

FINANCIAL STATEMENTS

Indiana University Health Foundation, Inc.
Years Ended December 31, 2019 and 2018
With Report of Independent Auditors

Ernst & Young LLP



Indiana University Health Foundation, Inc.

Financial Statements

Years Ended December 31, 2019 and 2018

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Report of Independent Auditors

The Board of Directors
Indiana University Health Foundation, Inc.

We have audited the accompanying financial statements of Indiana University Health Foundation, Inc., which comprise the statements of financial position as of December 31, 2019 and 2018, and the related statements of activities and functional expenses and cash flows for the years then ended, and the related notes to the financial statements.

Management’s Responsibility for the Financial Statements

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

Auditor’s Responsibility

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

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

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



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Indiana University Health Foundation, Inc. at December 31, 2019 and 2018, and the 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

May 5, 2020

Indiana University Health Foundation, Inc.

Statements of Financial Position

	December 31	
	2019	2018
Assets		
Current assets:		
Cash and cash equivalents	\$ 11,033,533	\$ 27,949,170
Current portion of assets limited as to use	2,565,561	1,735,847
Accounts receivable and other	641,629	808,448
Contributions receivable, net	1,698,661	817,488
Total current assets	<u>15,939,384</u>	31,310,953
Assets limited as to use	127,346,005	96,923,080
Other assets:		
Beneficial interest in perpetual trusts	9,858,779	8,527,165
Beneficial interest in charitable remainder trusts	6,174,282	4,765,506
Contributions receivable, net	4,901,333	3,272,100
Other	177,132	1,106,264
Total other assets	<u>21,111,526</u>	17,671,035
Total assets	<u><u>\$ 164,396,915</u></u>	<u>\$ 145,905,068</u>
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued expenses	\$ 5,949,030	\$ 2,268,992
Funds held for others	335,000	—
Due on split interest agreements	238,847	220,244
Total current liabilities	<u>6,522,877</u>	2,489,236
Noncurrent liabilities:		
Due on split interest agreements	2,634,078	2,493,923
Funds held for others	760,000	—
Total noncurrent liabilities	<u>3,394,078</u>	2,493,923
Total liabilities	<u>9,916,955</u>	4,983,159
Net assets:		
Without donor restriction	74,792,829	67,404,995
With donor restriction	79,687,131	73,516,914
Total net assets	<u>154,479,960</u>	140,921,909
Total liabilities and net assets	<u><u>\$ 164,396,915</u></u>	<u>\$ 145,905,068</u>

See accompanying notes.

Indiana University Health Foundation, Inc.

Statements of Activities and Functional Expenses

Year Ended December 31, 2019

	Without Donor Restriction	With Donor Restriction	Total
Revenue and other support:			
Contributions and grants	\$ 981,170	\$ 5,656,179	\$ 6,637,349
In-kind revenues	8,722,194	13,039	8,735,233
Professional fees income	1,961,131	-	1,961,131
Registration fees and dues income	15,219	-	15,219
Event income	694,215	-	694,215
Clinical research support	247,011	-	247,011
Other	346,779	-	346,779
Net assets released from restriction	4,111,590	(4,111,590)	-
Total revenue and other support	17,079,309	1,557,628	18,636,937
Expenses:			
Program services			
Program support	11,050,221	-	11,050,221
Administrative support	1,487,439	-	1,487,439
Total program services	12,537,660	-	12,537,660
Management and general			
Salaries and benefits	1,067,304	-	1,067,304
Other operating and facility	885,047	-	885,047
Total management and general	1,952,351	-	1,952,351
Fundraising			
Fundraising salaries and benefits	2,788,423	-	2,788,423
Special events	1,618,631	-	1,618,631
Other fundraising	992,203	-	992,203
Total fundraising	5,399,257	-	5,399,257
Total expenses	19,889,268	-	19,889,268
Excess of (expenses over revenue and other support) or revenue and other support over expenses	(2,809,959)	1,557,628	(1,252,331)
Other gains (losses):			
Investment income, net	11,975,430	1,984,145	13,959,575
Change in value of split interest agreements	13,921	2,567,711	2,581,632
Loss on uncollectible contributions	(17,677)	(2,029)	(19,706)
Other	(61,779)	62,762	983
Total other gains, net	11,909,895	4,612,589	16,522,484
Transfer to IU Health, Inc.	(1,712,102)	-	(1,712,102)
Increase in net assets	7,387,834	6,170,217	13,558,051
Net assets at beginning of year	67,404,995	73,516,914	140,921,909
Net assets at end of year	\$ 74,792,829	\$ 79,687,131	\$ 154,479,960

See accompanying notes.

