thereafter		101,368
	\$	<u>160,116</u>

Amounts above have not been reduced by sublease income totaling \$943,000 through 2021.

Lease expense for the leases shown above and other month-to-month rental agreements totaled \$19,111,000 and \$14,880,000 in 2019 and 2018, respectively.

Assets Constructed by Landlord – Under ASC 840, *Leases*, a build to suit arrangement exists when a lessee is, among other things, financially involved in the construction of certain structural improvements prior to the commencement of the lease. Under both of the lease agreements discussed below, the Foundation will be financially involved in the construction of non-normal tenant improvements of the building, which results in the Foundation being considered the owner of the assets during the construction period. As construction of the medical office buildings progresses, the Foundation will record the costs paid by the landlord to construct the building as construction in progress and a related long-term financing obligation.

Upon completion of construction, projects will be evaluated for sales lease-back treatment, and, should the criteria not be met, the Foundation will carry and amortize the financing obligation to the extent that lease payments are applied to the liability and depreciate the building over the estimated useful life.

In December 2016, the Foundation entered into a 15-year lease agreement with San Antonio Regional Hospital (SARH) for an outpatient cancer center to be owned and operated by the

City of Hope

Notes to Consolidated Financial Statements (continued)

12. Commitments and Contingencies (continued)

Foundation. The lease agreement provides for the design and construction of a medical office building by SARH. The lease agreement is subject to build to suit accounting under ASC 840. Upon completion of construction of this building in 2019, the Foundation re-evaluated the lease agreement under sales lease-back guidance, and it was determined that the lease qualifies for sales lease-back treatment. As of September 30, 2019, the Foundation has derecognized \$18,447,000 in construction in progress and other long-term liabilities. The Foundation began operating a multidisciplinary community cancer center at this location in September 2019.

On October 23, 2018, the Foundation entered into a 15-year lease agreement with a developer for a medical office building. The lease provides for the design and construction of an office building that is subject to build to suit accounting under ASC 840. Upon completion of construction of this building in 2021, the Foundation will evaluate the lease under sales lease back criteria to determine whether the Foundation will continue to carry and amortize the construction costs over the life of the lease. The Foundation expects to begin operating a multidisciplinary community cancer center at this location in 2021. The aggregate lease payments that the Foundation will be obligated to make under the lease agreement are approximately \$16,470,000.

Collective Bargaining Agreements

City of Hope is subject to six collective bargaining agreements related to certain members of its labor force. Approximately 48% of employees are covered under collective bargaining agreements as of September 30, 2019. Three of the six agreements will expire within one year of September 30, 2019, and these agreements are anticipated to be renegotiated and renewed for one to three years, depending on the agreement.

Litigation and Administrative Actions

From time to time, City of Hope is subject to claims arising in the ordinary course of business. In the opinion of management, with the exception of the matters discussed below, the ultimate resolution of legal proceedings and other claims currently pending will not have a material adverse effect on the consolidated financial position, statements of activities, or cash flows of City of Hope.

City of Hope has been engaged in various proceedings involving challenges to the validity of U.S. Patent No. 6,331,415 issued December 18, 2001, titled “Methods of Producing Immunoglobulins, Vectors and Transformed Host Cells for Use Therein” (the Cabilly II patent) and U.S. Patent No. 7,923,221 titled “Methods of Making Antibody Heavy and Light Chains Having Specificity

City of Hope

Notes to Consolidated Financial Statements (continued)

12. Commitments and Contingencies (continued)

for a Desired Antigen” (the Cabilly III patent and, together with Cabilly II patent, the Cabilly patents). Both Cabilly patents are co-owned by City of Hope and Genentech and expired in December 2018. The only pending litigation involving the patents are the Amgen litigations summarized below:

On October 6, 2017, Amgen Inc. filed a lawsuit against Genentech, Inc. and City of Hope, Case No. 2:17-cv-07349 GW, in the United States District Court (USDC) for the Central District of California. Amgen is seeking a declaratory judgment of patent non-infringement, invalidity, and unenforceability against the Cabilly patents relating to its Avastin biosimilar product. Defendants filed a motion to dismiss Amgen’s complaint on November 15, 2017. The motion was granted on February 2, 2018.

