Mayo Clinic

Unaudited Condensed Consolidated Financial Reports
Quarter Ended March 31, 2019

Mayo Clinic

Contents

MAYO CLINIC

Condensed Consolidated Statements of Financial Position
(In Millions)

	March 31, 2019 Unaudited	December 31, 2018
Assets		
Current assets:		
Cash and cash equivalents	$ 29	$ 29
Accounts receivable for medical services	2,048	1,828
Securities lending collateral	10	5
Other receivables	377	378
Other current assets	198	187
Total current assets	2,662	2,427
Investments	9,814	9,384
Investments under securities lending agreement	77	70
Other long-term assets	870	695
Property, plant and equipment, net	4,760	4,729
Total assets	$ 18,183	$ 17,305
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	$ 482	$ 464
Accrued payroll	616	646
Accrued employee benefits	152	146
Deferred revenue	46	63
Long-term variable-rate debt	620	620
Securities lending payable	10	5
Other current liabilities	396	337
Total current liabilities	2,322	2,281
Long-term debt, net of current portion	2,799	2,800
Accrued pension and postretirement benefits, net of current portion	1,757	1,749
Other long-term liabilities	1,493	1,323
Total liabilities	8,371	8,153
Net assets:		
Without donor restrictions	6,467	5,937
With donor restrictions	3,345	3,215
Total net assets	9,812	9,152
Total liabilities and net assets	$ 18,183	$ 17,305

See notes to condensed consolidated financial statements.

MAYO CLINIC

Condensed Consolidated Statements of Activities
Unaudited (in Millions)

	Three Months Ended March 31, 2019			Three Months Ended March 31, 2018		
	Without Donor Restrictions	With Donor Restrictions	Total	Without Donor Restrictions	With Donor Restrictions	Total
Revenue, gains and other support:						
Medical service revenue	$ 2,789	$ —	$ 2,789	$ 2,590	$ —	$ 2,590
Grants and contracts	157	—	157	120	—	120
Investment return allocated to current activities	85	7	92	90	20	110
Contributions available for current activities	31	7	38	14	59	73
Other	271	—	271	217	—	217
Net assets released from restrictions	43	(43)	—	50	(50)	—
Total revenue, gains and other support	3,376	(29)	3,347	3,081	29	3,110
Expenses:						
Salaries and benefits	1,915	—	1,915	1,827	—	1,827
Supplies and services	947	—	947	878	—	878
Depreciation and amortization	142	—	142	137	—	137
Facilities	68	—	68	62	—	62
Finance and investment	34	—	34	30	—	30
Total expenses	3,106	—	3,106	2,934	—	2,934
Income (loss) from current activities	270	(29)	241	147	29	176
Noncurrent and other items:						
Contributions not available for current activities, net	(1)	64	63	(4)	62	58
Unallocated investment return (loss), net	215	95	310	(93)	12	(81)
Income tax expense	(8)	—	(8)	(8)	—	(8)
Benefit credit	33	—	33	22	—	22
Other	—	—	—	(4)	—	(4)
Total noncurrent and other items	239	159	398	(87)	74	(13)
Increase in net assets before other changes in net assets	509	130	639	60	103	163
Pension and other postretirement benefit adjustments	21	—	21	36	—	36
Increase in net assets	530	130	660	96	103	199
Net assets at beginning of year	5,937	3,215	9,152	5,018	3,005	8,023
Net assets at end of year	$ 6,467	$ 3,345	$ 9,812	$ 5,114	$ 3,108	$ 8,222

See notes to consolidated financial statements.

MAYO CLINIC

Condensed Consolidated Statements of Cash Flows
Unaudited (In Millions)