Indiana University Health Foundation, Inc.

Statements of Activities and Functional Expenses

Year Ended December 31, 2018

	Without Donor Restriction	With Donor Restriction	Total
Revenue and other support:			
Contributions and grants	\$ 1,977,923	\$ 7,142,082	\$ 9,120,005
In-kind revenues	7,006,465	-	7,006,465
Professional fees income	1,791,782	-	1,791,782
Registration fees and dues	446,641	-	446,641
Event income	310,066	-	310,066
Clinical research support	255,314	-	255,314
Other	188,699	-	188,699
Net assets released from restriction	4,355,360	(4,355,360)	-
Total revenue and other support	16,332,250	2,786,722	19,118,972
Expenses:			
Program services			
Program support	9,412,877	-	9,412,877
Administrative support	1,380,309	-	1,380,309
Total program services	10,793,186	-	10,793,186
Management and general			
Salaries and benefits	897,695	-	897,695
Other operating and facility	1,124,845	-	1,124,845
Total management and general	2,022,540	-	2,022,540
Fundraising			
Fundraising salaries and benefits	2,211,096	-	2,211,096
Special events	1,540,701	-	1,540,701
Other fundraising	114,658	-	114,658
Total fundraising	3,866,455	-	3,866,455
Total expenses	16,682,181	-	16,682,181
Excess of (expenses over revenue and other support) or revenue and other support over expenses	(349,931)	2,786,722	2,436,791
Other (losses) gains:			
Investment loss, net	(2,502,228)	-	(2,502,228)
Change in value of split interest agreements	(4,232)	(872,302)	(876,534)
Loss on uncollectible contributions	(10,512)	(63,771)	(74,283)
Other	119,269	90,153	209,422
Total other losses, net	(2,397,703)	(845,920)	(3,243,623)
Transfer from IU Health, Inc.	933,015	-	933,015
(Decrease) increase in net assets	(1,814,619)	1,940,802	126,183
Net assets at beginning of year	69,219,614	71,576,112	140,795,726
Net assets at end of year	\$ 67,404,995	\$ 73,516,914	\$ 140,921,909

See accompanying notes.

Indiana University Health Foundation, Inc.

Statements of Cash Flows

	Year Ended December 31	
	2019	2018
Operating activities		
Change in net assets	\$ 13,558,051	\$ 126,183
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Assets limited as to use	(31,252,639)	27,156,543
Change in beneficial interests in trusts	(2,740,390)	(1,550,202)
New beneficial interests in trusts	–	(1,475,760)
Loss on provision for uncollectible contributions	19,706	74,283
Depreciation	–	11,250
Loss on disposal of property and equipment	–	16,375
Changes in operating assets and liabilities:		
Contributions receivable, net	(2,530,112)	(2,576,241)
Accounts receivable and other	166,819	(492,379)
Other assets	929,132	(1,001,131)
Due on split-interest agreements	158,758	2,426,738
Funds held for others	1,095,000	–
Accounts payable and accrued expenses	3,680,038	1,816,506
Net cash (used in) provided by operating activities	(16,915,637)	24,532,165
Net change in cash and cash equivalents	(16,915,637)	24,532,165
Cash and cash equivalents at beginning of year	27,949,170	3,417,005
Cash and cash equivalents at end of year	\$ 11,033,533	\$ 27,949,170

See accompanying notes.

Indiana University Health Foundation, Inc.