On October 6, 2017, Genentech and City of Hope filed a lawsuit against Amgen, Case No. 1:17-cv-01407, in the USDC for the District of Delaware. Genentech and City of Hope assert, inter alia, the Cabilly patents against Amgen relating to Amgen’s Avastin biosimilar product. On October 10, 2017, Amgen moved to transfer the case to the Central District of California. The Court denied Amgen’s motion on January 22, 2018. Amgen filed a motion to dismiss Count 1 of the amended complaint on December 20, 2017. On April 17, 2018, the Court granted the motion without prejudice. On May 1, 2018, Amgen answered the amended complaint and asserted affirmative defenses. Amgen also counterclaimed against plaintiffs, seeking a declaration of non-infringement and invalidity of the patents in suit. On June 5, 2018, Amgen amended its answer, affirmative defenses, and counterclaims. On June 19, 2018, Genentech and City of Hope moved to dismiss or strike Amgen’s amended counterclaims and certain affirmative defenses asserted by Amgen. This matter has been fully briefed. On October 22, 2018, this case was consolidated with 1:17-cv-01471, discussed below, and was named the lead action.

On October 18, 2017, Genentech and City of Hope filed another lawsuit against Amgen, Case No. 1:17-cv-01471, in the USDC for the District of Delaware. This declaratory relief action for patent infringement is substantially similar to Case No. 1:17-cv-01407, which was filed to ensure compliance with certain provisions of the Biologics Price Competition and Innovation Act of 2009 (BPCIA). Amgen moved to transfer this case to the Central District of California on October 23, 2017. The Court denied Amgen’s motion on January 22, 2018. On December 20, 2017, Amgen moved to dismiss Count 30 of the amended complaint. On April 17, 2018, the Court granted the motion without prejudice. Amgen filed its answer, affirmative defenses, and counterclaims on May 1, 2018. On May 22, 2018, Genentech and City of Hope moved to dismiss and/or strike Amgen’s counterclaims and several affirmative defenses. The motion has been fully briefed. On

City of Hope

Notes to Consolidated Financial Statements (continued)

12. Commitments and Contingencies (continued)

July 10, 2019, Genentech moved in the consolidated actions for a temporary restraining order to prevent Amgen from commercially launching its Avastin biosimilar product in the United States on the grounds that Amgen failed to adhere to the requirements of the BCPIA. That motion was denied on July 18, 2019, and Amgen commercially launched its Avastin biosimilar product on the same day. Genentech filed an appeal of this decision on July 19, 2019, and briefing is in progress. In the district court litigation, discovery continues, with fact discovery scheduled to close on December 20, 2019, and expert discovery scheduled to close on May 22, 2020. Trial is set to begin on November 30, 2020.

A final adverse ruling on validity or enforceability of either of the Cabilly patents in any of the proceedings listed above could significantly reduce or eliminate only the post-expiry revenue, which could have a material adverse impact on the financial condition of the Obligated Group. The Obligated Group expects to receive carryover revenue related to sales from products manufactured before the expiry date. However, that amount cannot be determined at this time.

Health Care Regulations

The Center and the Foundation are subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, licensure, accreditation, governmental health care program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Federal laws prohibit submission of claims for reimbursement to the Medicare and Medicaid programs for services not rendered in accordance with applicable rules, laws, and regulations. Any overpayments received must be refunded to the government payor. Violation of these laws can result in substantial civil and criminal penalties and fines, including treble damages and mandatory penalties of up to \$11,000 per claim, as well as possible debarment from future participation in government health care programs. Management believes that the Center and the Foundation are presently in compliance with fraud and abuse laws, as well as other applicable government laws and regulations. While no material regulatory inquiries about past or present conduct have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

Capital Commitments (Unaudited)

As of September 30, 2019, City of Hope has committed to spend approximately \$109,302,000 through 2020 and beyond for building renovations, multiple campus facility renovations, and various information technology projects.

City of Hope

Notes to Consolidated Financial Statements (continued)

13. Subsequent Events

City of Hope has evaluated subsequent events occurring between the end of the most recent fiscal year and December 20, 2019, the date these consolidated financial statements were issued.