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Cash flows from operating activities:		
Cash from medical services	**2,397**	**2,321**
Cash from external lab services	**172**	**160**
Cash from grants and contracts	**133**	**104**
Cash from benefactors	**11**	**28**
Cash from other activities	**64**	**217**
Cash for salaries and benefits	**(1,825)**	**(1,964)**
Cash for supplies, services, and facilities	**(868)**	**(941)**
Interest and dividends received	**21**	**29**
Interest paid	**(9)**	**(8)**
Income taxes paid	**(1)**	**(4)**
Net cash provided by (used in) operating activities	**95**	**(58)**
Cash flows from investing activities:		
Purchase of property, plant and equipment	**(181)**	**(193)**
Purchases of investments	**(803)**	**(332)**
Sales and maturities from investments	**807**	**561**
Net cash provided by (used in) investing activities	**(177)**	**36**
Cash flows from financing activities:		
Restricted gifts, bequests and other	**83**	**37**
Payment of long-term debt	**(1)**	**(1)**
Net cash provided by (used in) financing activities	**82**	**36**
Net increase in cash and cash equivalents	**—**	**14**
Cash and cash equivalents at beginning of period	**29**	**66**
Cash and cash equivalents at end of period	**$ 29**	**$ 80**

See notes to condensed consolidated financial statements.

Note 1. Basis of Presentation

Mayo Clinic (the Clinic) and its Arizona, Florida, Iowa, Minnesota and Wisconsin affiliates provide comprehensive medical care and education in clinical medicine and medical sciences and conduct extensive programs in medical research. The Clinic and its affiliates also provide hospital and outpatient services, and at each major location, the clinical practice is closely integrated with advanced education and research programs. The Clinic has been determined to qualify as a tax-exempt organization under Section 501(c) (3) of the Internal Revenue Code (Code) and as a public charity under Section 509(a) (2) of the Code. Included in the Clinic's condensed consolidated financial statements are all of its wholly owned or wholly controlled subsidiaries, which include both tax-exempt and taxable entities. All significant intercompany transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included and are of a normal and recurring nature. Operating results for the three months ended March 31, 2019, are not necessarily indicative of the results to be expected for the year ending December 31, 2019. For further information, refer to the audited consolidated financial statements and notes thereto for the year ended December 31, 2018.

The Clinic has elected to present the condensed consolidated statements of cash flows using the direct method beginning January 1, 2019 to enhance the utility of the financial statements and disclosures. The statements have been restated for the prior period presented.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Although estimates are considered to be fairly stated at the time the estimates are made, actual results could differ from those estimates.

Note 2. New Accounting Standards

Effective January 1, 2019, the Clinic adopted Financial Accounting Standards Board (FASB) Accounting Standard Update (ASU) No. 2016-02, *Leases (Topic 842)* using a modified retrospective approach and by electing practical expedients, did not reassess whether any existing or expired agreements contain leases, the lease classification for any expired or existing leases, and the initial direct costs for any expired or existing leases. This ASU required the rights and obligations arising from the lease contracts, including existing and new arrangements, to be recognized as assets and liabilities on the statements of financial position in addition to disclosures to help financial statement users better understand the amount, timing, and uncertainty of cash flows arising from leases. The Clinic recorded right-of-use assets and obligations for current operating leases in the amount of $149 in the condensed consolidated statements of financial position.

Effective January 1, 2019, the Clinic adopted FASB Accounting Standard Update (ASU) No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities (Topic 958).* The ASU changed certain financial statement requirements for not-for-profit entities in an effort to make the information more meaningful to users and reduce reporting complexity. The Clinic adopted the net asset classes in the condensed consolidated statements of financial position, the condensed consolidated statements of activities and provided additional disclosures related to liquidity, expense reporting and investment return and restated prior periods presented.

Note 2. New Accounting Standards (Continued)

Effective January 1, 2019, the Clinic adopted FASB Accounting Standard Update (ASU) No. 2017-07, *Compensation - Retirement Benefits (Topic 715)* using a retrospective approach. This ASU required other components of net periodic benefit costs other than service cost be presented separately from presentation of service cost in the condensed consolidated statements of activities. The adoption of this ASU resulted in a $33 and $22 increase in salaries and benefits expense offset by an increase in benefit credit on the condensed consolidated statements of activities for the three months ended March 31, 2019 and March 31, 2018, respectively.

Effective January 1, 2019, the Clinic adopted FASB Accounting Standard Update (ASU) No. 2018-08, *Not-for-Profit Entities - Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made (Topic 958)* on a modified prospective basis. The ASU provided a more robust framework to determine when a transaction should be accounted for as a contribution or as an exchange transaction and provided additional guidance about how to determine whether a contribution is conditional. The adoption of this ASU did not materially impact the condensed consolidated financial statements.

