

Vanderbilt University Medical Center

**Consolidated Financial Statements and
Supplementary Information
Years Ended June 30, 2021 and 2020**

Ernst & Young LLP



Vanderbilt University Medical Center
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June 30, 2021 and 2020

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Report of Independent Auditors

The Board of Directors
Vanderbilt University Medical Center

We have audited the accompanying consolidated financial statements of Vanderbilt University Medical Center, which comprise the consolidated balance sheets as of June 30, 2021 and 2020, and the related consolidated statements of operations and changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 Vanderbilt University Medical Center at June 30, 2021 and 2020, and the consolidated results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

October 1, 2021

Vanderbilt University Medical Center
Consolidated Balance Sheets
June 30, 2021 and 2020

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|---------------------|---------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 837,312 | \$ 1,170,526 |
| Current investments | 215,484 | 232,178 |
| Patient accounts receivable | 553,874 | 470,550 |
| Grants and contracts receivable | 77,365 | 60,031 |
| Inventories | 140,281 | 104,603 |
| Other current assets | 118,259 | 118,439 |
| Total current assets | 1,942,575 | 2,156,327 |
| Restricted cash | 27,404 | 11,806 |
| Noncurrent investments | 779,389 | 539,173 |
| Noncurrent investments limited as to use | 127,414 | 113,526 |
| Property, plant, and equipment, net | 1,630,325 | 1,525,103 |
| Operating lease assets | 839,850 | 846,695 |
| Other noncurrent assets | 96,351 | 53,347 |
| Total assets | <u>\$ 5,443,308</u> | <u>\$ 5,245,977</u> |
| Liabilities and Net Assets | | |
| Current liabilities: | | |
| Current portion of long-term debt | \$ 14,704 | \$ 14,321 |
| Short-term borrowings | 300,000 | 100,000 |
| Accounts payable and other accrued expenses | 356,171 | 309,162 |
| Medicare accelerated payments | 189,427 | 222,445 |
| Estimated payables under third-party programs | 37,669 | 45,957 |
| Accrued compensation and benefits | 316,531 | 238,039 |
| Current portion of operating lease liabilities | 67,343 | 70,062 |
| Current portion of deferred revenue | 4,240 | 4,827 |
| Current portion of medical malpractice self-insurance reserves | 15,820 | 12,577 |
| Total current liabilities | 1,301,905 | 1,017,390 |
| Long-term debt, net of current portion | 1,432,150 | 1,841,290 |
| Noncurrent portion of operating lease liabilities | 795,330 | 797,811 |
| Fair value of interest rate exchange agreements | 76,864 | 100,342 |
| Noncurrent portion of medical malpractice self-insurance reserves | 56,770 | 47,682 |
| Noncurrent portion of deferred revenue | 2,923 | 4,027 |
| Other noncurrent liabilities | 46,986 | 35,449 |
| Total liabilities | 3,712,928 | 3,843,991 |
| Net assets | | |
| Net assets without donor restrictions controlled by Vanderbilt University Medical Center | 1,497,483 | 1,208,796 |
| Net assets without donor restrictions related to noncontrolling interests | 8,339 | 6,635 |
| Total net assets without donor restrictions | 1,505,822 | 1,215,431 |
| Net assets with donor restrictions | 224,558 | 186,555 |
| Total net assets | 1,730,380 | 1,401,986 |
| Total liabilities and net assets | <u>\$ 5,443,308</u> | <u>\$ 5,245,977</u> |

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

Vanderbilt University Medical Center
Consolidated Statements of Operations
Years Ended June 30, 2021 and 2020

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|-------------------|-------------------|
| Operating revenues | | |
| Patient service revenue | \$ 4,691,814 | \$ 4,031,720 |
| Academic and research revenue | 614,611 | 552,822 |
| Other operating revenue | 228,204 | 301,143 |
| Total operating revenues | <u>5,534,629</u> | <u>4,885,685</u> |
| Operating expenses | | |
| Salaries, wages, and benefits | 2,836,544 | 2,495,795 |
| Supplies and drugs | 1,216,203 | 1,046,398 |
| Facilities and equipment | 296,748 | 273,405 |
| Services and other | 795,287 | 740,255 |
| Depreciation and amortization | 151,454 | 126,654 |
| Interest | 60,530 | 60,771 |
| Total operating expenses | <u>5,356,766</u> | <u>4,743,278</u> |
| Income from operations | <u>177,863</u> | <u>142,407</u> |
| Nonoperating revenues and expenses | | |
| Income from investments | 68,201 | 27,224 |
| Gift income | 19,104 | 20,702 |
| Earnings of unconsolidated organizations | 8,100 | 4,865 |
| Unrealized gain (loss) on interest rate exchange agreements, net of cash settlements | <u>17,372</u> | <u>(37,152)</u> |
| Total nonoperating revenues and expenses | <u>112,777</u> | <u>15,639</u> |
| Excess of revenues over expenses | 290,640 | 158,046 |
| Excess of revenues over expenses attributable to noncontrolling interests | <u>(6,295)</u> | <u>(4,074)</u> |
| Excess of revenues over expenses attributable to VUMC | 284,345 | 153,972 |
| Other changes in net assets without donor restrictions | | |
| Change in noncontrolling interests' net assets | 1,704 | (1,141) |
| Net assets released from restriction for capital | 474 | 4,773 |
| Other changes | 3,868 | (458) |
| Total changes in net assets without donor restrictions | <u>\$ 290,391</u> | <u>\$ 157,146</u> |

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

Vanderbilt University Medical Center
Consolidated Statements of Changes in Net Assets
Years Ended June 30, 2021 and 2020

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|---------------------|---------------------|
| Net assets without donor restrictions | | |
| Net assets without donor restrictions at the beginning of the period | \$ 1,215,431 | \$ 1,058,285 |
| Excess of revenues over expenses | 284,345 | 153,972 |
| Change in noncontrolling interests' net assets | 1,704 | (1,141) |
| Net assets released from restriction for capital | 474 | 4,773 |
| Other changes | 3,868 | (458) |
| Change in net assets without donor restrictions | 290,391 | 157,146 |
| Net assets without donor restrictions at the end of the period | <u>\$ 1,505,822</u> | <u>\$ 1,215,431</u> |
| Net assets with donor restrictions | | |
| Net assets with donor restrictions at the beginning of the period | \$ 186,555 | \$ 155,897 |
| Contributions | 46,824 | 45,079 |
| Restricted investment income | 11,169 | 1,727 |
| Net assets released from restrictions for operations | (15,647) | (13,788) |
| Net assets released from restriction for capital | (474) | (4,773) |
| Other changes | (3,869) | 2,413 |
| Change in net assets with donor restrictions | 38,003 | 30,658 |
| Net assets with donor restrictions at the end of the period | <u>\$ 224,558</u> | <u>\$ 186,555</u> |
| Total net assets | | |
| Beginning of the period | \$ 1,401,986 | \$ 1,214,182 |
| Change in total net assets | 328,394 | 187,804 |
| End of the period | <u>\$ 1,730,380</u> | <u>\$ 1,401,986</u> |

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

Vanderbilt University Medical Center
Consolidated Statements of Cash Flows
Years Ended June 30, 2021 and 2020

| (\$ in thousands) | 2021 | 2020 |
|---|------------|--------------|
| Cash flows from operating activities | | |
| Change in total net assets | \$ 328,394 | \$ 187,804 |
| Adjustments to reconcile change in total net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | 151,454 | 126,654 |
| Amortization of debt issuance costs, and original issue premium and discount | 953 | 709 |
| Loss on disposal of assets | 524 | 1,116 |
| Undistributed equity in earnings of equity method affiliates | (2,949) | (1,754) |
| Investment gains and losses | (64,917) | (8,662) |
| Purchases of trading securities | (391,959) | (392,111) |
| Sales of trading securities | 363,454 | 242,191 |
| Change in split-interest trusts | (2,380) | 260 |
| Unrealized (gain) loss on interest rate exchange agreements | (23,478) | 32,441 |
| Restricted contributions for endowments and property, plant, and equipment | (21,755) | (14,073) |
| Increase (decrease) in cash due to changes in: | | |
| Patient accounts receivable | (83,324) | 11,935 |
| Accounts payable and other accrued expenses | 44,666 | 21,141 |
| Medicare accelerated payments | (33,018) | 222,445 |
| Other assets and other liabilities, net | 46,411 | 6,755 |
| Net cash provided by operating activities | 312,076 | 436,851 |
| Cash flows from investing activities | | |
| Purchase of property, plant, and equipment | (236,244) | (238,291) |
| Acquisition of hospitals | (15,600) | (19,252) |
| Acquisition of equity method investment | (36,927) | - |
| Purchases of long-term securities | (437,281) | (255,581) |
| Sales and maturities of long-term securities | 295,673 | 239,623 |
| Proceeds on sale of property, plant, and equipment | 15 | 5 |
| Net cash used in investing activities | (430,364) | (273,496) |
| Cash flows from financing activities | | |
| Proceeds from issuance of debt | 200,000 | 463,600 |
| Draws on lines of credit | 100,000 | 100,000 |
| Debt issuance costs | (459) | (1,645) |
| Repayment of debt and lines of credit | (510,267) | (133,070) |
| Principal payments under finance lease obligations | (5,766) | (4,334) |
| Restricted contributions for endowments and property, plant, and equipment | 21,755 | 14,073 |
| Distributions to noncontrolling interests | (4,591) | (6,333) |
| Net cash (used in) provided by financing activities | (199,328) | 432,291 |
| Net change in cash, cash equivalents, and restricted cash | (317,616) | 595,646 |
| Cash, cash equivalents, and restricted cash | | |
| Beginning of the period | 1,182,332 | 586,686 |
| End of the period | \$ 864,716 | \$ 1,182,332 |

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

Vanderbilt University Medical Center

Notes to Consolidated Financial Statements

June 30, 2021 and 2020

1. Description of Organization

Vanderbilt University Medical Center (“VUMC”) is a Tennessee not-for-profit corporation incorporated in March 2015 to operate an academic medical center, including a comprehensive research, teaching, and patient care health system (the “Medical Center”). Until April 29, 2016, the Medical Center operated as a unit within Vanderbilt University (“the University” or “VU”), as a part of the University’s administrative structure, with the same governing board, legal, financial, and other shared services.

VUMC began operations effective April 30, 2016, following the closing of the sale of the Medical Center by the University (the “Acquisition”). VUMC owns and operates three hospitals located on the main campus of the University in Nashville, Tennessee: Vanderbilt University Hospital (“VUH”), Monroe Carell Junior Children’s Hospital at Vanderbilt (“MCJCHV”), and Vanderbilt Psychiatric Hospital (“VPH”). In addition, VUMC partially owns Vanderbilt Stallworth Rehabilitation Hospital (“VSRH”), also located on the main campus of the University, through a joint venture with Encompass Health Corp. in which VUMC holds a 50% interest, which includes a 1% interest held by Vanderbilt Health Services, LLC, (“VHS”), a VUMC wholly owned subsidiary. Effective August 1, 2019, VUMC acquired a hospital from Community Health Systems, Inc. (“CHS”): Tennova Healthcare – Lebanon, now known as Vanderbilt Wilson County Hospital (“VWCH”). Effective January 1, 2021, VUMC acquired from CHS: Tennova Healthcare – Shelbyville and Tennova Healthcare – Harton, now known as Vanderbilt Bedford Hospital (“VBCH”) and Vanderbilt Tullahoma-Harton Hospital (“VTHH”). At the same time as the acquisition of VBCH and VTHH, VUMC acquired a noncontrolling ownership interest of 20% in CHS’s affiliated Tennova Healthcare – Clarksville (“VMH”). VUH, MCJCHV, VPH, VWCH, VBCH, and VTHH are licensed for 1,664 beds, and VSRH is licensed for 80 beds.

VUMC consists of two major operating divisions and an administrative overhead division. The operating divisions include the Clinical Enterprise and Academic Enterprise divisions. The administrative overhead division is referred to as Medical Center Administration (“MCA”).

The Clinical Enterprise division includes the professional clinical practice revenues and related expenses of Vanderbilt Medical Group (“VMG”), and technical revenues and associated expenses for the operation of VUMC’s hospitals and clinic facilities, including VUH, MCJCHV, VPH, VWCH, VBCH, and VTHH. The Clinical Enterprise also includes VHS.

- VUH is a quaternary care teaching hospital licensed for 726 acute care and specialty beds. VUH, a Level I trauma center, provides advanced patient care and serves as a key site for medical education and clinical research conducted by physician faculty. VUH includes a comprehensive burn center, the Vanderbilt Transplant Center, the Vanderbilt Heart and Vascular Institute, and the Vanderbilt Ingram Cancer Center. As of June 30, 2021, VUMC held a temporary license provided under the Board for Licensing Health Care Facilities (“BLHCF”) Policy 82 to license 49 additional beds in response to COVID-19. This licensure increase is comprised of 34 observation beds and 15 double occupancy beds. The beds associated with this temporary license are not included in the above VUH bed count.
- MCJCHV is a pediatric quaternary care teaching hospital licensed for 343 beds (159 acute and specialty, 65 pediatric intensive care, and 119 neonatal intensive care). MCJCHV is the region’s only full-service pediatric hospital, with over 30 pediatric specialties. MCJCHV serves as a site for medical education and clinical research conducted by pediatric physician faculty, houses the only Level IV neonatal intensive care center and the only Level 1 pediatric trauma center within the region, and is a regional referral center for extracorporeal membrane oxygenation (heart and lung failure).