Notes to Financial Statements

December 31, 2019 and 2018

1. Organization and Summary of Significant Accounting Policies

Description of Organization

Indiana University Health Foundation, Inc. (the Foundation), a not-for-profit corporation, is an educational and charitable corporation which aids and supports Indiana University Health, Inc. (IU Health) and all hospitals within the State of Indiana that are operated, supervised, or controlled directly by or in connection with IU Health. IU Health is the sole member of the Foundation and approves the appointment of all members of the Foundation's Board of Directors.

Nature of Operations

The Foundation operates to harness the positive impact of philanthropy in support of the IU Health vision to make Indiana one of the nation's healthiest states. The Foundation's activities and policies support this vision by championing IU Health as a health care change agent, ensuring gifts are managed and stewarded in support of the IU Health vision, and by serving as a catalyst for fundraising.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents

Investments in highly liquid instruments with an original maturity of three months or less when purchased, excluding assets limited as to use, are considered by management to be cash and cash equivalents. Investments include money market funds, including treasury and agency money market funds that are considered by management to be cash equivalents. Such instruments, as well as bank deposits, are potentially subject to concentrations of credit risk. In order to mitigate such risk, cash and cash equivalent instruments are invested in high-credit-quality instruments.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Contributions

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is made. Contributions receivable are discounted based on the nature of the individual pledge using a discount rate commensurate with the risks involved. Discount rates reflect the economic conditions of the year in which the pledge is made. Amortization of the discount is included as a reduction to contributions and grants within the statements of activities and functional expenses. Conditional promises to give are reported at fair value at the date the gift is made and the conditions are satisfied.

Promises to give with donor restrictions that limit the use of the donated assets are reported as net assets with donor restrictions until the donor restriction expires. If a restriction is fulfilled in the same time period in which the contribution is received, the contribution is reported as with donor restriction and released from restriction.

Allowance for Uncollectible Contributions

An allowance for uncollectible contributions is recorded based upon the Foundation's historical losses, specific circumstances, and economic conditions.

Assets Limited as to Use

Substantially all of the Foundation's investments are in a pooled structure (the IU Health Pool) with IU Health's assets, where the Foundation's share in the IU Health Pool is reported as assets limited as to use in the statements of financial position.

Gains and losses on investments are allocated to the Foundation based on its investment balance relative to the total investment balance of the IU Health Pool. Investment income (loss), net includes realized and unrealized gains and losses on investments, dividends, and interest, and are included in the other gains (losses), net in the statements of activities and functional expenses.

Investments in the IU Health Pool consist of cash and short-term, liquid investments, debt securities (including asset-backed securities, bank loans, corporate debt, government and agencies, and bond funds) and domestic and international equity securities, which can be in the form of individual securities or funds, as well as commodities, hedge funds, and private funds. Investments in equity and debt securities and commodities are measured at fair value based on Financial

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, *Fair Value Measurement*. The value of alternatives held within the IU Health Pool is recorded on an equity method basis and reflect the net contribution to the alternative investment and an allocated share of the realized and unrealized investment income and expenses. The values provided by the respective partnerships are based on historical cost, appraisals, third-party pricing sources, and other estimates that require varying degrees of judgments.

The IU Health Pool is structured in a manner that endeavors to take a prudent amount of investment risk in its pursuit of the return objectives. Short-term volatility and uncertainty of investment results are recognized as real risks that are managed through diversification and specific asset allocation strategies. The IU Health Pool invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the financial statements.

Net Assets

Net assets without donor restrictions do not contain either a time or purpose restriction; though, in certain cases, they may be internally designated by the Board in support of various programs.

Net assets with donor restrictions include those whose use by the Foundation has been restricted by the donor for future time periods or specific purposes and net assets restricted by donors to be maintained in perpetuity.

Expense Classification and Allocation

Expenses have been classified as program services, management and general, and fundraising in the statements of activities and functional expenses based on the nature of the actual direct expenditures and cost allocations. Certain expenses are allocated to the Foundation by IU Health, including salaries and benefits expense. These expenses are allocated on a reasonable basis that is consistently applied. Salaries and benefits are allocated based on the duties performed by each employee supporting the Foundation.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Tax Status

The IRS has determined that the Foundation is a tax-exempt organization as defined in Section 501(c)(3) of the Internal Revenue Code (IRC) and is exempt from federal and state income taxes.

