

## **HCD Inc**

### **Excerpts From Financial Statements**

This document includes excerpts from a real set of financial statements from a company in the healthcare sector. The firm describes itself as a diversified healthcare services company. They operate regionally focused, integrated healthcare delivery networks, primarily in large urban and suburban markets in the United States. At the end of their most recent fiscal year, they operated 79 hospitals, 20 short-stay surgical hospitals, over 470 outpatient centers, and nine facilities in other countries.

The following pages include the Balance Sheet, Income Statement (they call it the Statement of Operations), and Statement of Cash Flows. Parts of their footnotes describing their revenues and issues related to the collectability of their accounts are also included.

**HCD, INC**  
**CONSOLIDATED BALANCE SHEETS**  
Dollars in Millions

|  | December 31,<br>20x2 | December 31,<br>20x1 |
|--|----------------------|----------------------|
| <b>ASSETS</b>  |                      |                      |
| <b>Current assets:</b>   |                      |                      |
| Cash and cash equivalents  | \$ 716               | \$ 356               |
| Accounts receivable, less allowance for doubtful accounts (\$1,031 at December 31, 20x2 and \$887 at December 31, 20x1)  | 2,897                | 2,704                |
| Inventories of supplies, at cost   | 326                  | 309                  |
| Income tax receivable  | 4                    | 7                    |
| Assets held for sale   | 29                   | 550                  |
| Other current assets   | 1,285                | 1,245                |
| <b>Total current assets</b>  | <b>5,257</b>         | <b>5,171</b>         |
| Investments and other assets   | 1,250                | 1,175                |
| Deferred income taxes  | 871                  | 776                  |
| Property and equipment, at cost, less accumulated depreciation and amortization (\$4,974 at December 31, 20x2 and \$4,323 at December 31, 20x1)                  | 8,053                | 7,915                |
| Goodwill   | 7,425                | 6,970                |
| Other intangible assets, at cost, less accumulated amortization (\$772 at December 31, 20x2 and \$659 at December 31, 20x1)                                      | 1,845                | 1,675                |
| <b>Total assets</b>  | <b>\$ 24,701</b>     | <b>\$ 23,682</b>     |
| <b>LIABILITIES AND EQUITY</b>  |                      |                      |
| <b>Current liabilities:</b>  |                      |                      |
| Current portion of long-term debt  | \$ 191               | \$ 127               |
| Accounts payable   | 1,329                | 1,380                |
| Accrued compensation and benefits  | 872                  | 880                  |
| Professional and general liability reserves  | 181                  | 177                  |
| Accrued interest payable   | 210                  | 205                  |
| Liabilities held for sale  | 9                    | 101                  |
| Accrued legal settlement costs   | 8                    | 294                  |
| Other current liabilities  | 1,234                | 1,144                |
| <b>Total current liabilities</b>   | <b>4,034</b>         | <b>4,308</b>         |
| Long-term debt, net of current portion   | 15,064               | 14,383               |
| Professional and general liability reserves  | 613                  | 578                  |
| Defined benefit plan obligations   | 626                  | 595                  |
| Deferred income taxes  | 279                  | 37                   |
| Other long-term liabilities  | 610                  | 557                  |
| <b>Total liabilities</b>   | <b>21,226</b>        | <b>20,458</b>        |
| Commitments and contingencies  |                      |                      |
| Redeemable noncontrolling interests in equity of consolidated subsidiaries   | 2,393                | 2,266                |
| <b>Equity:</b>   |                      |                      |
| <b>Shareholders' equity:</b>   |                      |                      |
| Common stock, \$0.05 par value; authorized 262,500,000 shares; 148,106,249 shares issued at December 31, 20x2 and 146,920,454 shares issued at December 31, 20x1 | 7                    | 7                    |
| Additional paid-in capital   | 4,827                | 4,815                |
| Accumulated other comprehensive loss   | (258)                | (164)                |
| Accumulated deficit  | (1,742)              | (1,550)              |
| Common stock in treasury, at cost, 48,420,650 shares at December 31, 20x2 and 48,425,298 shares at December 31, 20x1   | (2,417)              | (2,417)              |
| <b>Total shareholders' equity</b>  | <b>417</b>           | <b>691</b>           |
| <b>Noncontrolling interests</b>  | <b>665</b>           | <b>267</b>           |
| <b>Total equity</b>  | <b>1,082</b>         | <b>958</b>           |
| <b>Total liabilities and equity</b>  | <b>\$ 24,701</b>     | <b>\$ 23,682</b>     |

See accompanying Notes to Consolidated Financial Statements.