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- VPH is a psychiatric hospital licensed for 106 beds and provides inpatient care to pediatric, adolescent, adult, and geriatric patients. Also, VPH provides partial hospitalization programs to both adult and adolescent patients, psychiatric assessment services, adult intensive outpatient programs, pediatric and adult ambulatory outpatient treatment, and neuromodulation procedures through electroconvulsive therapy and transcranial magnetic stimulation.
- VWCH is a two-campus facility licensed for 245 beds and is a substantial provider of both inpatient and outpatient medical services in Lebanon, Tennessee. Services offered include an accredited chest pain center, a stroke center, and a comprehensive total joint program for orthopedics. In addition, Vanderbilt Ingram Cancer Center extended services to this campus in 2020, and it includes a state-of-the-art linear accelerator.
- VBCH is a 60-bed, Joint Commission-accredited hospital, which offers a range of inpatient and outpatient medical and surgical services, along with urgent care services.
- VTHH is a 135-bed Joint Commission-accredited hospital, which offers a full range of inpatient and outpatient surgical and specialty services including a sleep center, cardiac rehabilitation, and physical rehabilitation. The hospital features an accredited Chest Pain Center.
- VMG is the practice group of physicians and advanced practice nurses employed by VUMC, most of whom have faculty appointments from the University, who perform billable professional medical services. VMG is not a separate legal entity. VMG has a board which consists of the VUMC clinical service chiefs, who also serve as clinical department chairs. Under the oversight of VUMC executive leadership, VMG sets professional practice standards, bylaws, policies, and procedures. VUMC bills for services rendered by VMG clinicians in both inpatient and outpatient locations. VMG includes nationally recognized physicians whose expertise spans the spectrum from primary care to the most specialized quaternary discipline. The entire clinical faculty is “board certified” or eligible for board certification. All staff members are re-credentialed every two years by the National Committee for Quality Assurance standards. All specialties and subspecialties currently recognized by the various national specialty boards are represented on the clinical faculty.
- VHS serves as a holding company for 16 first-tier health care related subsidiaries and joint ventures owned with various entities, including, but not limited to, VSRH and the Vanderbilt Health Affiliated Network (“VHAN”). VHS operations primarily consist of community physician practices, walk-in and retail health clinics, imaging services, outpatient surgery centers, radiation oncology centers, a home health care agency, a home infusion and respiratory service, an affiliated health network, accountable care organizations, and a rehabilitation hospital. These subsidiaries include clinics managed in multiple outpatient locations throughout middle Tennessee and southwestern Kentucky.
- Health Professional Solutions, LLC (“HPS”) is a holding company that holds interest in five VUMC subsidiaries that engage in or support various health care activities in order to improve the quality and availability of health care services in the community. These subsidiaries include businesses focused on pharmacy, supply chain, and clinically integrated support services.
- Nashville Biosciences, LLC (“NashBio”) operates exclusively in support of VUMC’s non-academic medical research activities. NashBio deploys the biospecimens and genomic data and de-identified medical records of VUMC known as “BioVU”, along with other information, to provide commercial services and products to life science industry customers in connection with pharmaceutical, biotechnology, and medical research and development activities.

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The Academic Enterprise division includes all clinically related research, research-support activities, and faculty endeavors supporting post-graduate training programs. A significant funding source for VUMC's research is the federal government. Federal funding is received from the Department of Health and Human Services, the Department of Defense, the National Science Foundation, and other federal agencies. Sponsored research awards, including multiple year grants and contracts from government sources, foundations, associations, and corporations signify future research commitments. Also, core activities supporting research, including advanced computing and grant administration, are included in this division.

The terms "Company," "VUMC," "we," "our", or "us" as used herein and unless otherwise stated or indicated by context refer to Vanderbilt University Medical Center and its affiliates. The terms "facilities" or "hospitals" refer to entities owned and operated by VUMC and its affiliates, and the term "employees" refers to employees of VUMC and its affiliates.

VUMC operates on a fiscal year which ends on June 30. The term "Fiscal" preceding a year refers to a particular VUMC fiscal year.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared on the accrual basis in accordance with accounting principles generally accepted in the U.S. ("GAAP"). Based on the existence or absence of donor-imposed restrictions, VUMC classifies resources into two categories: net assets without donor restrictions and net assets with donor restrictions.

Principles of Consolidation

The consolidated financial statements include the accounts of VUMC and its wholly owned, majority-owned, and controlled organizations. Noncontrolling interests in less-than-wholly owned consolidated subsidiaries of VUMC are presented as a component of net assets to distinguish between the interests of VUMC and the interests of the noncontrolling owners. All material intercompany transactions and account balances among the various entities have been eliminated.

VUMC uses the equity method to account for its interests in unconsolidated partnerships, joint ventures, and limited liability entities over which it exercises significant influence. Investment carrying amounts are adjusted for VUMC's share of investee earnings or losses based on percentage of ownership. Distributions received from unconsolidated entities that represent returns on VUMC's investment (i.e., dividends) are reported as cash flows from operating activities in VUMC's statement of cash flows.

Use of Estimates

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

Cash and Cash Equivalents

Cash and cash equivalents are liquid assets with minimal interest rate risk and maturities of three months or less when purchased. VUMC invests operating assets in a diversified manner. At times, VUMC may have cash and cash equivalents at a financial institution in excess of federally insured limits, and therefore, bears a risk of loss.

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Liquidity and Availability

As of June 30, 2021, VUMC has \$2,386.1 million of financial assets available within one year of the balance sheet date to meet cash needs for general expenditures consisting of cash and cash equivalents of \$837.3 million, patient accounts receivable of \$553.9 million, and unrestricted investments of \$994.9 million. As of June 30, 2020, VUMC had \$2,412.5 million of financial assets available within one year of the balance sheet date to meet cash needs for general expenditures consisting of cash and cash equivalents of \$1,170.5 million, patient accounts receivable of \$470.6 million, and unrestricted investments of \$771.4 million. None of these financial assets are subject to donor or other contractual restrictions that make them unavailable for general expenditure within one year of the balance sheet date.

VUMC has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, as part of its liquidity management, VUMC invests cash in excess of daily requirements in various short-term investments, including certificates of deposit and short-term treasury instruments.

As more fully described in Note 11 Long-Term Debt, VUMC also has committed lines of credit in the amount of \$200.0 million, which it could draw upon in the event of an unanticipated liquidity need, with \$100.0 million drawn as of June 30, 2021 and 2020.

Revenue Recognition – Patient Services

VUMC recognizes revenue from patient services at the amount that reflects the consideration to which VUMC expects to be paid for providing such services. These amounts, representing transaction price, are due from patients, third-party payors (including health insurers and government programs), and others and include variable consideration for retroactive revenue adjustments due to settlements of audits, reviews, and investigations. Patient service revenue is recognized as performance obligations based on the nature of the services provided by VUMC are satisfied.

Performance obligations satisfied over time relate to admitted patients in VUMC hospitals receiving inpatient acute care services from admission to the point when services are no longer required, which is generally at the time of discharge. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected or actual charges. Outpatient services are performance obligations satisfied at a point in time with the related revenue being recognized when goods or services are provided.

VUMC has elected to apply the optional exemption provided in FASB (ASC) 606-10-50-14 as substantially all of its performance obligations relate to contracts with a duration of less than one year. Therefore, VUMC is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially satisfied at the end of the reporting period. Unsatisfied or partially satisfied performance obligations are primarily related to in-house patients at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which is typically within a week.

VUMC uses a portfolio approach consisting of major payor classes to account for categories of patient contracts as a collective group rather than recognizing revenue on an individual contract basis. Based on historical collection trends and other analysis, VUMC believes that revenue recognized by utilizing the portfolio approach approximates the revenue that would have been recognized if an individual contract approach were used.

VUMC determines the transaction price, which involves estimates and judgment, based on standard charges for goods and services provided, reduced by explicit and implicit price concessions, including contractual adjustments provided to third-party payors, discounts provided

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to uninsured and underinsured patients in accordance with VUMC policy, and historical collection experience. VUMC analyzes its history and identifies trends for each of its major revenue categories to estimate the appropriate price concessions. Management regularly reviews data for these major revenue categories in evaluating the reasonableness of the transaction price, taking into consideration recent experience by payor category, payor agreement rate changes, and other factors.

In addition to patient payments, VUMC earns revenue and reimbursements from certain services provided under federal healthcare programs and other contracts with third-party payors. These compensation arrangements are complex programs which extend over multiple accounting periods and are subject to the interpretation of federal and state-specific reimbursement rates, new or changing legislation, and final cost report settlements. Estimated settlements under these programs are recorded in the period the related services are performed and are subsequently adjusted, as needed, based on new information.

VUMC provides care to patients who meet the criteria for charity care under its financial assistance policy for no payment or at payment amounts less than its established charge rates. VUMC does not recognize the charges that qualify as charity care as revenue because VUMC does not pursue collection of these amounts.

Revenue Recognition – Non-Patient Services

Revenue for non-patient services is recognized at an amount that reflects the consideration VUMC expects to be entitled in exchange for providing goods or services. The amounts recognized reflect considerations due from customers, the U.S. government, and others, and is recognized as performance obligations are satisfied. Primary categories of non-patient revenue include academic and research revenue as well as other miscellaneous activities as further described in Note 8 Other Relevant Financial Information.

VUMC receives funding through grants and contracts issued by departments and agencies of the U.S. government, industry, and other foundation sponsors who restrict the use of such funds to academic and research purposes. VUMC recognizes revenue from these grants and contracts in accordance with contract terms, as defined in the agreements governing that funding. VUMC recognizes facilities and administrative ("F&A") costs recovery as revenue when the allowable expenditure is incurred on the associated grant or contract. This activity represents reimbursement, primarily from the federal government, of F&A costs on sponsored activities.

Grants and contracts receivable include amounts due from these sponsors of externally funded research. These amounts have been billed or are billable to the sponsor and are recorded at the amount that reflects the consideration VUMC expects to receive.

Deferred Revenue

Deferred revenue is recorded for funds received in advance. The related revenue is recognized when the performance obligations have been met.

Gift Income and Pledges

VUMC recognizes unconditional promises to give cash and other assets, referred to as pledges, as gift income at fair value when the pledge is received. Conditional promises to give are recognized as pledges once the conditions are substantially met. Pledges are recognized as net assets with donor restrictions. Gifts received with donor stipulations limiting the use of the donated assets are reported as net assets with donor restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as gift income in the consolidated statements of operations. Gift income is recognized when a donor restriction expires, that is, when a stipulated

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time restriction ends or purpose restriction is accomplished. Gifts of cash or other assets that must be used to acquire long-lived assets are reported as net assets with donor restrictions until the assets are placed in service, at which point they are reclassified to net assets without donor restrictions.

Pledges receivable are reported net of allowances for uncollectible amounts based on an analysis of past collection experience and other judgmental factors. Pledges receivable are included in other current or other noncurrent assets in the consolidated balance sheets based on the expected timing of cash flows. VUMC discounts the noncurrent portion of pledges receivables at a rate commensurate with the scheduled timing of receipt. VUMC applied annual discount rates ranging from 0.5% to 1.5% to amounts outstanding as of June 30, 2021 and 2020.

Concentrations of Credit Risk

VUMC grants unsecured credit to its patients, primarily residing in Nashville, Tennessee and the surrounding areas of middle Tennessee, most of whom are insured under commercial, Medicare (both traditional fee-for-service and Managed Medicare), or TennCare agreements. Medicare, Blue Cross Blue Shield ("BCBS"), and TennCare (which includes BCBS of Tennessee, United, and Amerigroup) represent VUMC's significant concentrations of credit risk from payors.

Inventories

VUMC reports inventories at the lower of cost or market, with cost being determined on the first-in, first-out method. Inventories consist primarily of medical supplies, surgical implants, and pharmaceuticals.

Restricted Cash

VUMC reports cash whose use is restricted at cost, which approximates fair value. The cash is primarily restricted for use in purchasing and constructing property, plant, and equipment.

Investments

VUMC reports investments held at fair value in the consolidated balance sheets. Private equity investments are reported using the equity method of accounting based on net asset value (NAV) provided by the respective fund manager. VUMC records purchases and sales of securities on the trade dates, and realized gains and losses are determined based on the average historical cost of the securities sold. VUMC reports net receivables and payables arising from unsettled trades as a component of investments.

Property, Plant, and Equipment, Net

VUMC records purchases of property, plant, and equipment at cost and expenses repairs and maintenance costs as incurred. VUMC capitalizes interest cost incurred on borrowed funds during the period of construction of capital assets as a component of the cost of acquiring those assets. VUMC capitalizes donated assets at fair value on the date of donation.

Capitalized software for internal use is recorded during the application development stage. These costs include fees paid to third parties for direct costs of materials and services consumed in developing or obtaining the software; payroll related costs and capitalized interest costs. Costs for training and application maintenance in the post-implementation operation stage are expensed as incurred.

VUMC computes depreciation using the straight-line method over the estimated useful life of land improvements (5 to 18 years), buildings and leasehold improvements (2 to 40 years), and equipment (2 to 20 years). Equipment costs also include capitalized internal use software costs, which are expensed over the expected useful life, which is generally 3 to 12 years.

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Software for internal use is amortized on a straight-line basis over its estimated useful life. In determining the estimated useful life, management considers the effects of obsolescence, technology, competition, other economic factors, and rapid changes that may be occurring in the development of software products, operating systems, and computer hardware. Amortization begins once the software is ready for its intended use.

Impairment of Long-Lived Assets

VUMC reviews long-lived assets, such as property, plant, and equipment, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. VUMC measures the recoverability of assets to be held and used by comparing the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, VUMC recognizes an impairment charge to the extent the carrying amount of the asset exceeds its fair value.

Conditional Asset Retirement Costs and Obligations

VUMC recognizes the estimated fair value of liabilities for existing legal obligations to perform certain activities, primarily asbestos removal, in connection with the retirement, disposal, or abandonment of assets. These liabilities are included in other noncurrent liabilities on the consolidated balance sheets and total \$6.7 million and \$6.5 million as of June 30, 2021 and 2020, respectively. VUMC measures these liabilities using estimated cash flows with an inflation rate applied of 3.0% as of June 30, 2021 and 2020. VUMC discounts those cash flow estimates at a credit-adjusted, risk-free rate, which ranged from 2.9% to 4.2% as of June 30, 2021 and 2020, and adjusts these liabilities for accretion costs and revisions in estimated cash flows.

Long-Term Debt

The carrying value of VUMC's debt is the par amount adjusted for the net unamortized amount of debt issuance costs, bond premiums and discounts.

Interest Rate Exchange Agreements

VUMC reports interest rate exchange agreements at fair value, which is determined to be the present value of future net cash settlements that reflect market yields as of the measurement date and estimated amounts that VUMC would pay, or receive, to terminate the contracts as of the report date. VUMC considers current interest rates and creditworthiness of the interest rate exchange counterparties when estimating termination settlements.

Self-Insurance Reserves

VUMC elects to self-insure a portion of its medical malpractice, professional, and general liability coverage via an irrevocable self-insurance trust. For Fiscal 2021 and 2020, the maximum annual self-insurance retention was \$6.0 million per occurrence, up to \$46.0 million in the aggregate. Actuarial firms assist management in estimating expected losses on an annual basis, at which time VUMC records medical malpractice, professional, and general liability expense within the limits of the program. These liabilities are classified as current or noncurrent based on the expected timing of cash flows and are measured at the net present value of those cash flows using a discount rate of 2.5% as of June 30, 2021 and 2020. For both Fiscal 2021 and 2020, VUMC obtained excess medical malpractice, professional, and general liability coverage from commercial insurance carriers for claims exceeding the retention limits, up to \$175.0 million. These policies would also provide coverage up to \$175.0 million if any claims in the aggregate exceeded the retention limits.