New Accounting Standards Not Yet Adopted:

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820).* This ASU improves the effectiveness of the notes to financial statements through changes in the disclosure requirements for fair value measurement. The ASU is effective January 1, 2020 and will be applied using a retrospective approach.

In August 2018, the FASB issued ASU No. 2018-14, *Compensation - Retirement Benefits - Defined Benefit Plans (Topic 715).* This ASU modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. The ASU is effective January 1, 2021 and will be applied using a retrospective approach.

In August 2018, the FASB issued ASU No. 2018-15, *Intangibles - Goodwill and Other, Internal-Use Software (Subtopic 350-40), Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract.* This ASU aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software.The ASU is effective January 1, 2021 and will be applied using a prospective approach.

The Clinic is currently assessing the impact of the preceding ASUs on its condensed consolidated financial statements.

Note 3. Liquidity and Availability

Financial assets available for general expenditure within one year of the balance sheet date, comprise the following at March 31:

		2019
Cash and cash equivalents	$	29
Accounts receivable		2,048
Promises to give		153
Grants receivable		99
Other receivables		125
Investments		5,962
Total financial assets available within one year	$	8,416

Note 4. Medical Service Revenue

Medical service revenue is reported at the amount that reflects the consideration to which the Clinic expects to be entitled in exchange for providing patient care. These amounts, representing transaction price, are due from patients, third-party payors (including health insurers and government programs), and others and includes variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, the Clinic bills the patients and third-party payors several days after the services are performed and/or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

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

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

The Clinic determines the transaction price based on standard charges for goods and services provided to patients, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with the Clinic’s policy, and/or implicit price concessions based on historical collection experience.

Agreements with third-party payors typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payors follows:

- **Medicare:** Certain inpatient acute care services are paid at prospectively determined rates per discharge based on clinical, diagnostic and other factors. Certain services are paid based on cost-reimbursement methodologies subject to certain limits. Physician services are paid based upon established fee schedules. Outpatient services are paid using prospectively determined rates.
- **Medicaid:** Reimbursements for Medicaid services are generally paid at prospectively determined rates per discharge, per occasion of service, or per covered member.
- **Other:** Payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations provide for payment using prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Note 4. Medical Service Revenue (Continued)

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge the Clinic's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon the Clinic. In addition, the contracts the Clinic has with commercial payors also provide for retroactive audit and review of claims.

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. The Clinic also provides services to uninsured patients, and offers those uninsured patients a discount, either by policy or law, from standard charges. The Clinic estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to medical service revenue in the period of the change. For the three months ended March 31, 2019 and 2018, revenue recognized due to changes in its estimates of transaction price concessions for performance obligations satisfied in prior years was not significant. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense. Bad debt expense for the three months ended March 31, 2019 and 2018 and was not significant.

Settlements with third-party payors for retroactive adjustments due to audits, reviews, or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor, and the Clinic's historical settlement activity, including an assessment to ensure it is probable a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available), or as years are settled or are no longer subject to such audits, reviews, and investigations. Adjustments arising from a change in the transaction price were not significant in 2019 or 2018.

Patients who meet the Clinic's criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue.

March 31, 2019 (in Millions)

Note 4. Medical Service Revenue (Continued)

The composition of medical service revenue based on the regions of the country the Clinic operates in, its lines of business, and timing of revenue recognition for the three months ended March 31, 2019 and 2018 are as follows:

	March 31, 2019			
	Midwest	Southeast	Southwest	Total
Hospital	$ 1,067	$ 181	$ 245	$ 1,493
Clinic	763	174	165	1,102
Senior Care & Nursing Home	4	—	—	4
Other	13	—	—	13
Total patient care service revenue	1,847	355	410	2,612
External lab	177	—	—	177
Total medical service revenue	$ 2,024	$ 355	$ 410	$ 2,789
Timing of revenue and recognition:				
At time services are rendered	$ 953	$ 174	$ 165	$ 1,292
Services transferred over time	1,071	181	245	1,497
Total	$ 2,024	$ 355	$ 410	$ 2,789