The Tax Cuts and Jobs Act (TCJA) was enacted on December 22, 2017. For tax-exempt entities, the TCJA requires organizations to pay an excise tax on compensation above certain thresholds, and record income or losses for tax determination purposes from unrelated business activities on an activity-by-activity basis, among other provisions. Proposed regulations and interim guidance, necessary for implementation, have been issued on most aspects of the TCJA. It is expected that proposed regulations will be issued as final regulations by the IRS in 2020. As of and for the years ended December 31, 2019 and 2018, the Foundation has determined the impacts of the TCJA to be immaterial to its audited financial statements. The Foundation will continue to refine its calculations in future periods, as additional regulations and guidance are issued by the IRS.

Subsequent Events

For the financial statements as of and for the years ended December 31, 2019, management has evaluated subsequent events through May 5, 2020, the date that these financial statements were issued.

The effects of the global viral outbreak of coronavirus disease 2019 (COVID-19) in 2020, which include significant stock market exchange volatility, various temporary business closures, and event cancellations, may impact the Foundation's fundraising activities and future support to be provided to IU Health. While the ultimate impact of these matters to the Foundation and its financial condition is presently unknown, the effects of COVID-19 could negatively impact the Foundation's financial condition.

The accompanying financial statements as of and for the year ended December 31, 2019, do not reflect the effects of these subsequent events.

Recent Accounting Pronouncements Adopted

Effective January 1, 2019, the Foundation adopted Accounting Standards Update (ASU) No. 2018-08, *Not-for-Profit Entities: Topic 958 – Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made*. This ASU provides a more robust framework

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

to determine when a transaction should be accounted for as a contribution or as an exchange transaction and provides additional guidance about how to determine whether a contribution is conditional. The Foundation adopted this guidance on a modified prospective basis, which resulted in no material changes to the presentation of the financial statements.

New Accounting Guidance Not Yet Applicable

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820): Disclosure Requirements for Fair Value Measurements*. This ASU removes and modifies certain disclosure requirements on fair value measurements to improve the effectiveness and clarify the information required in the disclosures. This ASU is effective for The Foundation beginning January 1, 2020. The Foundation expects the primary effect of this ASU will be on the disclosures in the notes to the financial statements, and it will not have a material impact on the statement of financial position or statement of activities and functional expenses.

2. Assets Limited as to Use

The following is a summary of assets limited as to use as of:

	December 31	
	2019	2018
IU Health Pool	\$ 129,911,566	\$ 98,043,919
Other investments	–	615,008
	<u>\$ 129,911,566</u>	<u>\$ 98,658,927</u>

As of December 31, 2018, other investments represent amounts due from investment managers for previously redeemed investments. These amounts were received in 2019.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

2. Assets Limited as to Use (continued)

Substantially all of the Foundation's investments are in the IU Health Pool. The carrying value of the assets held by the Foundation is an allocation of the underlying market value of the assets in the IU Health Pool based on its relative ownership percentage, which was 2.11% and 1.96% at December 31, 2019 and 2018, respectively. The Foundation's relative share of the IU Health Pool consisted of the following:

	December 31	
	2019	2018
Cash	\$ 660,227	\$ 339,871
Debt securities:		
Asset backed	1,727,589	1,026,833
Bank loans	7,423,599	4,549,597
Corporate debt	4,635,474	3,319,337
Government and agencies	6,922,905	3,265,383
Bond funds	9,331,720	7,270,479
Total debt securities	<u>30,041,287</u>	19,431,629
Equity securities:		
Domestic equities	1,208,570	1,073,024
Domestic equity funds	26,488,766	17,019,371
International equities	1,620,385	1,733,272
International equity funds	18,907,034	14,688,812
Total equity securities	<u>48,224,755</u>	34,514,479
Commodities	4,712,740	3,751,347
Alternatives:		
Hedge funds	32,943,169	28,310,807
Private funds	13,329,388	11,695,786
Total alternatives	<u>46,272,557</u>	40,006,593
Total share of IU Health Pool	129,911,566	98,043,919
Less current portion	(2,565,561)	(1,735,847)
Share of IU Health Pool less current portion	<u>\$ 127,346,005</u>	<u>\$ 96,308,072</u>