**HCD, INC**  
**CONSOLIDATED STATEMENTS OF**  
**OPERATIONS** Dollars in Millions

|  | Years Ended December 31, |               |               |
|--|--------------------------|---------------|---------------|
|  | 20x2                     | 20x1          | 20x0          |
| <b>Net operating revenues:</b>   |                          |               |               |
| Net operating revenues before provision for doubtful accounts                | \$ 21,070                | \$ 20,111     | \$ 17,908     |
| Less: Provision for doubtful accounts  | 1,449                    | 1,477         | 1,305         |
| <b>Net operating revenues</b>  | <b>19,621</b>            | <b>18,634</b> | <b>16,603</b> |
| <b>Equity in earnings of unconsolidated affiliates</b>                       | <b>131</b>               | <b>99</b>     | <b>12</b>     |
| <b>Operating expenses:</b>   |                          |               |               |
| Salaries, wages and benefits   | 9,356                    | 9,011         | 8,023         |
| Supplies   | 3,124                    | 2,963         | 2,630         |
| Other operating expenses, net  | 4,891                    | 4,555         | 4,114         |
| Electronic health record incentives  | (32)                     | (72)          | (104)         |
| Depreciation and amortization  | 850                      | 797           | 849           |
| Impairment and restructuring charges, and acquisition-related costs          | 202                      | 318           | 153           |
| Litigation and investigation costs   | 293                      | 291           | 25            |
| Gains on sales, consolidation and deconsolidation of facilities              | (151)                    | (186)         | —             |
| <b>Operating income</b>  | <b>1,219</b>             | <b>1,056</b>  | <b>925</b>    |
| Interest expense   | (979)                    | (912)         | (754)         |
| Loss from early extinguishment of debt                                       | —                        | (1)           | (24)          |
| Investment earnings  | 8                        | 1             | —             |
| <b>Net income from continuing operations, before income taxes</b>            | <b>248</b>               | <b>144</b>    | <b>147</b>    |
| Income tax expense   | (67)                     | (68)          | (49)          |
| <b>Net income from continuing operations, before discontinued operations</b> | <b>181</b>               | <b>76</b>     | <b>98</b>     |
| <b>Discontinued operations:</b>  |                          |               |               |
| Net loss from operations   | (6)                      | (5)           | (17)          |
| Litigation and investigation (costs) benefit                                 | —                        | 8             | (18)          |
| Income tax benefit (expense)   | 1                        | (1)           | 13            |
| <b>Net income (loss) from discontinued operations</b>                        | <b>(5)</b>               | <b>2</b>      | <b>(22)</b>   |
| <b>Net income</b>  | <b>176</b>               | <b>78</b>     | <b>76</b>     |