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VUMC also elects to self-insure for employee health and workers' compensation expenses. Actuarial firms assist management in estimating expected losses on an annual basis. The maximum retention for workers' compensation was \$0.8 million per occurrence for both Fiscal 2021 and 2020. There is no stop loss insurance on health plan claims.

Income Taxes

VUMC is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code (the "Code") and is generally exempt from federal income taxes under Section 501(a) of the Code.

Excess of Revenues Over Expenses

The consolidated statements of operations include excess of revenues over expenses as a performance indicator. Excess of revenues over expenses includes all changes in net assets without donor restrictions, except for changes in noncontrolling interest holders' share of consolidated entities, net assets released from restrictions used for capital, and certain other items.

Statement of Cash Flows

For VUMC's consolidated statements of cash flows, cash, cash equivalents, and restricted cash is defined as those amounts included in the cash and cash equivalents caption and restricted cash caption on the consolidated balance sheets.

Recent Accounting Pronouncements

Periodically, the FASB issues Accounting Standards Updates ("ASUs") that may impact the recognition, measurement, and presentation of balances and activity in VUMC's consolidated financial statements or the disclosures contained within those statements. As part of preparing consolidated financial statements, VUMC evaluates the effects of the ASUs and applies the updated guidance within the required effective dates.

Adopted

- Effective July 1, 2020, VUMC adopted FASB ASU 2018-13, Fair Value Measurement. This ASU improves the effectiveness of the notes to the financial statements through changes in the disclosure requirements for fair value measurement. The adoption of this ASU did not materially impact the consolidated financial statements.

Not Yet Adopted

- In August 2018, the FASB issued ASU 2018-15, Intangibles – Goodwill and Other, Internal-Use Software (Subtopic 350-40), Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract. The primary effect of adopting this ASU will be capitalization of implementation costs incurred in hosting arrangements that are service contracts and subsequent amortization expenses in the consolidated statements of operations. The ASU is effective for fiscal years beginning after December 15, 2020 and will be applied using a prospective approach. VUMC is currently assessing the impact of this ASU on the consolidated financial statements.
- In September 2020, the FASB issued ASU 2020-07, Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets (Topic 958). This ASU requires presentation of nonfinancial assets as a separate line in the consolidated statement of operations, apart from contributions of cash or other financial assets. The ASU is effective for fiscal years beginning after June 15, 2021 and will be applied on a retrospective basis. VUMC is currently assessing the impact of this ASU on the consolidated financial statements.

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3. Related Parties

On April 29, 2016, VUMC acquired the assets, liabilities, rights, and obligations of the clinical enterprise, postgraduate medical training programs, and clinically related research of the University's owned and operated Medical Center, "the Acquisition".

The assets acquired and liabilities assumed from the Acquisition were detailed in a Master Transfer and Separation Agreement ("MTSA"). The MTSA contains the framework for the ongoing economic relationship between VUMC and the University. The relationship is memorialized in the form of an Academic Affiliation Agreement ("AAA"), a Trademark License Agreement ("TMLA"), a Ground Lease, and a Reciprocal Master Services Agreement ("MSA"). The agreements are described below.

- The AAA outlines the ongoing academic, research, and clinical affiliation between the University and VUMC for all the University's degree-granting, certificate, and research programs. The AAA allocates responsibility between the University and VUMC for jointly administered research and academic programs and is an exclusive agreement between VUMC and VU requiring VUMC to be organized, governed, and operated in a manner that supports VU's academic and research mission. The agreement provides that VU will be the exclusive academic affiliate of VUMC, and VUMC will be the exclusive clinical affiliate of VU.

The AAA requires VUMC to pay VU an annual fee in equal monthly payments adjusted annually for inflation based upon the Biomedical Research and Development Price Index ("BRDPI") in perpetuity under certain mutually agreed-upon termination or default clauses. During Fiscal 2021 and 2020, VUMC recorded operating expense totaling \$78.5 million and \$76.9 million, respectively, in connection with fees due under the AAA.

- Under the TMLA, VU grants, subject to certain consents and approvals, a perpetual license to use various VU-owned licensed marks in connection with VUMC's fundamental activities after the Acquisition date. The licensed marks, which VUMC continues to use as its primary brands, include virtually all those previously in use by VUMC. This agreement requires VUMC to pay VU royalties consisting of a monthly payment equal to 1.0% of all operating revenue of VUMC and 15% of income from operations. During Fiscal 2021 and 2020, VUMC recorded operating expense totaling \$83.7 million and \$70.4 million, respectively, in connection with the 1.0% of operating revenue and percentage of operating income payments due under the TMLA. Also, VUMC is required to pay in equal monthly installments an annual TMLA base fee royalty, which increases 3% annually, but is also reduced by the amount of principal payments made under a subordinate note discussed in Note 11 Long-Term Debt (the "Fixed TMLA Royalty Payment"). During Fiscal 2021 and 2020, VUMC recorded operating expense totaling \$64.6 million and \$62.5 million, respectively, in connection with this base fee royalty. In Fiscal 2018, VU sold its rights to future base fee royalty payments to a third party. In Fiscal 2019, VU sold its rights to future 1.0% of operating revenue payments to a third party. The TMLA is in force in perpetuity under certain mutually agreed-upon termination or default clauses.
- The Ground Lease is an agreement between VU and VUMC that allows VUMC to use the land on which VUMC's campus and related buildings are located. The initial term of the Ground Lease ends June 30, 2114, with the option to extend the lease for two additional terms of up to 50 to 99 years each with agreement between VU and VUMC. The lease covers 1.7 million square feet or 38.75 acres of space, payable monthly and CPI adjusted annually. During Fiscal 2021 and 2020, VUMC recorded operating expense totaling \$19.6 million and \$19.4 million, respectively, in connection with fees due under the Ground Lease.

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- The University and VUMC provide services to one another for agreed-upon consideration as outlined in the MSA. VU provides services to VUMC, such as information technology infrastructure support, utilities, and law enforcement staffing. VUMC provides various operational services for the University, such as a student health clinic and animal care. Additionally, the MSA encompasses an Employee Matters Agreement (“EMA”) and specific Employee Service Agreements (“ESAs”). The EMA and ESAs govern employee transactions and ongoing sharing between VU and VUMC in various capacities, such as research, teaching, clinical, and other administrative services. Services under the MSA can be terminated by either party subject to predetermined cancellation notification periods. In connection with the MSA, during Fiscal 2021 and 2020, VUMC recognized revenue totaling \$43.4 million and \$44.2 million, respectively, and recorded operating expense totaling \$119.5 million and \$123.4 million, respectively.
- Also, as part of the Acquisition, VUMC issued to VU a \$100.0 million subordinate promissory note payable, which is further described in Note 11 Long-Term Debt, with a balance of \$74.6 million as of June 30, 2021, and \$79.6 million as of June 30, 2020. VU sold its rights to future principal and interest payments on this note to a third party.

The impact of these agreements in the consolidated statements of operations during Fiscal 2021 and 2020 is as follows:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|-------------------------------|-------------------|-------------------|
| Academic and research revenue | \$ 15,816 | \$ 13,055 |
| Other operating revenue | 27,565 | 31,192 |
| Total operating revenues | <u>\$ 43,381</u> | <u>\$ 44,247</u> |
| Operating expenses | | |
| Salaries, wages, and benefits | \$ 8,223 | \$ 9,086 |
| Facilities and equipment | 56,910 | 59,516 |
| Services and other | 300,656 | 284,040 |
| Interest | 2,498 | 2,661 |
| Total operating expenses | <u>\$ 368,287</u> | <u>\$ 355,303</u> |

Other current assets include amounts receivable from VU, which totaled \$8.0 million as of June 30, 2021, and \$6.7 million as of June 30, 2020. Accounts payable and other accrued expenses include amounts payable to related parties, which totaled \$58.5 million as of June 30, 2021, and \$51.1 million as of June 30, 2020.

In the normal course of business, members of VUMC’s Board of Directors or VUMC employees may be directly or indirectly associated with companies engaged in business activities with VUMC. VUMC has a written conflict of interest policy that requires, among other things, that members of the VUMC community (including trustees) may not review, approve, or administratively control contracts or business relationships when (i) the contract or business relationship is between VUMC and a business in which the individual or a family member has a material financial interest, or (ii) the individual or a family member is an employee of the business and is directly involved with activities pertaining to VUMC.

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Furthermore, VUMC's conflict of interest policy extends beyond the foregoing business activities in that disclosure is required for any situation in which an applicable individual's financial, professional, or other personal activities may directly or indirectly affect, or have the appearance of affecting, an individual's professional judgment in exercising any VUMC duty or responsibility, including the conduct or reporting of research.

The policy extends to all individual members of the VUMC community (including Board of Directors, VUMC officials, full-time, part-time, temporary faculty and staff). Each applicable person is required to certify compliance with the conflict of interest policy on an annual basis. This certification includes specifically disclosing whether VUMC conducts business with an entity in which he or she (or an immediate family member) has a material financial interest, as well as any other situation that could appear to present a conflict with VUMC's best interests.

When situations exist relative to the conflict of interest policy, VUMC takes active measures to appropriately manage the actual or perceived conflict in the best interests of VUMC, including periodic reporting of measures taken to the Audit and Compliance Committee of the Board of Directors.

4. Patient Service Revenue, Patient Accounts Receivable, and Estimated Third-Party Settlements

Management has determined that the nature, amount, timing, and uncertainty of revenue and cash flows are affected by the major classes of payors. The sources of patient service revenue by payor for Fiscal 2021 and 2020 are as follows:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|---------------------|---------------------|
| Other third-party payors, primarily commercial carriers | \$ 2,961,480 | \$ 2,553,307 |
| Medicare/Managed Medicare | 1,084,216 | 924,241 |
| TennCare/Medicaid | 608,791 | 522,606 |
| Uninsured (self-pay) | 37,327 | 31,566 |
| | <u>\$ 4,691,814</u> | <u>\$ 4,031,720</u> |

Patient accounts receivable comprise amounts due from the following sources as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|-------------------|-------------------|
| Medicare | \$ 95,382 | \$ 77,696 |
| TennCare/Medicaid | 70,487 | 57,741 |
| Blue Cross | 115,028 | 99,861 |
| Other third-party payors, primarily commercial carriers | 219,643 | 192,258 |
| Patient responsibility ⁽¹⁾ | 53,334 | 42,994 |
| Patient accounts receivable | <u>\$ 553,874</u> | <u>\$ 470,550</u> |

⁽¹⁾ Includes self-pay after insurance.

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Estimated third-party settlements by major payor category as of June 30, 2021 and 2020, are as follows:

| <i>(\$ in thousands)</i> | <u>2021</u> | <u>2020</u> |
|--|------------------|------------------|
| Receivables under third-party programs | | |
| Tricare/Champus ⁽¹⁾ | \$ 4,635 | \$ 4,484 |
| Total receivables under third-party programs | <u>\$ 4,635</u> | <u>\$ 4,484</u> |
| Payables under third-party programs | | |
| TennCare/Medicaid | \$ 33,781 | \$ 37,781 |
| Medicare ⁽¹⁾ | 8,170 | 9,752 |
| Other | 353 | 2,908 |
| Total payables under third-party programs | <u>\$ 42,304</u> | <u>\$ 50,441</u> |

⁽¹⁾ These two federal healthcare programs are combined for presentation purposes on the face of the consolidated balance sheets and are reflected as an obligation in Fiscal 2021 and Fiscal 2020.

Certain contracts require pay for performance or episode of care settlements whereby VUMC receives additional payment or pays a penalty based on its ability to achieve certain clinical measures or manage the cost of care for patients within various thresholds. VUMC estimates and accrues these adjustments in the period the related services are rendered and adjusts these estimates in future periods as settlements are finalized. The aggregate liability associated with pay for performance and episode of care settlements at June 30, 2021 and 2020, was \$1.1 million and \$2.5 million, respectively, with the ultimate resolution of such financial arrangements not expected to have a material impact on the operating results of VUMC.

Medicare

Amounts received under Medicare are subject to review and final determination by program intermediaries or their agents. Final settlements have been reached for program periods ended June 30, 2015. Final settlements have not been reached for subsequent years due to audit delays experienced with the Medicare Administrative Contractor, and thus, those periods remain subject to audit by program representatives.

TennCare

TennCare is a Medicaid managed care program implemented by the state of Tennessee to provide healthcare coverage to those patients eligible for Medicaid through the Federal 1115 Waiver Program. VUMC contracts with each of the three TennCare managed care organizations ("MCOs"), which offer health maintenance organization ("HMO") and Medicare Special Needs Products for Dual Eligible Enrollees. VUMC receives inpatient reimbursement through payments that are primarily based on the Medicare severity diagnostic related group system ("MS-DRG") for these plans. VUMC receives outpatient payments generally based on an ambulatory payment classification system ("APC"), and/or a payor-developed fee schedule.

In accordance with the Tennessee Hospital Assessment Act, VUMC receives a payment of a portion of its unreimbursed TennCare costs based upon VUMC's share of uninsured TennCare costs for all of the covered hospitals.

There is no assurance that this program will be continued in its current structure or will not be materially modified in the future, however, we anticipate funding will remain relatively stable over the coming year.

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In Fiscal 2021 and 2020, patient service revenue includes the following supplemental amounts received in each respective period from TennCare.

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|------------------|------------------|
| Charity pool | \$ 26,659 | \$ 24,696 |
| Graduate medical education | 14,618 | 14,592 |
| Trauma fund | 1,560 | 1,685 |
| Virtual disproportionate share | 6,400 | 960 |
| Changes in prior year virtual disproportionate share reserve estimate | 20,411 | - |
| Total supplemental TennCare revenue, net of audit provision | <u>\$ 69,648</u> | <u>\$ 41,933</u> |

5. Charity Care Assistance, Community Benefits, and Other Unrecovered Costs

VUMC maintains a policy which sets forth the criteria under which health care services are provided to patients who have minimal financial resources to pay for medical care. Additionally, VUMC provides other services that benefit the economically disadvantaged for which little or no payment is expected.

Charity care is determined by examining patient and family income relative to the federal poverty guidelines. VUMC provides additional discounts based on the income level of the patient household using a sliding scale for those patients with a major catastrophic medical event not qualifying for full charity assistance. Tennessee law mandates that all uninsured patients receive a discount from billed charges for medically necessary services. These amounts are classified as charity care if the patient meets charity care criteria, for which no revenue is recorded, or is included as a part of price concessions.