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

2. Assets Limited as to Use (continued)

The composition of investment income (loss), net allocated to the Foundation and recorded in the statements of activities and functional expenses is as follows:

	December 31	
	2019	2018
Dividends and interest	\$ 2,652,204	\$ 2,236,864
Net realized gains on investments	1,420,013	11,567,640
Net change in unrealized gains (losses) on investments	9,887,358	(16,306,732)
Total investment income (loss), net	<u>\$ 13,959,575</u>	<u>\$ (2,502,228)</u>

3. Financial Assets and Liquidity Reserves

The table below represents financial assets available for general expenditures within one year as of December 31, 2019 and 2018. The Foundation defines general expenditures as the normal expenditures related to disbursement of funds to supported organizations.

	December 31	
	2019	2018
Financial assets:		
Cash and cash equivalents	\$ 11,033,533	\$ 27,949,170
Other receivables	641,629	808,448
Contributions receivable, net	6,599,994	4,089,588
Assets limited as to use	129,911,566	98,658,927
Beneficial interest in perpetual trusts	9,858,779	8,527,165
Beneficial interest in charitable remainder trusts	6,174,282	4,765,506
Total financial assets	<u>164,219,783</u>	144,798,804
Less amounts not available within one year or not designated for general expenditures:		
Noncurrent portion of contributions receivable, net	(4,901,333)	(3,272,100)
Endowment corpus and accumulated earnings	(40,238,132)	(40,460,860)
Board designation expendable for specific purpose	(39,958,818)	(35,777,860)
Beneficial interests in perpetual trusts	(9,858,779)	(8,527,165)
Beneficial interests in charitable remainder trusts	(6,174,282)	(4,765,506)
Campaign funds	(3,371,937)	(3,249,910)
Financial assets not available for use within one year	<u>(104,503,281)</u>	<u>(96,053,401)</u>
Financial assets and liquidity resources available for general expenditures within one year	<u>\$ 59,716,502</u>	<u>\$ 48,745,403</u>

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

4. Contributions Receivable

Outstanding contributions receivable consist of the following:

	December 31	
	2019	2018
Amounts due in:		
Less than one year	\$ 1,762,215	\$ 864,755
One to five years	1,156,778	421,064
Six years or more	5,630,000	5,880,000
	8,548,993	7,165,819
Allowance for uncollectible contributions	(60,738)	(64,312)
Unamortized present value discount	(1,888,261)	(3,011,919)
Contributions receivable, net	6,599,994	4,089,588
Less current portion, net of allowance for uncollectible contributions	(1,698,661)	(817,488)
Contributions receivable, net	\$ 4,901,333	\$ 3,272,100

Contributions receivable were discounted using a discount rate of 2.0% and 3.6% for 2019 and 2018, respectively.

5. Beneficial Interest in Trusts

The Foundation is the beneficiary under charitable remainder trusts administered by the Foundation and outside parties. Under a charitable remainder trust, the donors have specified income beneficiaries to receive distributions of investment returns annually until death. Upon the death of the income beneficiaries, the remaining assets in the trusts will be distributed to the Foundation. Based on the income beneficiaries' life expectancies and discount rates of 2.0% and 3.6% at December 31, 2019 and 2018, respectively, the present value of the future benefits expected to be received by the Foundation is estimated to be \$6,174,282 and \$4,765,506 at December 31, 2019 and 2018, respectively.