**HCD, INC**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
Dollars in Millions

|  | Years Ended December 31, |                |                |
|--|--------------------------|----------------|----------------|
|  | 20x2                     | 20x1           | 20x0           |
| <b>Net income</b>  | <b>\$ 176</b>            | <b>\$ 78</b>   | <b>\$ 76</b>   |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b>                   |                          |                |                |
| Depreciation and amortization  | 850                      | 797            | 849            |
| Provision for doubtful accounts  | 1,449                    | 1,477          | 1,305          |
| Deferred income tax expense  | 41                       | 42             | 30             |
| Stock-based compensation expense   | 68                       | 69             | 51             |
| Impairment and restructuring charges, and acquisition-related costs  | 202                      | 318            | 153            |
| Litigation and investigation costs   | 293                      | 291            | 25             |
| Loss from early extinguishment of debt   | —                        | 1              | 24             |
| Gains on sales, consolidation and deconsolidation of facilities  | (151)                    | (186)          | —              |
| Equity in earnings of unconsolidated affiliates, net of distributions received                             | (13)                     | (99)           | (10)           |
| Amortization of debt discount and debt issuance costs  | 41                       | 41             | 28             |
| Pre-tax (income) loss from discontinued operations   | 6                        | (3)            | 35             |
| Other items, net   | (1)                      | 59             | (30)           |
| <b>Changes in cash from operating assets and liabilities:</b>  |                          |                |                |
| Accounts receivable  | (1,604)                  | (1,632)        | (1,896)        |
| Inventories and other current assets   | (83)                     | (130)          | (314)          |
| Income taxes   | (8)                      | 18             | 3              |
| Accounts payable, accrued expenses and other current liabilities   | (51)                     | 68             | 505            |
| Other long-term liabilities  | 40                       | 38             | 44             |
| <b>Payments for restructuring charges, acquisition-related costs, and litigation costs and settlements</b> | <b>(691)</b>             | <b>(200)</b>   | <b>(168)</b>   |
| <b>Net cash used in operating activities from discontinued operations, excluding income taxes</b>          | <b>(6)</b>               | <b>(21)</b>    | <b>(23)</b>    |
| <b>Net cash provided by operating activities</b>   | <b>558</b>               | <b>1,026</b>   | <b>687</b>     |
| <b>Cash flows from investing activities:</b>   |                          |                |                |
| Purchases of property and equipment — continuing operations  | (875)                    | (842)          | (933)          |
| Purchases of businesses or joint venture interests, net of cash acquired                                   | (117)                    | (940)          | (428)          |
| Proceeds from sales of facilities and other assets   | 573                      | 549            | 6              |
| Proceeds from sales of marketable securities, long-term investments and other assets                       | 62                       | 60             | 52             |
| Purchases of equity investments  | (39)                     | (134)          | (12)           |
| Other assets   | (31)                     | (4)            | (8)            |
| Other items, net   | (3)                      | (6)            | 1              |
| <b>Net cash used in investing activities</b>   | <b>(430)</b>             | <b>(1,317)</b> | <b>(1,322)</b> |
| <b>Cash flows from financing activities:</b>   |                          |                |                |
| Repayments of borrowings under credit facility   | (1,895)                  | (2,815)        | (2,430)        |
| Proceeds from borrowings under credit facility   | 1,895                    | 2,595          | 2,245          |
| Repayments of other borrowings   | (154)                    | (2,049)        | (683)          |
| Proceeds from other borrowings   | 760                      | 3,158          | 1,608          |
| Repurchases of common stock  | —                        | (40)           | —              |
| Debt issuance costs  | (12)                     | (80)           | (27)           |
| Distributions paid to noncontrolling interests   | (218)                    | (110)          | (45)           |
| Proceeds from sale of noncontrolling interests   | 22                       | 11             | —              |
| Purchase of noncontrolling interests   | (186)                    | (268)          | —              |
| Proceeds from exercise of stock options  | 4                        | 15             | 26             |
| Other items, net   | 16                       | 37             | 21             |
| <b>Net cash provided by financing activities</b>   | <b>232</b>               | <b>454</b>     | <b>715</b>     |
| Net increase in cash and cash equivalents  | 360                      | 163            | 80             |
| Cash and cash equivalents at beginning of period   | 356                      | 193            | 113            |
| <b>Cash and cash equivalents at end of period</b>  | <b>\$ 716</b>            | <b>\$ 356</b>  | <b>\$ 193</b>  |
| <b>Supplemental disclosures:</b>   |                          |                |                |
| Interest paid, net of capitalized interest   | \$ (932)                 | \$ (859)       | \$ (726)       |
| Income tax payments, net   | \$ (33)                  | \$ (7)         | \$ (8)         |

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## HCD, INC - NOTES TO FINANCIAL STATEMENTS

### *Net Operating Revenues Before Provision for Doubtful Accounts*

We recognize net operating revenues before provision for doubtful accounts in the period in which our services are performed. Net operating revenues before provision for doubtful accounts primarily consist of net patient service revenues that are recorded based on established billing rates (i.e., gross charges), less estimated discounts for contractual and other allowances, principally for patients covered by Medicare, Medicaid, managed care and other health plans, as well as certain uninsured patients under our *Compact with Uninsured Patients* ("Compact") and other uninsured discount and charity programs.