	March 31, 2018			
	Midwest	Southeast	Southwest	Total
Hospital	$ 976	$ 157	$ 224	$ 1,357
Clinic	744	148	157	1,049
Senior Care & Nursing Home	5	—	—	5
Other	11	—	—	11
Total patient care service revenue	1,736	305	381	2,422
External lab	168	—	—	168
Total medical service revenue	$ 1,904	$ 305	$ 381	$ 2,590
Timing of revenue and recognition:				
At time services are rendered	$ 923	$ 148	$ 157	$ 1,228
Services transferred over time	981	157	224	1,362
Total	$ 1,904	$ 305	$ 381	$ 2,590

Hospital revenue includes a variety of services mainly covering inpatient procedures requiring overnight stays or outpatient operations that require anesthesia or use of complex diagnostic and surgical equipment as well as emergency care for traumas and other critical conditions. Clinic revenue includes services primarily focused on the care of outpatients covering primary and specialty healthcare needs. The Clinic's practice is to record certain radiology, pathology and other hospital related services in the Midwest region as clinic revenue in the amount of $264 and $226 for the three months ended March 31, 2019 and 2018, respectively. Examples of revenue at time services are rendered include

March 31, 2019 (in Millions)

Note 4. Medical Service Revenue (Continued)

clinical services, lab and transport; and services transferred over time include hospital and senior care revenue.

The composition of medical service revenue by payor for the three months ended March 31, is as follows:

	2019	2018
Medicare	$ 684	$ 629
Medicaid	97	80
Contract	1,644	1,498
Other, including self-pay	364	383
Total	$ 2,789	$ 2,590

The Clinic's practice is to assign a patient to the primary payor and not reflect other uninsured balances (for example, copays and deductibles) as self-pay. Therefore the payors listed above contain patient responsibility components, such as co-pays and deductibles.

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

Note 5. Investments

Investments in equity, debt securities, and alternative investments are recorded at fair value. Realized gains and losses are calculated based on the average cost method. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) are included in the condensed consolidated statements of activities.

Alternative investments (principally limited partnership interests in absolute return, hedge, private equity, real estate and natural resources funds), represents the Clinic's ownership interest in the net asset value (NAV) of the respective partnership. The investments in alternative investments may individually expose the Clinic to securities lending, short sales, and trading in futures and forward contract options and other derivative products. The Clinic's risk is limited to the investment's carrying value.

From time to time, the Clinic invests directly in certain derivative contracts that do not qualify for hedge accounting and are recorded at fair value in investments. Changes in fair value are reported as a component of net unrealized gains or losses in the investment returns. These contracts are used in the Clinic's investment management program to minimize certain investment risks. For the three months ended March 31, 2019 and 2018, the realized and unrealized gain (loss) from derivative contracts was not significant.

It is the Clinic's intent to maintain a long-term investment portfolio to support research, education, and other activities. Accordingly, the total investment return is shown in the condensed consolidated statements of activities in two segments. The investment return allocated to current activities is determined by a formula, which involves allocating five percent of a three-year moving average of investments related to endowments, the matching of financing costs for the assets required for operations and additional expenses covered by investment returns. Management believes this return is approximately equal to the real return that the Clinic expects to earn on its investments over the long term. The unallocated investment return, included in noncurrent and other items in the condensed consolidated statements of activities, represents the difference between the total investment return and the amount allocated to current activities.

Note 6. Fair Value Measurements

The Clinic holds certain financial instruments that are required to be measured at fair value on a recurring basis. The valuation techniques used to measure fair value under the *Fair Value Measurements and Disclosures* topic of the FASB ASC 820 are based upon observable and unobservable inputs. The standard establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

Level 1: Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the same term of the financial instrument.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The Clinic's policy is to recognize transfers in and transfers out as of the actual date of the event or change in circumstances that caused the transfer. There were no significant transfers or activity within Levels for the three months ended March 31, 2019 and 2018.