VUMC maintains records to identify and monitor the level of charity care provided, and these records include gross charges and patient deductibles, coinsurance and copayments foregone for services furnished under its charity care policy, and the estimated cost of those services. VUMC calculates a ratio of total costs to gross charges and then multiplies the ratio by foregone charity care charges in determining the estimated cost of charity care. The gross amount of foregone charity care revenue in Fiscal 2021 and 2020 totals \$474.1 million and \$422.7 million, respectively. The estimated cost of providing care to charity patients in Fiscal 2021 and 2020 totals \$123.6 million and \$110.1 million, respectively.

In addition to the charity care services described above, TennCare/Medicaid and state indigent programs do not cover the full cost of providing care to beneficiaries of those programs. As a result, in addition to direct charity care costs, VUMC provided services related to TennCare/Medicaid and state indigent programs and was reimbursed substantially below the cost of rendering such services. VUMC also provides public health education and training for new health professionals and provides, without charge, services to the community at large for many patients with special needs.

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6. Academic and Research Revenue, and Grants and Contracts Receivable

Academic and research revenue comprises the following for Fiscal 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|-------------------|-------------------|
| Grants and contracts revenue | | |
| Federally funded | \$ 345,745 | \$ 297,651 |
| Non-federally funded | 124,690 | 132,557 |
| | 470,435 | 430,208 |
| Facilities and administrative costs recovery | 144,176 | 122,614 |
| Academic and research revenue | <u>\$ 614,611</u> | <u>\$ 552,822</u> |

Grants and contracts receivable comprise the following as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---------------------------------------|------------------|------------------|
| Federally funded | \$ 38,472 | \$ 28,077 |
| Non-federally funded | 38,893 | 31,954 |
| Total grants and contracts receivable | <u>\$ 77,365</u> | <u>\$ 60,031</u> |

7. Pledges Receivable, Net

Pledges receivable, net of applied discounts and allowance for uncollectible pledges, as of June 30, 2021 and 2020, were as follows:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--------------------------------------|------------------|------------------|
| Amounts due | | |
| Within one year | \$ 10,660 | \$ 11,347 |
| In one to five years | 26,257 | 24,809 |
| Total pledges receivable | 36,917 | 36,156 |
| Unamortized discount | (1,225) | (1,112) |
| | 35,692 | 35,044 |
| Allowance for uncollectible pledges | (4,806) | (6,126) |
| Net pledges receivable | <u>\$ 30,886</u> | <u>\$ 28,918</u> |
| Net pledges receivable classified as | | |
| Current | \$ 6,615 | \$ 7,552 |
| Noncurrent | 24,271 | 21,366 |
| | <u>\$ 30,886</u> | <u>\$ 28,918</u> |

In addition to pledges reported as pledges receivable, VUMC had cumulative bequest intentions and conditional promises to give totaling \$79.5 million as of June 30, 2021, and \$66.9 million as of June 30, 2020. Due to their conditional nature, VUMC does not recognize intentions to give as assets.

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8. Other Relevant Financial Information

Other current assets comprise the following as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|-------------------|-------------------|
| Prepaid expenses | \$ 44,552 | \$ 42,115 |
| Other receivables | 55,295 | 59,436 |
| Amounts due from VU (see Note 3 Related Parties) | 7,977 | 6,684 |
| Current pledges receivable, net (see Note 7 Pledges Receivable, Net) | 6,615 | 7,552 |
| Expected recoveries from commercial insurance excess coverage | 3,820 | 2,652 |
| Total other current assets | <u>\$ 118,259</u> | <u>\$ 118,439</u> |

Other noncurrent assets comprise the following as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|------------------|------------------|
| Equity in unconsolidated organizations | \$ 63,109 | \$ 23,234 |
| Noncurrent pledges receivable (see Note 7 Pledges Receivable, Net) | 24,271 | 21,366 |
| Other | 8,971 | 8,747 |
| Total other noncurrent assets | <u>\$ 96,351</u> | <u>\$ 53,347</u> |

Other operating revenues comprise the following for Fiscal 2021 and 2020

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|-------------------|-------------------|
| CARES funding | \$ 63,045 | \$ 130,399 |
| Clinical contracts | 49,701 | 46,886 |
| Amounts recognized under MSA with VU (see Note 3 Related Parties) | 27,565 | 31,192 |
| VHS other revenue | 21,556 | 28,176 |
| Nonclinical contracts | 16,846 | 11,898 |
| Resident and house staff rotations | 10,151 | 10,557 |
| Other | 39,340 | 42,035 |
| Total other operating revenue | <u>\$ 228,204</u> | <u>\$ 301,143</u> |

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9. Investments

VUMC investments are made up of current investments, restricted cash, noncurrent investments, and noncurrent investments limited as to use on the face of the consolidated balance sheets. VUMC investments include assets limited as to use related to the following specified purposes as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | <u>2021</u> | <u>2020</u> |
|---|-------------------|-------------------|
| Self-insured malpractice program | \$ 46,991 | \$ 46,223 |
| Donor endowments | 65,083 | 52,590 |
| Split-interest trusts | 9,503 | 7,124 |
| Supplemental employee retirement program assets | 5,837 | 7,589 |
| | <u>\$ 127,414</u> | <u>\$ 113,526</u> |

VUMC's endowment does not include gift annuities, interests in trusts held by others, contributions pending donor designation, or contributions receivable.

The Board of Directors' interpretation of its fiduciary responsibilities for donor-restricted endowments under the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") requirements is to preserve intergenerational equity, barring the existence of any donor-specific provisions. Under this broad guideline, future endowment beneficiaries should receive at least the same level of real economic support as the current generation. The overarching objective is to preserve and enhance the real (inflation-adjusted) purchasing power of the endowment in perpetuity. VUMC invests assets to provide a relatively predictable and stable stream of earnings to meet spending needs and attain long-term return objectives without the assumption of undue risks.

Self-insured malpractice program – VUMC elects to self-insure a portion of its medical malpractice, professional, and general liability via an irrevocable self-insurance trust.

Donor endowments – Donor-restricted gifts where the principal amount is to be held in perpetuity. Distributions of earnings are restricted for use according to the donor's intent, as specified in a gift agreement. Donor endowments typically benefit specific programs in clinical departments of the Medical Center, for either, research, directorships, or general program support.

Split-interest trusts – Trusts established by donors where VUMC is named as beneficiary. Depending on the terms of the trust, VUMC may receive periodic distributions, and potentially a principal amount at some point in the future. Like donor endowments, split-interest trusts typically benefit specific programs as defined in the terms of the trust.

Supplemental executive retirement program assets – Assets set aside to fulfill obligations as they come due according to the terms of the retirement program.

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Investments were as follows as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|---------------------|-------------------|
| Corporate bonds | \$ 336,905 | \$ 235,249 |
| Equity mutual funds | 151,200 | 128,569 |
| Cash and cash equivalents | 27,681 | 13,147 |
| Split-interest trusts | 9,503 | 7,124 |
| Hedged equity mutual funds | 107,548 | 64,986 |
| Fixed income mutual funds | 217,762 | 190,054 |
| Certificates of deposit | 21,162 | 16,338 |
| Asset-backed securities | 28,971 | 26,448 |
| Mortgage-backed securities | 6,503 | - |
| Real estate mutual funds | - | 20,680 |
| Commercial paper | 37,040 | 22,218 |
| Government bonds | 53,133 | 80,145 |
| Hedged debt mutual funds | 114,474 | 70,958 |
| Commodities and managed futures mutual funds | 19,802 | 15,902 |
| Target date mutual funds | 5,168 | 4,865 |
| Total investments reported at fair value | \$ 1,136,852 | \$ 896,683 |
| Private equity investments recorded at net asset value | 12,839 | - |
| Total investments | <u>\$ 1,149,691</u> | <u>\$ 896,683</u> |

Investment returns comprise the following elements for Fiscal 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|------------------|------------------|
| Interest and dividend income | \$ 14,910 | \$ 20,740 |
| Net realized gains on sales of securities | 14,922 | 5,025 |
| Realized investment gains | 29,832 | 25,765 |
| Unrealized investment gains (losses), net | 49,995 | 3,637 |
| Total investment returns | 79,827 | 29,402 |
| Investment manager, trustee and other fees | (457) | (451) |
| Restricted investment income | (11,169) | (1,727) |
| Total income from investments, net | <u>\$ 68,201</u> | <u>\$ 27,224</u> |

VUMC has exposure to risks, including liquidity, interest rate, counterparty, basis, regulatory, market, and credit risks, for marketable securities. Due to the level of risk exposure, it is possible that material near-term valuation changes for investment securities may occur.

VUMC manages all investments, including endowments, in various investment pools.

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10. Property, Plant, and Equipment, Net

Property, plant, and equipment comprise the following as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|---------------------|---------------------|
| Land and land improvements | \$ 40,800 | \$ 40,800 |
| Buildings and improvements | 1,249,125 | 1,189,614 |
| Equipment and software | 683,108 | 562,360 |
| Leasehold improvements | 141,358 | 86,869 |
| Construction in progress | 94,027 | 77,739 |
| Property, plant, and equipment at cost | 2,208,418 | 1,957,382 |
| Accumulated depreciation and amortization | (578,093) | (432,279) |
| Property, plant, and equipment, net | <u>\$ 1,630,325</u> | <u>\$ 1,525,103</u> |

As part of the MTSA, VUMC acquired land and land improvements and buildings and improvements which are not allowed to be repurposed without the express consent of VU.

In Fiscal 2021 and 2020, VUMC capitalized interest of \$2.3 million and \$2.9 million, respectively, related to long-term capital projects, primarily the MCJCHV expansion and the VUH bed expansion.

Property, plant, and equipment balances above include the following amounts related to capitalized internal use software:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---------------------------------------|-------------------|-------------------|
| Equipment and software | \$ 188,334 | \$ 167,897 |
| Construction in progress | 7,095 | 11,063 |
| | 195,429 | 178,960 |
| Accumulated amortization | (58,662) | (40,823) |
| Internal use software, carrying value | <u>\$ 136,767</u> | <u>\$ 138,137</u> |

Depreciation and amortization comprise the following amounts in Fiscal 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|-------------------|-------------------|
| Depreciation of tangible assets | \$ 117,183 | \$ 97,976 |
| Amortization of finance leases, leasehold improvements, and internal use software | 34,271 | 28,678 |
| Total depreciation and amortization | <u>\$ 151,454</u> | <u>\$ 126,654</u> |

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11. Long-Term Debt

Long-term debt comprises the following as of June 30, 2021 and 2020:

| (\$ in thousands) | <u>2021</u> <u>Carrying</u> <u>Amount</u> | <u>2020</u> <u>Carrying</u> <u>Amount</u> | <u>Effective</u> <u>Interest</u> <u>Rate</u> ⁽²⁾ | <u>Fiscal</u> <u>Year of</u> <u>Maturity</u> |
|-----------------------------------|---|---|---|--|
| Series debt | | | | |
| Fixed-rate debt | | | | |
| Series 2016A | \$ 476,930 | \$ 476,930 | 4.1% | 2047 |
| Series 2016B | 300,000 | 300,000 | 4.1% | 2027 |
| Series 2017A | 121,270 | 121,270 | 4.1% | 2049 |
| Series 2017 | 100,000 | 100,000 | 4.2% | 2038 |
| Series 2019B | 128,600 | 128,600 | 3.9% | 2055 |
| Series 2020A | - | 300,000 | 2.2% | 2022 |
| Total fixed-rate debt | <u>1,126,800</u> | <u>1,426,800</u> | 3.8% | |
| Variable-rate debt | | | | |
| Series 2016D | - | 100,000 | 2.8% | 2047 |
| Series 2016F | 21,900 | 21,900 | 1.3% | 2025 |
| Series 2017B | 50,000 | 50,000 | 1.3% | 2047 |
| Series 2018 | 53,385 | 53,385 | 0.7% | 2050 |
| Series 2019A | 35,000 | 35,000 | 0.6% | 2050 |
| Series 2021A | 200,000 | - | 0.5% | 2022 |
| Total variable-rate debt | <u>360,285</u> | <u>260,285</u> | 1.2% | |
| Total series debt | <u>1,487,085</u> | <u>1,687,085</u> | | |
| Other long-term debt | | | | |
| Lines of credit | 100,000 | 100,000 | 0.7% | 2022 |
| Subordinated note payable | 74,583 | 79,583 | 3.2% | 2036 |
| Product financing arrangement | 25,121 | 29,236 | 4.2% | 2027 |
| Finance leases | 16,997 | 15,980 | 2.5% | Various |
| Subtotal ⁽¹⁾ | <u>1,703,786</u> | <u>1,911,884</u> | 3.3% | |
| Net unamortized premiums | 53,986 | 56,244 | | |
| Net unamortized issuance costs | <u>(10,918)</u> | <u>(12,517)</u> | | |
| Total long-term debt | <u>1,746,854</u> | <u>1,955,611</u> | | |
| Short-term borrowings | (300,000) | (100,000) | | |
| Current portion of long-term debt | <u>(14,704)</u> | <u>(14,321)</u> | | |
| Long-term debt, net | <u>\$ 1,432,150</u> | <u>\$ 1,841,290</u> | | |

(1) The effective interest rate of 3.3% as of June 30, 2021, is presented exclusive of interest rate exchange agreements discussed in Note 12 Interest Rate Exchange Agreements. Inclusive of these agreements, the overall portfolio effective interest rate was 3.6%.

(2) The effective interest rate for each debt instrument is calculated by dividing each instrument's interest expense by the weighted average debt outstanding, and where applicable, interest expense is reduced by premium amortization and increased by original issue discount amortization. Interest rates per the agreements are detailed in the accompanying notes.

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On April 29, 2016, VUMC issued the Series 2016 A, B, D, E, and F bonds (“2016 Series Debt”) and notes aggregating \$1.3 billion of proceeds for the purpose of financing the Medical Center Acquisition and paying a portion of the costs of issuance associated with the 2016 Series Debt.

The bonds and notes comprising the 2016 Series Debt were issued by the Health and Educational Facilities Board of The Metropolitan Government of Nashville and Davidson County, Tennessee (“HEFB”). As a conduit issuer, the HEFB loaned the debt proceeds to VUMC. VUMC’s debt service requirements under these loan agreements coincide with required debt service of the actual HEFB bonds.