The Foundation is also the beneficiary under perpetual trusts administered by outside parties. Under the terms of the trusts, the Foundation has the irrevocable right to receive amounts ranging from 10% to 100% of income earned on the trusts' assets in perpetuity, but the Foundation will never receive the assets held in trust. The fair value of these trusts is \$9,858,779 and \$8,527,165 at December 31, 2019 and 2018, respectively, which represents between 10% and 100% of the fair value of each trust's assets at year-end, depending on the percentage of trust earnings allocated to the Foundation.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

5. Beneficial Interest in Trusts (continued)

The change in the Foundation's beneficial interests in trusts is \$2,740,390 for the year ended December 31, 2019, and is reflected in the statements of activities and functional expenses as part of change in value of split-interest agreements. For the year ended December 31, 2018, the change in the Foundation's beneficial interests in trusts is \$3,025,962, of which \$4,000,000 is recorded as new gifts in the statements of activities and functional expenses as part of contributions and grants and of which \$974,036 is reflected in the statements of activities and functional expenses as part of change in the value of split-interest agreements.

6. Due on Split Interest Agreements

The Foundation is the recipient and, in some circumstances, administrator of several gift annuities and charitable remainder trusts, which require future payments to the donors or their named beneficiaries. The Foundation has recorded current and noncurrent liabilities which represent the present value of the future obligations as due on split-interest agreements in the statements of financial position. The liabilities are determined using discount rates ranging from 1.6% to 5.5%. The change in value of the Foundation's amount due on split-interest agreements for the years ended December 31, 2019 and 2018, is \$158,758 and \$2,426,738, respectively, of which \$2,524,240 was recorded net of new gifts on the statements of activities and functional expenses as part of contributions and grants for the year ended December 31, 2018.

7. Fair Value of Financial Instruments

The Foundation follows the provisions of ASC 820, which defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establishes a framework for measuring fair value. ASC 820 defines a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing an asset or a liability. As a basis for considering market participant assumptions in fair value measurements, and as noted above, ASC 820 defines a three-level fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity and the reporting entity's own assumptions about market participants. The fair value hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

7. Fair Value of Financial Instruments (continued)

The three levels in the fair value hierarchy are defined as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities as of the reporting date.
- Level 2 – Pricing inputs other than quoted prices included within Level 1 that are either directly observable or that can be derived or supported from observable data as of the reporting date.
- Level 3 – Pricing inputs include those that are significant to the fair value of the financial asset or financial liability and are not observable from objective sources. In evaluating the significance of inputs, the Indiana University Health System generally classifies assets or liabilities as Level 3 when their fair value is determined using unobservable inputs that, individually or when aggregated with other unobservable inputs, represent more than 10% of the fair value of the assets or liabilities. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

In instances where the determination of fair value measurement is based on inputs from different levels of the fair value hierarchy, the financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Foundation's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

In order to meet the requirements of ASC 820, the Foundation utilizes three basic valuation approaches to determine the fair value of its assets and liabilities required to be recorded at fair value. The first approach is the cost approach. The cost approach is generally the value a market participant would expect to replace the respective asset or liability. The second approach is the market approach. The market approach looks at what a market participant would consider an exact or similar asset or liability to that of the Foundation, including those traded on exchanges, to determine value. The third approach is the income approach. The income approach uses estimation techniques to determine the estimated future cash flows of the Foundation's respective asset or liability expected by a market participant and discounts those cash flows back to present value (typically referred to as a discounted cash flow approach).

The fair value of other investments held outside the IU Health Pool (Level 2 of the fair value hierarchy) \$615,008 at December 31, 2018.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

7. Fair Value of Financial Instruments (continued)

Based on the Foundation's method of accounting for its share of the IU Health Pool, fair value measurements disclosure under ASC 820 is not required within the notes to the financial statements. The Foundation believes the carrying amount of the IU Health Pool approximates fair value based on the nature of the underlying assets.

The fair value of the Foundation's contributions receivable, based on discounted cash flow analysis and adjusted for consideration of the donors' credit and other factors, was \$6,599,994 and \$4,089,588 at December 31, 2019 and 2018, respectively. Management believes these are Level 2 fair value measurements recorded on a nonrecurring basis.