Hospitals are typically paid amounts that are negotiated with insurance companies or are set by the government. Revenues under the traditional fee-for-service Medicare and Medicaid programs are based primarily on prospective payment systems. Because the laws, regulations, instructions and rule interpretations governing Medicare and Medicaid reimbursement are complex and change frequently, the estimates recorded by us could change by material amounts.

Revenues under managed care plans are based primarily on payment terms involving predetermined rates per diagnosis, per-diem rates, discounted fee-for-service rates and/or other similar contractual arrangements. These revenues are also subject to review and possible audit by the payers, which can take several years before they are completely resolved. The payers are billed for patient services on an individual patient basis.

We also provide charity care to patients who are financially unable to pay for the healthcare services they receive. Most patients who qualify for charity care are charged a per-diem amount for services received, subject to a cap. Except for the per-diem amounts, our policy is not to pursue collection of amounts determined to qualify as charity care; therefore, we do not report these amounts in net operating revenues or in provision for doubtful accounts. Patient advocates from Conifer's Medical Eligibility Program screen patients in the hospital to determine whether those patients meet eligibility requirements for financial assistance programs. They also expedite the process of applying for these government programs.

The table below shows the sources of net operating revenues before provision for doubtful accounts from continuing operations:

|  | Years Ended December 31, |                  |                  |
|--|--------------------------|------------------|------------------|
|  | 20x2                     | 20x1             | 20x0             |
| <b>General Hospitals:</b>  |                          |                  |                  |
| Medicare   | \$ 3,374                 | \$ 3,403         | \$ 3,395         |
| Medicaid   | 1,346                    | 1,451            | 1,482            |
| Managed care   | 10,126                   | 10,098           | 9,027            |
| Indemnity, self-pay and other  | 1,621                    | 1,726            | 1,561            |
| Acute care hospitals — other revenue                                 | 21                       | 63               | 53               |
| <b>Other:</b>  |                          |                  |                  |
| Other operations   | 4,582                    | 3,370            | 2,390            |
| <b>Net operating revenues before provision for doubtful accounts</b> | <b>\$ 21,070</b>         | <b>\$ 20,111</b> | <b>\$ 17,908</b> |

### ***Provision for Doubtful Accounts***

Although outcomes vary, our policy is to attempt to collect amounts due from patients, including co-pays and deductibles due from patients with insurance, at the time of service while complying with all federal and state statutes and regulations, including, but not limited to, the Emergency Medical Treatment and Active Labor Act (“EMTALA”). Generally, as required by EMTALA, patients may not be denied emergency treatment due to inability to pay. Therefore, services, including the legally required medical screening examination and stabilization of the patient, are performed without delaying to obtain insurance information.

We provide for an allowance against accounts receivable that could become uncollectible by establishing an allowance to reduce the carrying value of such receivables to their estimated net realizable value. Generally, we estimate this allowance based on the aging of our accounts receivable by hospital, our historical collection experience by hospital and for each type of payer over a look-back period, and other relevant factors. A significant portion of our provision for doubtful accounts relates to self-pay patients, as well as co-pays and deductibles owed to us by patients with insurance. Payment pressure from managed care payers also affects our provision for doubtful accounts. We typically experience ongoing managed care payment delays and disputes; however, we continue to work with these payers to obtain adequate and timely reimbursement for our services. There are various factors that can impact collection trends, such as changes in the economy, which in turn have an impact on unemployment rates and the number of uninsured and underinsured patients, the volume of patients through our emergency departments, the increased burden of co-pays and deductibles to be made by patients with insurance, and business practices related to collection efforts. These factors continuously change and can have an impact on collection trends and our estimation proce

patient co-pays and deductibles. The table below shows the net accounts receivable and allowance for doubtful accounts by payer at December 31, 20x2 and December 31, 20x1:

|  | December 31, 20x2  |                                 |                 | December 31, 20x1  |                                 |                 |
|--|--|---------------------------------|-----------------|--|---------------------------------|-----------------|
|  | Accounts Receivable Before Allowance for Doubtful Accounts | Allowance for Doubtful Accounts | Net             | Accounts Receivable Before Allowance for Doubtful Accounts | Allowance for Doubtful Accounts | Net             |
| Medicare   | \$ 404   | \$ —                            | \$ 404          | \$ 360   | \$ —                            | \$ 360          |
| Medicaid   | 46   | —                               | 46              | 70   | —                               | 70              |
| Net cost report settlements payable and valuation allowances | (14)   | —                               | (14)            | (42)   | —                               | (42)            |
| Managed care   | 1,965  | 175                             | 1,790           | 1,715  | 126                             | 1,589           |
| Self-pay uninsured   | 488  | 442                             | 46              | 509  | 436                             | 73              |
| Self-pay balance after insurance                             | 211  | 155                             | 56              | 208  | 142                             | 66              |
| Estimated future recoveries                                  | 141  | —                               | 141             | 144  | —                               | 144             |
| Other payers   | 458  | 216                             | 242             | 442  | 166                             | 276             |
| Total Hospital Operations and other                          | 3,699  | 988                             | 2,711           | 3,406  | 870                             | 2,536           |
| Ambulatory Care  | 227  | 43                              | 184             | 182  | 17                              | 165             |
| Total discontinued operations                                | 2  | —                               | 2               | 3  | —                               | 3               |
|  | <b>\$ 3,928</b>  | <b>\$ 1,031</b>                 | <b>\$ 2,897</b> | <b>\$ 3,591</b>  | <b>\$ 887</b>                   | <b>\$ 2,704</b> |

A significant portion of our provision for doubtful accounts relates to self-pay patients, as well as co-pays and deductibles owed to us by patients with insurance. Collection of accounts receivable has been a key area of focus, particularly over the past several years. At December 31, 20x2, our Hospital Operations and other segment collection rate on self-pay accounts was approximately 26.1%. Our self-pay collection rate includes payments made by patients, including co-pays and deductibles paid by patients with insurance. Based on our accounts receivable from self-pay patients and co-pays and deductibles owed to us by patients with insurance at December 31, 20x2, a 10% decrease or increase in our self-pay collection rate, or approximately 3%, which we believe could be a reasonably likely change, would result in an unfavorable or favorable adjustment to provision for doubtful accounts of approximately \$9 million.

Payment pressure from managed care payers also affects our provision for doubtful accounts. We typically experience ongoing managed care payment delays and disputes; however, we continue to work with these payers to obtain adequate and timely reimbursement for our services. Our estimated Hospital Operations and other segment collection rate from managed care payers was approximately 97.8% at December 31, 20x2.

We manage our provision for doubtful accounts using hospital-specific goals and benchmarks such as (1) total cash collections, (2) point-of-service cash collections, (3) accounts receivable days outstanding (“AR Days”), and (4) accounts receivable by aging category. The following tables present the approximate aging by payer of our net accounts receivable from the continuing operations of our Hospital Operations and other segment of \$2.725 billion and \$2.578 billion at December 31, 20x2 and 20x1, respectively, excluding cost report settlements payable and valuation allowances of \$14 million and \$42 million at December 31, 20x2 and 20x1, respectively:

|               | December 31, 20x2 |              |              |                               |              |
|---------------|-------------------|--------------|--------------|-------------------------------|--------------|
|               | Medicare          | Medicaid     | Managed Care | Indemnity, Self-Pay and Other | Total        |
| 0-60 days     | 92 %              | 75 %         | 61 %         | 24 %                          | 60 %         |
| 61-120 days   | 5 %               | 15 %         | 15 %         | 14 %                          | 13 %         |
| 121-180 days  | 2 %               | 4 %          | 8 %          | 10 %                          | 6 %          |
| Over 180 days | 1 %               | 6 %          | 16 %         | 52 %                          | 21 %         |
| <b>Total</b>  | <b>100 %</b>      | <b>100 %</b> | <b>100 %</b> | <b>100 %</b>                  | <b>100 %</b> |