- The Series 2016A tax-exempt fixed-rate revenue bonds were issued in the par amount of \$476.9 million and include an original issue premium of \$59.6 million. The Series 2016A bonds have a final maturity date of July 1, 2046, and can be optionally redeemed at par on or after July 1, 2026. The 2016A bonds were structured as serial bonds with maturities from Fiscal 2030 through 2032, as well as three term bonds maturing Fiscal 2036 through 2047, which are subject to mandatory sinking fund redemption in lots. The Series 2016A bonds bear interest at 5% per annum and pay interest semiannually on July 1 and January 1.
- The Series 2016B taxable fixed-rate revenue bonds were issued in the par amount of \$300.0 million, bearing interest at 4.1% per annum. Interest is paid semiannually on July 1 and January 1, and has a bullet maturity of July 1, 2026. VUMC is entitled, at its option, to redeem all or a portion of the Series 2016B bonds before April 1, 2026, at a make-whole redemption price, which equals the greater of (i) 100% of the remaining outstanding principal and (ii) the net present value of the remaining scheduled principal and interest payments to the original maturity date, using a discount rate of 35 basis points above rates for U.S. Treasury securities with comparable maturities.
- The Series 2016D taxable variable-rate revenue notes (“floating rate notes”) were issued in the par amount of \$100.0 million and bear interest initially at a fixed spread to one-month LIBOR of 2.5% through the initial mandatory tender date of July 1, 2021, and a final maturity of July 1, 2046. Beginning six months prior to the mandatory tender date of July 1, 2021, the bonds have an optional redemption feature. If the Series 2016D bonds are successfully remarketed at the mandatory tender date, they are subject to mandatory redemption in lots commencing on July 1, 2021, and each July thereafter until final maturity. During Fiscal 2021, the Series 2016D floating rate notes were extinguished using cash on hand.
- The Series 2016E taxable term loan revenue notes were issued in the par amount of \$128.1 million and were placed privately with a bank. The notes bear interest in a variable-rate mode at a fixed spread to one-month LIBOR of 2.4% through the initial mandatory tender date of July 1, 2022, and a final maturity of July 1, 2046. During Fiscal 2018, VUMC renegotiated the interest to a variable-rate mode at a fixed spread to one-month LIBOR of 1.8%. In addition to optional redemption of all or a portion of the notes at any time, subject to notice, the Series 2016E notes are subject to principal amortization commencing on July 1, 2022, as defined in the Series 2016E loan agreement between VUMC and the lender. During Fiscal 2020, the Series 2016E bonds were extinguished using proceeds from the 2019B taxable fixed private placement notes, discussed further below.
- The Series 2016F taxable variable-rate revenue bonds were issued in the par amount of \$75.0 million and were placed privately with a bank. The bonds bear interest in a variable-rate mode at a fixed spread to one-month LIBOR of 2.5% through the initial mandatory tender date of July 1, 2022. During Fiscal 2018, \$53.1 million of the Series 2016F bonds were extinguished using proceeds from the 2018 tax-exempt fixed-rate revenue bonds, discussed further below.

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The renegotiated interest rate on the remaining \$21.9 million of principal outstanding is a variable-rate mode at a fixed spread to one-month LIBOR of 1.2%. The remaining principal has a mandatory tender date of July 1, 2024. Prior to that, VUMC must pay \$2.1 million of principal on July 1, 2022, and \$2.2 million of principal on July 1, 2023. The remaining \$17.6 million of principal is due on July 1, 2024.

On July 26, 2017, the Series 2017A Tax-Exempt and Series 2017 Taxable Corporate Bonds were issued, and on August 1, 2017, the Series 2017B Taxable Revenue Bonds were issued ("2017 Series Debt"), aggregating \$271.3 million of proceeds for the purpose of refinancing existing debt, funding capital projects related to the MCJCHV expansion and the VUH bed expansion/clinical relocation, which is a phased project, and paying a portion of the costs of issuance associated with the 2017 Series Debt.

The Series 2017A Tax-Exempt Revenue Bonds and the Series 2017B Taxable Term Loan Revenue Note were issued by the HEFB. The Series 2017 Taxable Bonds were a corporate issue with VUMC as the issuer.

- The Series 2017A tax-exempt fixed-rate revenue bonds were issued in the par amount of \$121.3 million and include an original issue premium of \$5.1 million. The final maturity date is July 1, 2048, and optional redemption at par can occur on or after July 1, 2027. The Series 2017A bonds bear interest at 4.4% per annum and pay interest semiannually on July 1 and January 1.
- The Series 2017 taxable fixed-rate corporate bonds were issued in the par amount of \$100.0 million, bearing interest at 4.2% per annum. Interest is paid semiannually on July 1 and January 1, and the bonds have a final maturity date of July 1, 2037. There is a bullet payable beginning July 1, 2026, that allows VUMC to call the debt.
- The Series 2017B taxable variable-rate term loan notes were issued in the par amount of \$50 million and placed privately with a bank. The notes bear interest initially at a fixed-spread to one-month LIBOR of 1.2%. The notes have a final maturity date of July 1, 2046, a tender date of August 1, 2024, and may be redeemed at any time. Proceeds from the issuance of the Series 2017B notes were used to extinguish the Series 2016C R-FLOATs, initially issued on April 29, 2016.

On April 20, 2018, the Series 2018 Tax-Exempt Revenue Bonds ("2018 Series Debt") aggregating \$53.4 million of proceeds were issued for the purpose of refinancing existing debt and paying a portion of the costs of issuance associated with the 2018 Series Debt. The Series 2018 Tax-Exempt Revenue Bonds were issued by the HEFB, were placed privately with a bank, and bear interest at a fixed spread to 81% of one-month LIBOR of 0.6%. The bonds have a final maturity date of July 1, 2049 and can be optionally redeemed on or after July 1, 2025. Proceeds from the issuance of the Series 2018 bonds were used to extinguish a portion of the Series 2016F taxable variable-rate bonds.

On July 30, 2019, VUMC entered into a term loan agreement (2019A Term Loan) with a lender for \$35 million to pay for the acquisition of Tennova – Lebanon (now VWCH) hospital facilities, near term capital expenditures, and costs of issuance. The term loan bears interest at a variable rate plus a fixed spread to one-month LIBOR of 0.50% through the maturity date of August 1, 2029. VUMC has the option to redeem prepay all or a portion of the loan at any time, subject to notice. The 2019 loan is subject to principal amortization commencing on July 1, 2024 and ending July 1, 2049, as defined in the 2019 loan agreement between VUMC and the lender.

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On October 22, 2019, the Series 2019B Taxable Fixed Private Placement Notes ("Series 2019B Notes") aggregating \$128.6 million of proceeds were issued for the purpose of refinancing existing debt and paying a portion of the costs of issuance associated with the Series 2019B Notes. The Series 2019B Notes were placed privately with a bank, and bear interest at a fixed rate of 3.9% per annum. The notes have a final maturity date of July 1, 2054. Proceeds from the issuance of the Series 2019B Notes were used to extinguish the Series 2016E Taxable Term Loan Revenue Notes.

On April 9, 2020, the Series 2020A Taxable Fixed Term Loan ("Series 2020A Loan") aggregating \$300 million was issued to provide additional liquidity during the COVID-19 pandemic. The lender for the Series 2020A Loan was JPMorgan Chase Bank. The debt bears interest at a fixed rate of 2.1% per annum, has an optional redemption after one year, and has a final maturity date of April 1, 2022. During Fiscal 2021, the Series 2020A Loan was extinguished using proceeds from the Series 2021A Short-Term Loan discussed further below, and draws on available lines of credit.

On April 9, 2021, the Series 2021A Short-Term Loan was issued in the par amount of \$200.0 million for the purpose of refinancing the Series 2020A Loan. The lender for the Series 2021A Short-Term Loan was Royal Bank of Canada. The debt bears interest at a fixed spread to LIBOR of 0.4% and has a maturity of April 8, 2022.

Each of the bonds and notes comprising the 2016, 2017, 2018, 2019, 2020, and 2021 Series Debt represent separate obligations under a Master Trust Indenture ("MTI") structure. The MTI provides the flexibility for multiple parties to participate in debt issuances as part of an obligated group; presently, VUMC has no other third-party members participating in the obligated group. All debt issued under the MTI is a general obligation of the obligated group. Under the provisions of the Leasehold Deed of Trust, Security Agreement, Assignment of Rents and Leases, and Fixture Filing (the "Security Agreement") within the MTI, gross receivables of the obligated group are pledged as collateral. Additionally, the Security Agreement established a mortgage lien on (i) the leasehold interest of the land subject to the Ground Lease; (ii) the buildings, structures, improvements, and fixtures now or hereafter located on the land subject to the Ground Lease; and (iii) certain other collateral.

Trust indentures for certain bond issues contain covenants and restrictions, the most material of which include limitations on the issuance of additional debt, maintenance of a specified debt service coverage ratio, and a minimum amount of days cash on hand. VUMC complied with such covenants and restrictions as of June 30, 2021 and 2020.

On April 29, 2016, VUMC delivered a secured subordinated promissory note in the amount of \$100.0 million to VU to finance the Acquisition (the "subordinated note"). In July of 2018, VU sold its rights to future principal and interest payments on this note to a third party. The note was issued at a fixed rate of 3.25% with monthly principal payments totaling \$5.0 million annually commencing on May 31, 2016, for a period of 20 years ending on April 30, 2036. VUMC may, at any time and from time to time, without premium or penalty, prepay all or any portion of the unpaid principal amount of the subordinated note. This note is secured by the gross receivables and mortgaged property described in the Security Agreement subject to the requirements of the 2016 Series Debt and the MTI.

As part of the Acquisition, VUMC assumed a 10-year, unsecured, noninterest-bearing product financing arrangement with a vendor for the purchase and implementation of internal use software. The annual payment of \$5.3 million is payable in monthly installments, is considered principal and imputed interest, and continues through Fiscal 2027. The balance due under the Product Financing Arrangement is \$25.1 million and \$29.2 million as of June 30, 2021 and 2020, respectively.

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At June 30, 2021 and 2020, \$4.3 million and \$4.1 million was included in the current portion of long-term debt caption, with the remaining balance in long-term debt, net of current portion.

In Fiscal 2021 and 2020, noncash investing and financing activities totaled \$6.8 million and \$19.1 million, respectively, related to finance leases.

VUMC has an agreement with a bank to provide a general use line of credit with a maximum available commitment totaling \$100.0 million. On March 18, 2020, VUMC drew down the available \$100 million, which bears interest at a fixed spread to one-month LIBOR of 0.65% and has no maturity date if the line of credit is renewed annually. The outstanding balance on the line of credit is \$59.5 million and \$100.0 million as of June 30, 2021 and 2020, respectively. The line of credit accrues a commitment fee of 0.15% per annum on any unused portion of the line of credit.

VUMC established one additional line of credit with a bank in Fiscal 2021. A \$50 million line of credit with Royal Bank of Canada, bearing interest at a fixed spread to one-month LIBOR of 0.45%, maturing in Fiscal 2022 with a commitment fee of 0.2% on any unused portion of the line of credit. As of June 30, 2021, this line of credit had an outstanding balance of \$40.5 million.

VUMC established three additional lines of credit with banks in Fiscal 2020:

- \$50 million line of credit with Truist, bearing interest at a fixed spread to one-month LIBOR of 1.0%, maturing in Fiscal 2022 with a commitment fee of 0.25% on any unused portion of the line of credit. As of June 30, 2021 and 2020, this line of credit had no outstanding balance.
- \$50 million line of credit with Truist, bearing interest at a fixed spread to one-month LIBOR of 0.85%, maturing in Fiscal 2021 with a commitment fee of 0.25% on any unused portion of the line of credit. As of June 30, 2020, this line of credit had no outstanding balance. This line of credit expired during Fiscal 2021.
- \$50 million line of credit with Bank of New York Mellon, bearing interest at a fixed spread to one-month LIBOR of 1.4%, maturing in Fiscal 2021 with a commitment fee of 0.25% on any unused portion of the line of credit. As of June 30, 2020, this line of credit had no outstanding balance. This line of credit expired during Fiscal 2021.

The total outstanding balance on lines of credit is \$100.0 million as of June 30, 2021 and 2020. Commitment fees for the lines of credit totaled \$0.4 million and \$0.2 million in Fiscal 2021 and Fiscal 2020, respectively.

Interest paid on all obligations, including interest rate swap settlements, net of amounts capitalized, was \$68.4 million and \$62.7 million in Fiscal 2021 and 2020, respectively.

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Principal retirements and scheduled sinking fund requirements based on nominal maturity schedules for long-term debt due in subsequent fiscal years ending June 30 are as follows:

(\$ in thousands)

| | |
|------------|---------------------|
| 2022 | \$ 314,585 |
| 2023 | 16,094 |
| 2024 | 15,915 |
| 2025 | 80,974 |
| 2026 | 64,785 |
| Thereafter | 1,211,433 |
| | <u>\$ 1,703,786</u> |

12. Interest Rate Exchange Agreements

Key features of VUMC interest rate exchange agreements are summarized below:

| <u>Notional Amount</u> | <u>Pay Fixed Rate</u> | <u>Receive Variable Rate</u> | <u>Mandatory Termination Date</u> |
|------------------------|-----------------------|------------------------------|-----------------------------------|
| \$75.0 million | 4.28% | 68% of one-month LIBOR | April 29, 2026 |
| \$75.0 million | 4.18% | 68% of one-month LIBOR | April 29, 2023 |

VUMC incorporates these interest rate exchange agreements into its debt portfolio management strategy. There are no collateral pledging requirements. The agreements terminate automatically on April 29, 2026 and 2023, if not renegotiated or extended, at which point the exchange agreements will be settled at fair value.

VUMC recorded the following activity related to the interest rate exchange agreements during Fiscal 2021 and 2020:

| <i>(\$ in thousands)</i> | <u>2021</u> | <u>2020</u> |
|--|------------------|--------------------|
| Mark-to-market adjustments | \$ 23,478 | \$ (32,441) |
| Cash settlements | (6,106) | (4,711) |
| Unrealized gain (loss) on interest rate exchange agreements, net of cash settlements | <u>\$ 17,372</u> | <u>\$ (37,152)</u> |

13. Leases

VUMC has operating and finance leases for real estate, personal property and equipment. VUMC determines if an arrangement is a lease at the inception of a contract. Leases with an initial term of twelve months or less are not recorded on the consolidated balance sheets.

VUMC has lease agreements which require payments for lease and non-lease components and has elected to account for these as a single lease component. For leases that commenced before the effective date of ASU 2016-02, VUMC elected the permitted practical expedients to not reassess the following: (i) whether any expired or existing contracts contain leases; (ii) the lease classification for any expired or existing leases; and (iii) initial direct costs for any existing leases.