The Foundation is an income beneficiary of charitable remainder trusts and perpetual trusts, valued at \$16,033,060 and \$13,292,671 at December 31, 2019 and 2018, respectively. The Foundation has recorded the fair value of the ownership interest of these trusts based on its pro rata share of the underlying assets or income. Based on the observable inputs, typically marketable debt or equity securities held in the irrevocable trust funds, the Foundation has determined its beneficial interests in outside trusts are within Level 2 of the fair value hierarchy.

8. Net Assets With Donor Restrictions

Net assets with donor restrictions consist of the following:

	December 31	
	2019	2018
Restricted by time:		
Beneficial interests in trusts	\$ 3,574,553	\$ 2,338,618
Restricted by purpose:		
Program services	10,126,208	6,628,214
Education and research	3,105,615	3,424,025
Capital projects	3,113,903	3,113,047
Financial assistance and other	2,740,863	2,765,072
Endowment earnings available for spending (<i>Note 9</i>)	6,929,078	7,192,928
Accumulated endowment earnings (<i>Note 9</i>)	6,277,382	6,026,831
Restricted in perpetuity:		
Endowment funds (<i>Note 9</i>)	33,897,865	33,442,433
Beneficial interests in perpetual trusts	9,858,779	8,527,165
Beneficial interests in assets held by others	62,885	58,581
	<u>\$ 79,687,131</u>	<u>\$ 73,516,914</u>

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

9. Endowment Funds

The Foundation's endowment consists of endowment funds with donor restrictions for various purposes associated with the benefit of IU Health. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

The Board of Directors of the Foundation has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as net assets with donor restrictions (i) the original value of gifts donated to the permanent endowment, (ii) the original value of subsequent gifts to the permanent endowment, and (iii) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment is also classified as net assets with donor restrictions until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by SPMIFA.

In accordance with SPMIFA, the organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (i) The duration and preservation of the fund
- (ii) The purposes of the organization and the donor-restricted endowment fund
- (iii) General economic conditions
- (iv) The possible effects of inflation and deflation
- (iv) The expected total return from income and the appreciation of investments
- (v) Other resources of the organization
- (vi) The investment policies of the organization

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

9. Endowment Funds (continued)

Investment Objectives and Policy

The Foundation's investment and spending policies for endowment assets attempt to preserve capital, maximize the return within reasonable and prudent levels of risk, and provide a return to the donor-restricted funds which the Foundation must hold in perpetuity. To satisfy long-term rate-of-return objectives, the Foundation follows the investment strategy of the IU Health Pool, a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (dividends and interest). The IU Health Pool targets a diversified asset allocation that places an emphasis on equity-based, fixed-income and alternative investments to achieve its long-term return objectives within prudent risk constraints. Investment returns are allocated to the funds periodically based on the actual returns of the investment portfolio.

Spending Policy and How the Investment Objectives Relate to Spending Policy

Distributions are made for the purposes of supporting various IU Health program services. The amount available for distribution each year is based on 4.5% of the endowment fund balance through June 30. Any unspent funds are accumulated and can be used in a later period for allowable expenditures or can be returned to the endowment fund to grow the corpus.

Additionally, the Foundation's investment policy includes a three-year commitment, expiring June 30, 2021, made by IU Health to financially support the Foundation in the form of a corpus backstop in the event of investment losses or returns below 4.5%. The backstop ensures the maintenance of purchasing power of the endowment regardless of negative developments related to investment performance, realized inflation, and distribution methodology. The backstop applies to current endowment funds and new endowment funds established over the three-year period ending June 30, 2021. In the event there is a shortfall, IU Health will make a contribution to the Foundation in the amount necessary to bring the endowment to the level of the original value of the total donor gifts multiplied by the Consumer Price Index over the three-year commitment period.

Funds With Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor of SPMIFA requires the Foundation to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

9. Endowment Funds (continued)

as net assets with donor restrictions. Unless determined a prudent use of funds, the Foundation will not appropriate endowment funds for spending until the market value of the funds exceeds the original value of the gift. As of December 31, 2019 and 2018, deficiencies resulted from disbursement of accumulated earnings in excess of historic investment earnings. At December 31, 2019, seven endowments with accumulated gift value of \$3,879,835, fair value of \$3,711,319 and deficiencies of \$168,516 are reported within net assets with donor restrictions. At December 31, 2018, five endowments with accumulated gift value of \$2,766,569, fair value of \$2,715,750 and deficiencies of \$50,819 are reported within net assets with donor restrictions.