March 31, 2019 (in Millions)

Note 6. Fair Value Measurements (Continued)

The following tables present the financial instruments carried at fair value as of March 31, 2019 and December 31, 2018, by caption on the condensed consolidated statements of financial position categorized by the valuation hierarchy and NAV:

	March 31, 2019				
	Level 1	Level 2	Level 3	NAV	Total Fair Value
Assets:					
Securities lending collateral	$ 10	$ —	$ —	$ —	$ 10
Investments:					
Cash and equivalents	1,383	—	—	—	1,383
Fixed-income securities:					—
U.S. government	—	270	—	—	270
U.S. government agencies	—	415	—	—	415
U.S. corporate	—	365	—	—	365
Foreign	—	32	—	—	32
Common and preferred stocks:					—
U.S.	596	—	—	—	596
Foreign	388	—	—	—	388
Funds:					—
Fixed-income	474	—	—	—	474
Equities	555	461	—	—	1,016
Other investments	—	—	—	—	—
Less securities under lending agreement	(77)	—	—	—	(77)
Investments at NAV	—	—	—	4,952	4,952
Total investments	3,319	1,543	—	4,952	9,814
Investments under securities lending agreement	77	—	—	—	77
Other long-term assets:					
Trust receivables	64	30	57	—	151
Technology-based ventures	—	—	34	—	34
Total other long-term assets	64	30	91	—	185
Total assets at fair value	$ 3,470	$ 1,573	$ 91	$ 4,952	$ 10,086
Liabilities:					
Securities lending payable	$ 10	$ —	$ —	$ —	10
Total liabilities at fair value	$ 10	$ —	$ —	$ —	$ 10

March 31, 2019 (in Millions)

Note 6. Fair Value Measurements (Continued)

	December 31, 2018				
	Level 1	Level 2	Level 3	NAV	Total Fair Value
Assets:					
Securities lending collateral	$ 5	$ —	$ —	$ —	$ 5
Investments:					
Cash and equivalents	1,372	—	—	—	1,372
Fixed-income securities:					—
U.S. government	—	288	—	—	288
U.S. government agencies	—	352	—	—	352
U.S. corporate	—	297	—	—	297
Foreign	—	27	—	—	27
Common and preferred stocks:					—
U.S.	533	—	—	—	533
Foreign	349	—	—	—	349
Funds:					—
Fixed-income	454	—	—	—	454
Equities	531	451	—	—	982
Other investments	—	18	—	—	18
Less securities under lending					—
agreement	(70)	—	—	—	(70)
Investments at NAV	—	—	—	4,782	4,782
Total investments	3,169	1,433	—	4,782	9,384
Investments under securities lending agreement	70	—	—	—	70
Other long-term assets:					
Trust receivables	60	28	57	—	145
Technology-based ventures	—	—	32	—	32
Total other long-term assets	60	28	89	—	177
Total assets at fair value	$ 3,304	$ 1,461	$ 89	$ 4,782	$ 9,636
Liabilities:					
Securities lending payable	$ 5	$ —	$ —	$ —	5
Total liabilities at fair value	$ 5	$ —	$ —	$ —	$ 5

March 31, 2019 (in Millions)

Note 6. Fair Value Measurements (Continued)

The following is a description of the Clinic's valuation methodologies for assets and liabilities measured at fair value. Fair value for Level 1 is based upon quoted market prices. Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources, including market participants, dealers and brokers. Level 3 primarily consists of trusts recorded at fair value based on the underlying value of the assets in the trust or discounted cash flow of the expected payment streams. The trusts reported as Level 3 are primarily perpetual trusts managed by third parties invested in stocks, mutual funds, and fixed-income securities that are traded in active markets with observable inputs, and since the Clinic will never receive the trust assets, these perpetual trusts are reported as Level 3.

The methods described above and those recorded at NAV may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Clinic believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The carrying values of cash and cash equivalents, and short-term investments, accounts receivable, accounts payable and accrued expenses are reasonable estimates of their fair value due to the short-term nature of these financial instruments. The estimated fair value of long-term debt, based on quoted market prices for the same or similar issues (Level 2), was approximately $168 and $79 more than its carrying value at March 31, 2019 and December 31, 2018, respectively. Other long-term assets and liabilities have a carrying value that approximates fair value.

The following information pertains to those alternative investments recorded at NAV in accordance with the *Fair Value Measurements and Disclosures* topic of the FASB ASC 820.