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Right-of-use assets represent VUMC's right to use an underlying asset during the lease term, and lease liabilities represent VUMC's obligation to make lease payments arising from the lease. Right-of-use assets and liabilities are recognized at the commencement date, based on the net present value of fixed lease payments over the lease term. VUMC's lease terms include options to extend or terminate the lease when it is reasonably certain that the options will be exercised. As most of VUMC's operating leases do not provide an implicit rate, VUMC uses its incremental borrowing rate based on the information available at the commencement date in determining the present value of lease payments. VUMC considers recent debt issuances, as well as publicly available data for instruments with similar characteristics when calculating its incremental borrowing rates. Finance lease agreements generally include an interest rate that is used to determine the present value of future lease payments. Operating fixed lease expense and finance lease depreciation expense are recognized on a straight-line basis over the lease term. Variable lease costs consist primarily of common area maintenance and other index adjustments.

Operating and finance lease right-of-use assets and lease liabilities as of June 30, 2021 and 2020, are as follows:

| (\$ in thousands) | Balance Sheet Classification | 2021 | 2020 |
|---|---|-------------------|-------------------|
| Assets: | | | |
| Operating leases | Operating leases | \$ 839,850 | \$ 846,695 |
| Finance leases | Property, plant, and equipment, net | 17,363 | 16,712 |
| Total lease assets | | <u>\$ 857,213</u> | <u>\$ 863,407</u> |
| Liabilities: | | | |
| Current: | | | |
| Operating leases | Current portion of operating lease liabilities | \$ 67,343 | \$ 70,062 |
| Finance leases | Current portion of long-term debt | 5,412 | 5,206 |
| Noncurrent: | | | |
| Operating leases | Noncurrent portion of operating lease liabilities | 795,330 | 797,811 |
| Finance leases | Long-term debt, net of current portion | 11,584 | 10,774 |
| Total lease liabilities | | <u>\$ 879,669</u> | <u>\$ 883,853</u> |
| Weighted-average remaining term: | | | |
| Operating leases | | 57.4 years | 57.3 years |
| Finance leases | | 3.6 years | 3.8 years |
| Weighted-average discount rate: | | | |
| Operating leases | | 3.7% | 3.7% |
| Finance leases | | 2.4% | 2.4% |

Included in the tables above is the Ground Lease with VU expiring in 2114 discussed below. Excluding this lease, the weighted average remaining lease term for VUMC's operating leases is 8.2 years as of June 30, 2021. As of June 30, 2021 and 2020, the land lease comprises \$489.2 million and \$489.7 million, respectively, of the operating lease asset and \$491.9 million and \$492.5 million, respectively, of the operating lease liability detailed above.

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Lease expense for finance and operating leases for the years ended June 30, 2021 and 2020, are as follows:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|-------------------|-------------------|
| Finance lease expense: | | |
| Amortization of leased assets | \$ 6,125 | \$ 4,433 |
| Interest on lease liabilities | 410 | 273 |
| Operating lease expense ⁽¹⁾ | 109,665 | 107,358 |
| Short-term lease expense ⁽¹⁾ | 4,578 | 3,787 |
| Variable lease expense ⁽¹⁾ | 16,181 | 13,321 |
| | <u>\$ 136,959</u> | <u>\$ 129,172</u> |

⁽¹⁾ Expense is included in "Facilities and equipment" in the consolidated statements of operations.

The following table presents supplemental cash flow information for the years ended June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|---|-------------|-------------|
| Cash paid for amounts included in the measurement of lease liabilities: | | |
| Operating cash flows for operating leases | \$ 105,136 | \$ 103,166 |
| Operating cash flows for finance leases | 410 | 273 |
| Financing cash flows for finance leases | 5,766 | 4,334 |

The following table reconciles the undiscounted minimum lease payments to the operating and financing lease liabilities recorded on the consolidated balance sheet at June 30, 2021:

| <i>(\$ in thousands)</i> | Operating Leases | Finance Leases |
|--|-------------------------|-----------------------|
| 2022 | \$ 95,338 | \$ 5,666 |
| 2023 | 82,660 | 4,743 |
| 2024 | 74,699 | 4,176 |
| 2025 | 69,689 | 2,567 |
| 2026 | 58,694 | 360 |
| Thereafter | 1,848,298 | 202 |
| Total minimum lease payments | <u>2,229,378</u> | <u>17,714</u> |
| Less: amount of lease payments representing interest | <u>(1,366,705)</u> | <u>(718)</u> |
| Present value of future minimum lease payments | 862,673 | 16,996 |
| Less: current lease obligations | <u>(67,343)</u> | <u>(5,412)</u> |
| Long-term lease obligations | <u>\$ 795,330</u> | <u>\$ 11,584</u> |

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Essential provisions of leases considered by management to be material are as follows:

- On April 29, 2016, VUMC entered into a Ground Lease with VU for approximately 1.7 million square feet of land for an initial term ending June 30, 2114, and an option to extend for up to two additional terms of 50 to 99 years each upon agreement by VU and VUMC. The annual base rent is payable monthly, and is CPI adjusted annually. VUMC made rental payments totaling \$19.6 million and \$19.4 million in Fiscal 2021 and Fiscal 2020, respectively. The Ground Lease allows VUMC to use the land on which its campus and related buildings are located. Included in the table above are \$1.8 billion in ground lease payments representing future minimum rentals based on the initial annual base rent of \$19.4 million, excluding annual CPI adjustments.
- In July 2007, VU entered into an agreement to lease approximately 50% of the space in the 850,000 square foot One Hundred Oaks shopping center located approximately five miles from the main campus ("100 Oaks Lease"). VU redeveloped this leased space primarily for medical and office uses. In October 2014, VU agreed to an amendment which extends the original lease term to November 30, 2035, with an option to renew the lease further for four additional 10-year periods. As part of the lease agreement, the lessee also has first rights on leasing additional space in the shopping center and first rights on purchasing if the landlord desires to sell. On April 29, 2016, the 100 Oaks Lease was assigned to VUMC. As a condition of the assignment, amendments to the 100 Oaks Lease were added which required VUMC to provide the landlord a \$25.0 million irrevocable standby letter of credit. The amounts related to this standby letter of credit are recorded as facilities and equipment expense and totaled \$0.2 million in both Fiscal 2021 and 2020. The standby letter of credit is no longer required under the lease and has been released as of June 10, 2021. VUMC included minimum property rental payments totaling \$111.6 million related to this space in the above minimum lease payments table.
- On April 29, 2016, VU assigned to VUMC a lease for approximately 231,000 square feet of office space at 2525 West End Avenue with expiration dates ranging from 2026 through 2030, with options to renew for two additional five-year periods. VUMC included minimum lease payments totaling \$59.0 million related to this space in the above minimum lease payments table.
- On April 29, 2016, VUMC and VU entered into certain lease agreements for the use of space in buildings owned by both entities. As of June 30, 2021, VUMC's estimated future minimum lease payments to VU totaled \$33.6 million. Estimated future lease receipts from VU for the fiscal year ended June 30, 2022, are \$7.5 million, subject to annual renewal.

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14. Net Assets

Net asset restrictions relate to the following purposes as of June 30, 2021 and 2020:

| <i>(\$ in thousands)</i> | 2021 | 2020 |
|--|-------------------|-------------------|
| Donor-restricted – time or purpose | | |
| Property, plant, and equipment | \$ 13,044 | \$ 10,920 |
| Research and education | 115,897 | 106,167 |
| Operations | 15,087 | 4,661 |
| Total donor-restricted – time or purpose | <u>\$ 144,028</u> | <u>\$ 121,748</u> |
| Donor restricted – perpetuity | | |
| Research and education | <u>\$ 80,530</u> | <u>\$ 64,807</u> |

Net assets without donor restrictions are free of donor-imposed restrictions. This classification includes all revenues, gains, and losses not restricted by donors. VUMC reports all expenditures in net assets without donor restrictions since the use of restricted contributions in accordance with donors' stipulations results in the release of the restriction.

Donor restricted – time or purpose contain donor-imposed stipulations that expire with the passage of time or that can be satisfied by the action of VUMC. These net assets may include restricted gifts including unconditional pledges, split-interest agreements, interests in trusts held by others, and accumulated appreciation on donor-restricted endowments not yet appropriated by the Board of Directors for distribution. Donor gifts that are restricted for funding capital projects are considered released from restriction once related capital expenditures have been made and the asset is placed in service.

Donor restricted – perpetuity contains amounts held in perpetuity as requested by donors. These net assets may include unconditional pledges, donor-restricted endowments, split-interest agreements, and interests in trusts held by others. Generally, the donors of these assets permit VUMC to use a portion of the income earned on related investments for specific purposes.

UPMIFA specifies that unless stated otherwise in a gift instrument, donor-restricted assets in an endowment fund are restricted assets until appropriated for expenditure. Barring the existence of specific instructions in gift agreements for donor-restricted endowments, VUMC reports the historical value of such endowments as donor restricted – perpetuity and the net accumulated appreciation as donor restricted – time or purpose. In this context, the historical value represents the original value of initial contributions restricted as permanent endowments plus the original value of subsequent contributions and, if applicable, the value of accumulations made in accordance with the direction of specific donor gift agreements.

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15. Fair Value Measurements

Fair value measurements represent the amount at which the instrument could be exchanged in an orderly transaction between market participants at the measurement date. VUMC utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels:

- | | |
|---------|---|
| Level 1 | Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that VUMC has the ability to access. |
| Level 2 | Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, inputs other than quoted prices that are observable for the assets or liabilities, and inputs that are derived principally from or corroborated by observable market data by correlation or other means. |
| Level 3 | Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs reflect VUMC's assumptions about the inputs market participants would use in pricing the asset or liability, including assumptions about risk. Unobservable inputs are developed based on the best information available in the circumstances and may include VUMC's own data. |

VUMC's principal assets and liabilities are cash and cash equivalents, investments, patient accounts receivable, estimated receivables and payables under third-party programs, grants and contracts receivable, pledges receivable, operating lease assets, accounts payable and other accrued expenses, self-insurance reserves, operating lease liabilities, long-term debt, and interest rate exchange agreements. Except for long-term debt, the carrying amount of these assets and liabilities approximates fair value.

As of June 30, 2021, the carrying value and estimated fair value of total long-term debt totaled \$1.7 billion and \$1.9 billion, respectively. As of June 30, 2020, the carrying value and estimated fair value of total long-term debt totaled \$2.0 billion and \$2.0 billion, respectively. VUMC bases estimated fair value of long-term debt on market conditions prevailing at fiscal year-end reporting dates. Besides potentially volatile market conditions, fair value estimates typically reflect limited secondary market trading. The fair values of the fixed-rate Series Debt, as defined in Note 11 Long-Term Debt, were based on a Level 2 computation using quoted prices for similar liabilities in active markets as of June 30, 2021 and 2020, as applicable. The carrying amounts related to VUMC's variable-rate Series Debt and other long-term debt obligations approximate their fair values as of June 30, 2021 and 2020. As of June 30, 2021 and 2020, the fair values of the subordinated note payable and the product financing arrangement were based on a Level 2 discounted cash flow approach applying a risk-adjusted spread for issuers of similar credit quality to U.S. Treasury yields for securities with comparable maturities.

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For financial instruments measured at fair value on a recurring basis, the following tables summarize valuation hierarchy levels as of June 30, 2021 and 2020, determined by the nature of the financial instrument and the least observable input significant to the fair value measurement:

| (\$ in thousands) | Fair Value Measurements as of June 30, 2021 | | | |
|---|---|-------------------|-------------|-----------------------|
| | Level 1 | Level 2 | Level 3 | Total Carrying Amount |
| Assets | | | | |
| Corporate bonds | \$ 38,310 | \$ 298,595 | \$ - | \$ 336,905 |
| Equity mutual funds | 29,174 | 122,026 | - | 151,200 |
| Cash and cash equivalents | 27,681 | - | - | 27,681 |
| Beneficial interests in split-interest trusts | - | 9,503 | - | 9,503 |
| Hedged equity mutual funds | - | 107,548 | - | 107,548 |
| Fixed-income mutual funds | 114,871 | 102,891 | - | 217,762 |
| Certificates of deposit | - | 21,162 | - | 21,162 |
| Asset-backed securities | 6,982 | 21,989 | - | 28,971 |
| Mortgage-backed securities | - | 6,503 | - | 6,503 |
| Commercial paper | - | 37,040 | - | 37,040 |
| Government bonds | 21,884 | 31,249 | - | 53,133 |
| Hedged debt mutual funds | - | 114,474 | - | 114,474 |
| Commodities and managed futures mutual funds | 10,759 | 9,043 | - | 19,802 |
| Target date mutual funds | - | 5,168 | - | 5,168 |
| Total assets reported at fair value | <u>\$ 249,661</u> | <u>\$ 887,191</u> | <u>\$ -</u> | <u>\$ 1,136,852</u> |
| Liabilities | | | | |
| Interest rate exchange agreements | \$ - | \$ 76,864 | \$ - | \$ 76,864 |
| Total liabilities reported at fair value | <u>\$ -</u> | <u>\$ 76,864</u> | <u>\$ -</u> | <u>\$ 76,864</u> |

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| | Fair Value Measurements as of June 30, 2020 | | | |
|--|---|------------|---------|-----------------------|
| (\$ in thousands) | Level 1 | Level 2 | Level 3 | Total Carrying Amount |
| Assets | | | | |
| Corporate bonds | \$ 15,805 | \$ 219,444 | \$ - | \$ 235,249 |
| Equity mutual funds | 34,589 | 93,980 | - | 128,569 |
| Cash and cash equivalents | 13,147 | - | - | 13,147 |
| Beneficial interests in | | | | |
| split-interest trusts | - | 7,124 | - | 7,124 |
| Hedged equity mutual funds | - | 64,986 | - | 64,986 |
| Fixed-income mutual funds | 120,658 | 69,396 | - | 190,054 |
| Certificates of deposit | - | 16,338 | - | 16,338 |
| Asset-backed securities | - | 26,448 | - | 26,448 |
| Real estate mutual funds | - | 20,680 | - | 20,680 |
| Commercial paper | - | 22,218 | - | 22,218 |
| Government bonds | 10,665 | 69,480 | - | 80,145 |
| Hedged debt mutual funds | - | 70,958 | - | 70,958 |
| Commodities and managed | | | | |
| futures mutual funds | 9,121 | 6,781 | - | 15,902 |
| Target date mutual funds | - | 4,865 | - | 4,865 |
| Total assets reported at fair value | \$ 203,985 | \$ 692,698 | \$ - | \$ 896,683 |
| Liabilities | | | | |
| Interest rate exchange agreements | \$ - | \$ 100,342 | \$ - | \$ 100,342 |
| Total liabilities reported at fair value | \$ - | \$ 100,342 | \$ - | \$ 100,342 |

VUMC employs derivatives, primarily interest rate exchange agreements, to help manage interest rate risks associated with variable-rate debt. In addition to the credit risk of the counterparty owing a balance, VUMC calculates the fair value of interest rate exchange agreements based on the present value of future net cash settlements that reflect market yields as of the measurement date.