The Foundation's endowment-related activities with donor restrictions are as follows:

	December 31	
	2019	2018
Net assets at beginning of year	\$ 46,662,192	\$ 48,193,742
Contributions, net	455,432	726,498
Investment earnings	1,983,554	–
Appropriation for expenditure	(1,879,156)	(2,207,229)
Deficiency of investment earnings	(117,697)	(50,819)
Net assets at end of year	<u>\$ 47,104,325</u>	<u>\$ 46,662,192</u>

10. Board Designations

The Foundation has designated from net assets without donor restriction for the following purposes:

	December 31	
	2019	2018
Program services	\$ 12,160,186	\$ 13,016,675
Education and research	12,158,658	12,926,135
Capital projects	1,647,591	2,332,264
Financial assistance and other	8,867,576	7,502,786
	<u>\$ 34,834,011</u>	<u>\$ 35,777,860</u>

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

11. Related-Party Transactions

The Foundation periodically enters into business transactions with outside vendors that employ members of the Board of Directors. Under the Foundation's conflict of interest policy, the Board of Directors monitors these transactions, and steps are taken to ensure transactions are appropriate and properly approved. As of December 31, 2019, a liability of \$2,595,183 to a beneficiary of a charitable remainder trust, who is a member of the Board of Directors, is reported within liabilities due on split-interest agreements on the statements of financial position. Disbursements to the income beneficiary totaled \$196,892 for the year ended December 31, 2019. The beneficiary was not a member of the Board of Directors prior to January 1, 2019.

At December 31, 2019 and 2018, the Foundation reported \$5,624,510 and \$1,809,732, respectively, due to IU Health related to program support, which was included in accounts payable and accrued expenses in the statements of financial position.

Additionally, during 2019, the Foundation received \$350,000 related to IU Health's interest in assets held by an external foundation. The funds are included in funds held for others in the statements of financial position at December 31, 2019.

The Foundation recorded \$408,977 and \$1,067,783 as revenue and other support from IU Health in the statements of activities and functional expenses for the years ended December 31, 2019 and 2018, respectively.

The Foundation's administrative office and gift shop retail spaces are provided by IU Health at no charge for the duration of its occupancy. The value of the office and retail space is estimated at \$180,000 for the years ended December 31, 2019 and 2018, and is recorded within in-kind revenue and other operating and facility expenses in the statements of activities and functional expenses.

The Foundation provided direct funding to IU Health during 2019 and 2018 in the amount of \$11,212,221 and \$9,412,877, respectively, which is included in the statements of activities and functional expenses as program support.

As the Foundation has no employees, IU Health donated personnel and administrative services to the Foundation of \$7,539,092 and \$6,004,423 for the years ended December 31, 2019 and 2018, respectively, which was recorded as in-kind revenue and allocated among program services, management and general, and fundraising expenses based on the nature of the expense.

Indiana University Health Foundation, Inc.

Notes to Financial Statements (continued)

11. Related-Party Transactions (continued)

Additionally, IU Health created a \$100,000,000 Community Impact Investment (CII) Fund with the intent to support charitable activities in the following areas: (i) alleviating concentrated poverty; (ii) improving healthy living neighborhoods; (iii) workforce development; (iv) fostering career track and leadership succession; (v) alleviating the education achievement gap; (vi) improving academic and social supports; (vii) reducing infant mortality, the incidence of obesity, smoking use, and substance disorders; and (viii) increasing behavioral health access. The targeted areas of community impact initiatives may change over time. On December 31, 2019, the Foundation entered into a contract with IU Health to administer distributions from the CII Fund to grantees. Annually, IU Health will transfer \$4,500,000 from the CII Fund to the Foundation. The first distribution to the Foundation will be made in 2020. This agreement will remain in full and effect until December 31, 2022, and is renewable annually thereafter unless written notice to terminate the agreement is given by either party.

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