Supplementary Information

City of Hope and Affiliates
Consolidating Statements of Financial Position
(In Thousands)

September 30, 2019 and 2018

	Obligated Group						Consolidated 2019	Consolidated 2018
	City of Hope	Additional Obligated Group Members	Eliminating Entries	Obligated Group	Affiliated Group	Eliminating Entries		
Assets								
Current assets:								
Cash and cash equivalents	\$ 8,705	\$ 191,689	\$	\$ 200,394	\$ 38,141	\$	\$ 238,535	\$ 377,571
Investments	942,908	984,517	-	1,927,425	-	-	1,927,425	1,526,106
Self-insurance trust funds	-	3,418	-	3,418	-	-	3,418	3,765
Patient accounts receivable, net	-	235,989	-	235,989	-	-	235,989	238,384
Due from affiliates	1,913	65,060	(57,427)	9,546	24,818	(34,364)	-	-
Grants and other receivables	72,500	75,902	-	148,402	9,774	-	158,176	95,981
Due from third-party payors	-	-	-	-	-	-	-	342
Donor-restricted unconditional promises to give, net	16,287	-	-	16,287	8,162	-	24,449	18,576
Prepaid and other	80	42,787	-	42,867	4,284	-	47,151	39,105
Total current assets	1,042,393	1,599,362	(57,427)	2,584,328	85,179	(34,364)	2,635,143	2,299,830
Property and equipment, net	14,847	893,650	-	908,497	69,221	-	977,718	930,236
Other assets:								
Investments held for long-term purposes	17,544	220,020	-	237,564	-	-	237,564	302,822
Board-designated assets	93,775	801,335	-	895,110	-	-	895,110	884,127
Bond trust funds	-	380,242	-	380,242	-	-	380,242	-
With donor restrictions:								
Investments	507,355	23,270	-	530,625	26,511	-	557,136	518,251
Unconditional promises to give, net	45,088	-	-	45,088	499	-	45,587	60,741
Contributions receivable from annuity and split-interest agreements, net	15,716	-	-	15,716	-	-	15,716	13,182
Other	3,565	-	-	3,565	-	-	3,565	9,452
Intangible assets	-	380	-	380	9,658	-	10,038	10,667
Goodwill	-	-	-	-	53,160	-	53,160	59,067
Other long-term assets	55,077	79,556	-	134,633	2,870	(78,846)	58,657	47,428
Total other assets	738,120	1,504,803	-	2,242,923	92,698	(78,846)	2,256,775	1,905,737
Total assets	\$ 1,795,360	\$ 3,997,815	\$ (57,427)	\$ 5,735,748	\$ 247,098	\$ (113,210)	\$ 5,869,636	\$ 5,135,803

PRELIMINARY AND TENTATIVE FOR DISCUSSION ONLY

City of Hope and Affiliates

Consolidating Statements of Financial Position (continued)
(In Thousands)

September 30, 2019 and 2018

	Obligated Group						Consolidated 2019	Consolidated 2018
	City of Hope	Additional Obligated Group Members	Eliminating Entries	Obligated Group	Affiliated Group	Eliminating Entries		
Liabilities and net assets								
Current liabilities:								
Accounts payable and accrued liabilities	\$ 3,078	\$ 184,029	\$ -	\$ 187,107	\$ 10,974	\$ -	\$ 198,081	\$ 150,553
Accrued salaries, wages, and employee benefits	6,793	97,113	-	103,906	3,927	-	107,833	87,473
Long-term debt, current portion	-	10,544	-	10,544	2,948	-	13,492	13,051
Due to third-party payors	-	25,675	-	25,675	-	-	25,675	-
Deferred revenue	1,492	20,751	-	22,243	6,538	-	28,781	28,404
Due to affiliates	49,028	33,217	(57,427)	24,818	9,546	(34,364)	-	-
Total current liabilities	60,391	371,329	(57,427)	374,293	33,933	(34,364)	373,862	279,481
Long-term debt, net of current portion	-	1,332,560	-	1,332,560	41,097	-	1,373,657	1,003,810
Annuity and split-interest agreement obligations	19,068	-	-	19,068	-	-	19,068	20,464
Deferred rent	-	5,662	-	5,662	242	-	5,904	10,146
Interest rate swaps	-	19,489	-	19,489	-	-	19,489	6,549
Other	462	54,948	-	55,410	1,703	-	57,113	60,115
Total liabilities	79,921	1,783,988	(57,427)	1,806,482	76,975	(34,364)	1,849,093	1,380,565
Net assets:								
Without donor restrictions:								
Controlling interests	1,147,589	2,190,557	-	3,338,146	104,479	(78,846)	3,363,779	3,127,206
Noncontrolling interest	-	-	-	-	32,298	-	32,298	35,100
With donor restrictions	567,850	23,270	-	591,120	33,346	-	624,466	592,932
Total net assets	1,715,439	2,213,827	-	3,929,266	170,123	(78,846)	4,020,543	3,755,238
Total liabilities and net assets	\$ 1,795,360	\$ 3,997,815	\$ (57,427)	\$ 5,735,748	\$ 247,098	\$ (113,210)	\$ 5,869,636	\$ 5,135,803