Parties to interest rate exchange agreements are subject to risk for changes in interest rates, as well as the risk of credit loss in the event of nonperformance by the counterparty. VUMC deals only with high-quality counterparties that meet rating criteria for financial stability and credit-worthiness.

16. Retirement Plan

VUMC's full-time employees participate in a 403(b) defined contribution retirement plan administered by a third party. For eligible employees with one year of continuous service, this plan requires employer matching of employee contributions up to 5% of eligible compensation. The employee immediately vests in these contributions.

VUMC funds the obligations under this plan through monthly transfers to the respective retirement plan administrator with the corresponding expense recognized in the year incurred. During Fiscal 2021 and 2020, VUMC recognized \$76.8 million and \$69.8 million, respectively, of expense in connection with this plan.

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17. Functional Expense

VUMC provides general health care services primarily to residents within its geographic location and supports research and education programs. Total operating expense by nature and function for Fiscal 2021 and 2020 were as follows:

(\$ in thousands)

| | For the year ended June 30, 2021 | | | |
|-------------------------------|---|--|-------------------------------------|---------------------|
| | Healthcare Services | Academic Research and Education | Administrative and Other | Total |
| Salaries, wages, and benefits | \$ 2,021,532 | \$ 581,945 | \$ 233,067 | \$ 2,836,544 |
| Supplies and drugs | 1,134,657 | 56,507 | 25,039 | 1,216,203 |
| Facilities and equipment | 177,973 | 44,722 | 74,053 | 296,748 |
| Services and other | 599,477 | 107,610 | 88,200 | 795,287 |
| Depreciation and amortization | 128,181 | 1,582 | 21,691 | 151,454 |
| Interest | 49,351 | 11,163 | 16 | 60,530 |
| Total operating expense | <u>\$ 4,111,171</u> | <u>\$ 803,529</u> | <u>\$ 442,066</u> | <u>\$ 5,356,766</u> |

(\$ in thousands)

| | For the year ended June 30, 2020 | | | |
|-------------------------------|---|--|-------------------------------------|---------------------|
| | Healthcare Services | Academic Research and Education | Administrative and Other | Total |
| Salaries, wages, and benefits | \$ 1,773,506 | \$ 542,728 | \$ 179,561 | \$ 2,495,795 |
| Supplies and drugs | 980,544 | 46,640 | 19,214 | 1,046,398 |
| Facilities and equipment | 160,705 | 40,556 | 72,144 | 273,405 |
| Services and other | 549,059 | 98,291 | 92,905 | 740,255 |
| Depreciation and amortization | 103,734 | 1,521 | 21,399 | 126,654 |
| Interest | 47,172 | 13,585 | 14 | 60,771 |
| Total operating expense | <u>\$ 3,614,720</u> | <u>\$ 743,321</u> | <u>\$ 385,237</u> | <u>\$ 4,743,278</u> |

Certain expense categories are attributable to more than one function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. The expenses that are allocated include salaries, wages, and benefits, and services and other.

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18. Commitments and Contingencies

Management has policies, procedures, and an organizational structure to enforce and monitor compliance with government statutes and regulations. VUMC's compliance with such laws and regulations is subject to future government review and interpretations, as well as regulatory actions unknown or unasserted at this time.

- **Litigation.** VUMC is a defendant in certain lawsuits alleging medical malpractice and civil action.

In December 2019, VUMC was notified by the Internal Revenue Service (the "IRS") of its intention to conduct an examination of the 403b Plan for the year ending December 31, 2017. During that examination, the Company identified certain concerns relating to the calculation of the employer match provided by the Company under the 403b Plan, which was implemented by the Company in April 2016. Following review and discussion, in November 2020 the Company and IRS entered into a Closing Agreement, under which the IRS agreed to accept the Company's implementation of a retroactive amendment to the 403b Plan to correct the calculation of the employer match in exchange for payment by the Company of a penalty of a nominal amount. The execution and delivery of the Closing Agreement fully resolves such matters relating to the examination of the 403b Plan by the IRS.

Through the operation of its compliance program, VUMC from time to time initiates the review of billing for clinical services provided by VUMC and its affiliated providers. VUMC has established a liability reserve relating to certain matters under review as of June 30, 2021 and 2020, which is not material to VUMC's overall financial position.

- **Regulations.** VUMC's compliance with regulations and laws is subject to future government reviews and interpretations, as well as regulatory actions unknown at this time. VUMC believes that the liability, if any, from such reviews will not have a significant effect on VUMC's consolidated financial position.
- **Medical Malpractice Self-Insurance.** The consolidated balance sheets include reserves for medical malpractice, professional, and general liability coverage totaling \$72.6 million as of June 30, 2021, and \$60.3 million as of June 30, 2020. These liabilities are measured at the net present value of those cash flows using a discount rate of 2.5% at both dates and are classified as current or noncurrent based on the expected timing of cash flows. Other current assets include expected recoveries from commercial insurance carriers under excess coverage arrangements totaling \$3.8 million as of June 30, 2021, and \$2.7 million as of June 30, 2020. During Fiscal 2021 and 2020, VUMC recorded expenses for medical malpractice self-insurance of \$22.4 million and \$27.7 million, respectively.
- **Employee Health and Workers' Compensation Insurance.** Accrued compensation and benefits included actuarially determined liabilities for employee health and workers' compensation claims totaling \$21.8 million and \$6.7 million, respectively, as of June 30, 2021, and \$16.9 million and \$6.1 million, respectively, as of June 30, 2020. During Fiscal 2021 and 2020, VUMC recorded expenses for self-insured employee health benefit plans, net of employee premiums, totaling \$241.9 million and \$181.5 million, respectively. During Fiscal 2021 and 2020, VUMC recorded expenses for self-insured workers' compensation plans of \$4.9 million and \$2.9 million, respectively.

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- Federal and State Contracts and Other Requirements. Expenditures related to federal and state grants and contracts are subject to adjustment based upon review by the granting agencies. Amounts of expenditures that granting agencies might disallow cannot be determined at this time. These amounts affect government grants and contracts revenue, as well as facilities and administrative costs recovery. VUMC does not expect these costs to impact the consolidated financial position by material amounts.
- Health Care Services. In Fiscal 2021 and 2020, 85% and 83%, respectively, of VUMC's operating revenue was generated by providing health care services, where revenue is affected by reimbursement arrangements with federal and state healthcare programs, commercial insurance, and other managed care payors. If reimbursement rates from third-party payors decrease or if contract terms become less favorable in future periods, VUMC's operating revenues may decline. See Note 4 Patient Service Revenue, Patient Accounts Receivable, and Estimated Third-Party Settlements, for further information regarding healthcare revenues and related receivables.
- HIPAA Compliance. Under the Health Insurance Portability and Accountability Act of 1996 ("HIPAA"), the federal government has authority to complete fraud and abuse investigations. HIPAA has established substantial fines and penalties for offenders. VUMC maintains policies, procedures, and organizational structures to enforce and monitor compliance with HIPAA, as well as other applicable local, state, and federal statutes and regulations.
- Construction. VUMC had contractual commitments under major construction and equipment contracts totaling \$56.8 million and \$90.2 million as of June 30, 2021 and 2020, respectively.
- Letter of Credit. As a requirement of the assignment of the 100 Oaks Lease described in Note 13 Leases, VUMC provided an irrevocable standby letter of credit of \$25.0 million to the landlord of the property dated June 10, 2016. In FY21, this letter of credit was canceled and is no longer required as a result of VUMC achieving certain financial requirements.

19. Other Events

COVID-19

In March of Fiscal 2020, COVID-19, a disease caused by the novel strain of the coronavirus, was designated by the World Health Organization as a global pandemic. A state of emergency was subsequently announced by the State of Tennessee, quickly followed by "stay at home" orders and orders for hospitals and outpatient surgical facilities to stop non-essential procedures. This global health crisis negatively impacted many facets of the business, including lower patient volumes and related revenues, significant increases in certain supply cost (in particular personal protective equipment) as well as difficulties sourcing these supplies, and volatility in the U.S. and global financial markets impacting VUMC's investment portfolios. By the end of Fiscal 2020 and throughout Fiscal 2021, volumes rebounded, although subsequent surges of the virus in the winter of Fiscal 2021 and fall of Fiscal 2022 caused somewhat similar impacts, although to a lesser degree. Due to the evolving nature of the COVID-19 pandemic, despite positive indicators, the ultimate impact to VUMC and its financial condition is presently unknown.

Sources of pandemic relief include the federal stimulus package known as The Coronavirus Aid, Relief, and Economic Security ("CARES") Act, signed into law on March 27, 2020, the Coronavirus Response and Consolidated Appropriations Act ("CRCA") signed into law on December 27, 2020, and the American Rescue Plan ("ARP"), signed into law on March 11, 2021. These laws include a number of provisions: most importantly providing funding through the Public Health and Social

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June 30, 2021 and 2020

Services Emergency Fund ("Provider Relief Fund") to reimburse eligible health care providers for health care-related expenses or lost revenues not otherwise reimbursed that are directly attributable to COVID-19. These provider relief funds included amounts distributed to providers based on their share of the Medicare fee-for-service reimbursement ("General Distributions"). The funds also included for certain targeted distributions ("Targeted Distributions") to qualifying providers (primarily rural and high impact areas). For the period ended June 30, 2021, VUMC recognized as revenue approximately \$46.3 million in General Distributions and \$8.8 million in Targeted Distributions, for a total of \$55.1 million, under the Provider Relief Fund. For the period ended June 30, 2020, VUMC recognized as revenue approximately \$83.3 million in General Distributions and \$35.7 million in Targeted Distributions, for a total of \$119.0 million, under the Provider Relief Fund. These amounts are presented in Other operating revenue in the consolidated statement of operations.

In addition, the CARES Act provides for an expansion of the Medicare Accelerated and Advance Payment Program ("MAAPP") whereby inpatient acute care hospitals and other eligible providers may request an advanced payment of up to 100% of their Medicare payment amount for a six-month period to be repaid through withholding of future Medicare fee-for-service payments beginning 120 days after receipt. During Fiscal 2020, VUMC received advance payments from Medicare of \$222.4 million, which is recorded as a current liability on the consolidated balance sheet as of June 30, 2020.

On October 1, 2020, the Continuing Appropriations and Other Extensions Acts amended the repayment terms for the funds received under the MAAPP. Under the revised repayment terms, the Centers for Medicare and Medicaid Services ("CMS") began to automatically recoup the advance payments one year from the original date of issuance by offsetting the payments against newly submitted Medicare claims. Once the recoupment period began, for the first eleven (11) months, Medicare automatically recoups payments at a rate of 25% of the Medicare claims amount otherwise owed to VUMC. After the first recoupment period of eleven (11) months, and continuing for the following six (6) months, Medicare automatically recoups payments at a rate of 50% of the Medicare claims amount otherwise owed to VUMC. After this repayment term concludes, any balance that remains outstanding will be subject to interest at a rate of four percent (4%) per annum. In accordance with the repayment terms, CMS began recoupment of VUMC's MAAPP funds in April 2021 and has recouped \$33.0M as of June 30, 2021. VUMC expects the remaining liability will be subject to recoupment within the next twelve months, and as such, VUMC has classified the remaining MAAPP liability of \$189.4M as a current liability on the consolidated balance sheet as of June 30, 2021.

The CARES Act also allows for deferred payment of the employer portion of certain payroll taxes between March 27, 2020 and December 31, 2020, with 50% due December 31, 2021 and the remaining 50% due December 31, 2022. VUMC began deferring these payroll tax payments during the fourth quarter of Fiscal 2020. As of June 30, 2021, VUMC had deferred payroll tax payments of \$75.8 million, with \$37.9 million and \$37.9 million included in Accrued compensation and benefits and Other noncurrent liabilities, respectively, in the consolidated balance sheet. As of June 30, 2020, VUMC had deferred payroll tax payments of \$27.6 million, which are included in Other noncurrent liabilities in the consolidated balance sheet.

In addition, the CARES Act suspended the sequestration payment adjustment percentage of 2% applied to all Medicare Fee-for-Service claims from May 1, 2020 through December 31, 2020, with subsequent acts extending through December 31, 2021. This positively impacted Patient Service Revenue in the consolidated statements of operations by approximately \$14 million for Fiscal 2021 and \$3 million for Fiscal 2020. Beginning, September 1, 2020, the CARES Act also provided for a 20% Medicare supplement for Medicare patients diagnosed with COVID-19 that are admitted to the

Vanderbilt University Medical Center
Notes to Consolidated Financial Statements
June 30, 2021 and 2020

hospital, reflecting the additional costs of treating a patient with this diagnosis. VUMC recognized an additional \$6 million in Patient service revenue in the consolidated statement of operations for Fiscal 2021 related to this supplement.

Through the Paycheck Protection Program and Health Care Enhancement Act (the “PPHCE Act”), which was enacted on April 24, 2020, VUMC recognized an additional \$11.4 million as a payroll retention credit in Other operating revenue in Fiscal 2020.

During Fiscal 2021, VUMC recognized as Other operating revenue \$3.1 million for Tennessee staffing grants, \$2.0 million of business interruption insurance payments, \$2.0 million of State of Tennessee CARES funding, and \$0.8 million of other COVID-19 grants.

Acquisition of VBCH and VTHH

Effective January 1, 2021, VUMC acquired from CHS: Tennova Healthcare – Shelbyville and Tennova Healthcare – Harton, now known as Vanderbilt Bedford Hospital (“VBCH”) and Vanderbilt Tullahoma-Harton Hospital (“VTHH”) for total consideration of \$15.6 million.

The following table summarizes the fair value of net assets acquired:

(\$ in thousands)

| | |
|---|------------------|
| Inventories | \$ 2,808 |
| Other current assets | 882 |
| Property, plant, and equipment, net | 11,943 |
| Operating lease assets | 4,230 |
| Other noncurrent assets | 122 |
| Accounts payable and other accrued expenses | (155) |
| Operating lease liabilities | (4,230) |
| Total invested capital | <u>\$ 15,600</u> |

Acquisition of VWCH

Effective August 1, 2019, VUMC acquired from CHS: Tennova Healthcare – Lebanon, now known as Vanderbilt Wilson County Hospital (“VWCH”) for total consideration of \$19.3 million.

The following table summarizes the fair value of net assets acquired:

(\$ in thousands)

| | |
|---|------------------|
| Inventories | \$ 2,966 |
| Other current assets | 865 |
| Property, plant, and equipment, net | 15,780 |
| Accounts payable and other accrued expenses | (359) |
| Total invested capital | <u>\$ 19,252</u> |

The results of operations for these acquisitions are included in the consolidated statements of operations and changes in net assets beginning on the acquisition dates. Pro forma results of operations and changes in net assets as though these acquisitions occurred on July 1, 2019 are not materially different and accordingly are not provided.

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June 30, 2021 and 2020

Acquisition of Noncontrolling Interest in VMH

As discussed in Note 1 – Description of Organization, effective January 1, 2021, VUMC acquired a noncontrolling ownership interest of 20% in CHS's affiliated Tennova Healthcare – Clarksville for total consideration of \$36.9 million. The noncontrolling interest is accounted for as an equity method investment and is included in Other noncurrent assets on the consolidated balance sheet.

20. Subsequent Events

Management evaluated events after June 30, 2021 through October 1, 2021, the date on which the consolidated financial statements were issued. During this period, there were no subsequent events requiring recognition or disclosure in the consolidated financial statements that have not been recorded or disclosed.

Report of Independent Auditors on Supplementary Information

The Board of Directors
Vanderbilt University Medical Center

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying Vanderbilt University Medical Center consolidating balance sheets and consolidating statements of operations 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 of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Ernst & Young LLP

October 1, 2021

Vanderbilt University Medical Center
Consolidating Balance Sheet
June 30, 2021

| (\$ in thousands) | Obligated Group | Nonobligated Entity | Eliminations | Consolidated |
|--|---------------------|------------------------|---------------------|---------------------|
| Assets | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | \$ 737,347 | \$ 99,965 | \$ - | \$ 837,312 |
| Intercompany receivable | 174,781 | - | (174,781) | - |
| Current investments | 215,484 | - | - | 215,484 |
| Patient accounts receivable | 530,712 | 23,162 | - | 553,874 |
| Grants and contracts receivable | 77,365 | - | - | 77,365 |
| Inventories | 137,279 | 3,002 | - | 140,281 |
| Other current assets | 99,962 | 18,297 | - | 118,259 |
| Total current assets | 1,972,930 | 144,426 | (174,781) | 1,942,575 |
| Restricted cash | 26,404 | 1,000 | - | 27,404 |
| Noncurrent investments | 791,389 | - | (12,000) | 779,389 |
| Noncurrent investments limited as to use | 127,414 | - | - | 127,414 |
| Property, plant, and equipment, net | 1,608,313 | 22,012 | - | 1,630,325 |
| Operating lease assets | 823,092 | 16,758 | - | 839,850 |
| Other noncurrent assets | 42,348 | 54,003 | - | 96,351 |
| Total assets | <u>\$ 5,391,890</u> | <u>\$ 238,199</u> | <u>\$ (186,781)</u> | <u>\$ 5,443,308</u> |
| Liabilities and Net Assets | | | | |
| Current liabilities: | | | | |
| Current portion of long-term debt | \$ 13,906 | \$ 798 | \$ - | \$ 14,704 |
| Intercompany payable | - | 174,781 | (174,781) | - |
| Short-term borrowings | 300,000 | - | - | 300,000 |
| Accounts payable and other accrued expenses | 335,424 | 20,747 | - | 356,171 |
| Medicare accelerated payments | 187,370 | 2,057 | - | 189,427 |
| Estimated payables under third-party programs | 37,669 | - | - | 37,669 |
| Accrued compensation and benefits | 309,306 | 7,225 | - | 316,531 |
| Current portion of operating lease liabilities | 63,115 | 4,228 | - | 67,343 |
| Current portion of deferred revenue | 3,182 | 1,058 | - | 4,240 |
| Current portion of medical malpractice self-insurance reserves | 15,820 | - | - | 15,820 |
| Total current liabilities | 1,265,792 | 210,894 | (174,781) | 1,301,905 |
| Long-term debt, net of current portion | 1,430,398 | 1,752 | - | 1,432,150 |
| Noncurrent portion of operating lease liabilities | 782,199 | 13,131 | - | 795,330 |
| Fair value of interest rate exchange agreements | 76,864 | - | - | 76,864 |
| Noncurrent portion of medical malpractice self-insurance reserves | 56,770 | - | - | 56,770 |
| Noncurrent portion of deferred revenue | 2,335 | 588 | - | 2,923 |
| Other noncurrent liabilities | 46,122 | 864 | - | 46,986 |
| Total liabilities | <u>3,660,480</u> | <u>227,229</u> | <u>(174,781)</u> | <u>3,712,928</u> |
| Net assets: | | | | |
| Net assets without donor restrictions controlled by Vanderbilt University Medical Center | 1,506,852 | 2,631 | (12,000) | 1,497,483 |
| Net assets without donor restrictions related to noncontrolling interests | - | 8,339 | - | 8,339 |
| Total net assets without donor restrictions | 1,506,852 | 10,970 | (12,000) | 1,505,822 |
| Net assets with donor restrictions | 224,558 | - | - | 224,558 |
| Total net assets | <u>1,731,410</u> | <u>10,970</u> | <u>(12,000)</u> | <u>1,730,380</u> |
| Total liabilities and net assets | <u>\$ 5,391,890</u> | <u>\$ 238,199</u> | <u>\$ (186,781)</u> | <u>\$ 5,443,308</u> |

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

Vanderbilt University Medical Center
Consolidating Balance Sheet
June 30, 2020

| (\$ in thousands) | Obligated Group | Nonobligated Entity | Eliminations | Consolidated |
|--|---------------------|------------------------|--------------------|---------------------|
| Assets | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | \$ 1,123,404 | \$ 47,122 | \$ - | \$ 1,170,526 |
| Intercompany receivable | 64,833 | - | (64,833) | - |
| Current investments | 232,178 | - | - | 232,178 |
| Patient accounts receivable | 462,550 | 8,000 | - | 470,550 |
| Grants and contracts receivable | 60,031 | - | - | 60,031 |
| Inventories | 103,784 | 819 | - | 104,603 |
| Other current assets | 98,702 | 19,737 | - | 118,439 |
| Total current assets | 2,145,482 | 75,678 | (64,833) | 2,156,327 |
| Restricted cash | 11,806 | - | - | 11,806 |
| Noncurrent investments | 547,673 | - | (8,500) | 539,173 |
| Noncurrent investments limited as to use | 113,526 | - | - | 113,526 |
| Property, plant, and equipment, net | 1,515,849 | 9,254 | - | 1,525,103 |
| Operating lease assets | 832,085 | 14,610 | - | 846,695 |
| Other noncurrent assets | 39,482 | 13,865 | - | 53,347 |
| Total assets | <u>\$ 5,205,903</u> | <u>\$ 113,407</u> | <u>\$ (73,333)</u> | <u>\$ 5,245,977</u> |
| Liabilities and Net Assets | | | | |
| Current liabilities: | | | | |
| Current portion of long-term debt | \$ 13,486 | \$ 835 | \$ - | \$ 14,321 |
| Intercompany payable | - | 64,833 | (64,833) | - |
| Short-term borrowings | 100,000 | - | - | 100,000 |
| Accounts payable and other accrued expenses | 289,108 | 20,054 | - | 309,162 |
| Medicare accelerated payments | 219,881 | 2,564 | - | 222,445 |
| Estimated payables under third-party programs | 45,957 | - | - | 45,957 |
| Accrued compensation and benefits | 233,971 | 4,068 | - | 238,039 |
| Current portion of operating lease liabilities | 67,089 | 2,973 | - | 70,062 |
| Current portion of deferred revenue | 4,158 | 669 | - | 4,827 |
| Current portion of medical malpractice self-insurance reserves | 12,577 | - | - | 12,577 |
| Total current liabilities | 986,227 | 95,996 | (64,833) | 1,017,390 |
| Long-term debt, net of current portion | 1,840,922 | 368 | - | 1,841,290 |
| Noncurrent portion of operating lease liabilities | 785,665 | 12,146 | - | 797,811 |
| Fair value of interest rate exchange agreements | 100,342 | - | - | 100,342 |
| Noncurrent portion of medical malpractice self-insurance reserves | 47,682 | - | - | 47,682 |
| Noncurrent portion of deferred revenue | 3,957 | 70 | - | 4,027 |
| Other noncurrent liabilities | 35,205 | 244 | - | 35,449 |
| Total liabilities | <u>3,800,000</u> | <u>108,824</u> | <u>(64,833)</u> | <u>3,843,991</u> |
| Net assets: | | | | |
| Net assets without donor restrictions controlled by Vanderbilt University Medical Center | 1,219,348 | (2,052) | (8,500) | 1,208,796 |
| Net assets without donor restrictions related to noncontrolling interests | - | 6,635 | - | 6,635 |
| Total net assets without donor restrictions | 1,219,348 | 4,583 | (8,500) | 1,215,431 |
| Net assets with donor restrictions | 186,555 | - | - | 186,555 |
| Total net assets | <u>1,405,903</u> | <u>4,583</u> | <u>(8,500)</u> | <u>1,401,986</u> |
| Total liabilities and net assets | <u>\$ 5,205,903</u> | <u>\$ 113,407</u> | <u>\$ (73,333)</u> | <u>\$ 5,245,977</u> |

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

Vanderbilt University Medical Center
Consolidating Statement of Operations
Year Ended June 30, 2021

| (\$ in thousands) | Obligated Group | Nonobligated Entity | Eliminations | Consolidated |
|---|--------------------|------------------------|-----------------|-------------------|
| Operating revenues | | | | |
| Patient service revenue | \$ 4,545,568 | \$ 146,246 | \$ - | \$ 4,691,814 |
| Academic and research revenue | 613,820 | 791 | - | 614,611 |
| Other operating revenue | 198,001 | 49,401 | (19,198) | 228,204 |
| Total operating revenues | <u>5,357,389</u> | <u>196,438</u> | <u>(19,198)</u> | <u>5,534,629</u> |
| Operating expenses | | | | |
| Salaries, wages, and benefits | 2,736,936 | 99,608 | - | 2,836,544 |
| Supplies and drugs | 1,195,859 | 21,117 | (773) | 1,216,203 |
| Facilities and equipment | 283,721 | 13,149 | (122) | 296,748 |
| Services and other | 749,557 | 64,033 | (18,303) | 795,287 |
| Depreciation and amortization | 147,977 | 3,477 | - | 151,454 |
| Interest | 60,400 | 130 | - | 60,530 |
| Total operating expenses | <u>5,174,450</u> | <u>201,514</u> | <u>(19,198)</u> | <u>5,356,766</u> |
| Income from operations | <u>182,939</u> | <u>(5,076)</u> | <u>-</u> | <u>177,863</u> |
| Nonoperating revenues and expenses | | | | |
| Income from investments | 68,201 | - | - | 68,201 |
| Gift income | 19,104 | - | - | 19,104 |
| (Losses) earnings of unconsolidated organizations | (683) | 8,783 | - | 8,100 |
| Unrealized gain on interest rate exchange agreements, net of cash settlements | <u>17,372</u> | <u>-</u> | <u>-</u> | <u>17,372</u> |
| Total nonoperating revenues and expenses | <u>103,994</u> | <u>8,783</u> | <u>-</u> | <u>112,777</u> |
| Excess of revenues over expense | 286,933 | 3,707 | - | 290,640 |
| Excess of revenues over expense attributable to noncontrolling interests | <u>-</u> | <u>(6,295)</u> | <u>-</u> | <u>(6,295)</u> |
| Excess of revenues over expenses attributable to VUMC | <u>\$ 286,933</u> | <u>\$ (2,588)</u> | <u>\$ -</u> | <u>\$ 284,345</u> |

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

Vanderbilt University Medical Center
Consolidating Statement of Operations
Year Ended June 30, 2020

| (\$ in thousands) | Obligated Group | Nonobligated Entity | Eliminations | Consolidated |
|---|--------------------|------------------------|-----------------|-------------------|
| Operating revenues | | | | |
| Patient service revenue | \$ 3,939,273 | \$ 92,447 | \$ - | \$ 4,031,720 |
| Academic and research revenue | 552,996 | (174) | - | 552,822 |
| Other operating revenue | 272,110 | 55,375 | (26,342) | 301,143 |
| Total operating revenues | <u>4,764,379</u> | <u>147,648</u> | <u>(26,342)</u> | <u>4,885,685</u> |
| Operating expenses | | | | |
| Salaries, wages, and benefits | 2,428,566 | 67,229 | - | 2,495,795 |
| Supplies and drugs | 1,038,785 | 8,507 | (894) | 1,046,398 |
| Facilities and equipment | 265,294 | 8,204 | (93) | 273,405 |
| Services and other | 702,869 | 62,741 | (25,355) | 740,255 |
| Depreciation and amortization | 124,953 | 1,701 | - | 126,654 |
| Interest | 60,714 | 57 | - | 60,771 |
| Total operating expenses | <u>4,621,181</u> | <u>148,439</u> | <u>(26,342)</u> | <u>4,743,278</u> |
| Income from operations | <u>143,198</u> | <u>(791)</u> | <u>-</u> | <u>142,407</u> |
| Nonoperating revenues and expenses | | | | |
| Income from investments | 27,224 | - | - | 27,224 |
| Gift income | 20,702 | - | - | 20,702 |
| (Losses) earnings of unconsolidated organizations | (1,063) | 5,928 | - | 4,865 |
| Unrealized loss on interest rate exchange agreements, net of cash settlements | <u>(37,152)</u> | <u>-</u> | <u>-</u> | <u>(37,152)</u> |
| Total nonoperating revenues and expenses | <u>9,711</u> | <u>5,928</u> | <u>-</u> | <u>15,639</u> |
| Excess of revenues over expense | 152,909 | 5,137 | - | 158,046 |
| Excess of revenues over expense attributable to noncontrolling interests | <u>-</u> | <u>(4,074)</u> | <u>-</u> | <u>(4,074)</u> |
| Excess of revenues over expenses attributable to VUMC | <u>\$ 152,909</u> | <u>\$ 1,063</u> | <u>\$ -</u> | <u>\$ 153,972</u> |

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

Vanderbilt University Medical Center
Note to Supplementary Information
June 30, 2021 and 2020

1. Basis of Presentation

As discussed in Note 11, Long-Term Debt, each of the bonds and notes comprising the Series Debt represent separate obligations under an MTI structure. All debt issued under the MTI are general obligations of the obligated group, which, for purposes of the preceding consolidating financial statements comprises VUMC and its affiliates, as described in Note 1, Description of Organization, except for VHS, HPS, NashBio, VTHH, VBCH, and VMH, which are nonobligated entities.

The consolidating information is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position and the results of operations of the individual companies.

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

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