PRELIMINARY AND TENTATIVE FOR DISCUSSION ONLY

City of Hope and Affiliates

Consolidating Statements of Activities (In Thousands)

Years Ended September 30, 2019 and 2018

	Obligated Group						Consolidated 2019	Consolidated 2018
	City of Hope	Additional Obligated Group Members	Eliminating Entries	Obligated Group	Affiliated Group	Eliminating Entries		
Revenues:								
Net patient service revenues	-	1,555,575	-	1,555,575	-	-	1,555,575	1,375,498
Research grants and clinical trials	-	145,363	-	145,363	23,951	-	169,314	152,821
Contributions	114,050	4,011	-	118,061	56,030	(22,663)	151,428	163,215
Investment income	97,753	141,824	-	239,577	425	-	240,002	184,312
Net unrealized gain (loss) on investments	(62,288)	(88,201)	-	(150,489)	19	-	(150,470)	27,267
Royalty and licensing income	379,597	3,792	-	383,389	1,125	-	384,514	500,370
Professional fees revenue	-	81,007	(81,007)	-	-	-	-	-
Other revenue	1,083	52,754	(1,093)	52,744	31,037	(27,244)	56,537	44,566
Total revenues	530,195	1,896,125	(82,100)	2,344,220	112,587	(49,907)	2,406,900	2,448,049
Expenses:								
Salaries wages and employee benefits	34,717	752,026	-	786,743	39,352	-	826,095	740,439
Purchased services and professional fees	18,372	533,650	(81,425)	470,597	23,208	(28,013)	465,792	451,739
Supplies and pharmaceuticals	4,409	498,269	-	502,678	11,985	-	514,663	424,740
Royalty sharing	-	118,445	-	118,445	-	-	118,445	155,376
Interest, including changes in fair value of swap agreements	-	57,836	-	57,836	2,052	-	59,888	32,535
Depreciation and amortization	1,263	124,065	-	125,328	14,978	-	140,306	126,298
Hospital provider fee	-	15,735	-	15,735	-	-	15,735	40,836
Other expense	5,105	66,580	(675)	71,010	14,768	-	85,778	91,189
Total expenses	63,866	2,166,606	(82,100)	2,148,372	106,343	(28,013)	2,226,702	2,063,152
Excess (deficiency) of revenues and other increases over expenses	466,329	(270,481)	-	195,848	6,244	(21,894)	180,198	384,897
Distributions (to) from affiliates	(424,657)	398,020	-	(26,637)	3,974	22,663	-	-
Distributions to controlling and noncontrolling interests	-	-	-	-	(4,083)	2,046	(2,037)	-
Contributed capital - noncontrolling	-	-	-	-	-	-	-	34,911
Cumulative changes in net assets from adoption of new accounting standards	125,991	(38,847)	-	87,144	-	-	87,144	-
Changes in net assets	167,663	88,692	-	256,355	6,135	2,815	265,305	419,808
Net assets, beginning of year	1,547,776	2,125,135	-	3,672,911	163,988	(81,661)	3,755,238	3,335,430
Net assets, end of year	\$ 1,715,439	\$ 2,213,827	\$ -	\$ 3,929,266	\$ 170,123	\$ (78,846)	\$ 4,020,543	\$ 3,755,238

PRELIMINARY AND TENTATIVE FOR DISCUSSION ONLY

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