At March 31, 2019, alternative investments recorded at NAV consisted of the following:

	Fair Value	Unfunded Commitment	Redemption Frequency (If Currently Eligible)	Redemption Notice Period
Absolute return/hedge funds (a)	$ 2,380	$ —	Monthly to annually	30–90 days
Private partnerships (b)	2,572	1,108		
Total alternative investments	$ 4,952	$ 1,108		

At December 31, 2018, alternative investments recorded at NAV consisted of the following:

	Fair Value	Unfunded Commitment	Redemption Frequency (If Currently Eligible)	Redemption Notice Period
Absolute return/hedge funds (a)	$ 2,217	$ —	Monthly to annually	30–90 days
Private partnerships (b)	2,565	1,159		
Total alternative investments	$ 4,782	$ 1,159		

Note 6. Fair Value Measurements (Continued)

(a) This category includes investments in absolute return/hedge funds, which are actively managed commingled investment vehicles that derive the majority of their returns from factors other than the directional flow of the markets in which they invest. Representative strategies include high-yield credit, distressed debt, merger arbitrage, relative value, and long-short equity strategies. The fair values of the investments in this category have been estimated using the NAV per share of the investments. Investments in this category generally carry "lockup" restrictions that do not allow investors to seek redemption in the first year after acquisition. Following the initial lockup period, liquidity is generally available monthly, quarterly or annually following a redemption request. Over 90 percent of the investments in this category have at least annual liquidity.

(b) This category includes limited partnership interests in closed-end funds that focus on venture capital, private equity, real estate and resource-related strategies. The fair values of the investments in this category have been estimated using the NAV of the Clinic's ownership interest in partners' capital. Distributions from each fund will be received as the underlying investments of the funds are liquidated. It is estimated that the underlying assets of most funds will generally be liquidated over a seven- to ten-year period.

Note 7. Securities Lending

The Clinic has an arrangement with its investment custodian to lend Clinic securities to approved brokers in exchange for a fee. Among other provisions that limit the Clinic's risk, the securities lending agreement specifies that the custodian is responsible for lending securities and obtaining adequate collateral from the borrower. Collateral is limited to cash, government securities, and irrevocable letters of credit. Investments are loaned to various brokers and are returnable on demand. In exchange, the Clinic receives collateral. The cash collateral is shown as both an asset and a liability on the condensed consolidated statements of financial position.

At March 31, 2019 and December 31, 2018, the aggregate market value of securities on loan under securities lending agreements totaled $77 and $70, respectively, and the total value of the collateral supporting the securities is $81 and $74, respectively, which represents 105 and 106 percent of the value of the securities on loan at March 31, 2019 and December 31, 2018, respectively. The cash portion of the collateral supporting the securities as of March 31, 2019 and December 31, 2018, is $10 and $5, respectively. Noncash collateral provided to the Clinic is not recorded in the condensed consolidated statements of financial position, as the collateral may not be sold or repledged. The Clinic's claim on such collateral is limited to the market value of loaned securities. In the event of nonperformance by the other parties to the securities lending agreements, the Clinic could be exposed to a loss.

Note 8. Commitments and Contingencies

The Clinic has various construction projects in progress related to patient care, research, and educational facilities. The estimated costs committed to complete the various projects at March 31, 2019, approximated $1,264, all of which is expected to be expended over the next three to five years.

While the Clinic is self-insured for a substantial portion of its general and workers' compensation liabilities, the Clinic maintains commercial insurance coverage against catastrophic loss. Additionally, the Clinic maintains a self-insurance program for its long-term disability coverage. The provision for estimated self-insured claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported.

The Clinic is a defendant in various lawsuits arising in the ordinary course of business and records an estimated liability for probable claims. Although the outcome of these lawsuits cannot be predicted with certainty, management believes the ultimate disposition of such matters will not have a material effect on the Clinic's condensed consolidated statements of financial position or statementsof activities.

March 31, 2019 (in Millions)

Note 9. Net Assets with Donor Restrictions

The Clinic receives contributions in support of research, education and clinical activities. Net assets with donor restrictions were available for the following:

	March 31, 2019	December 31, 2018
Subject to expenditure for specified purpose:		
Research	$ 379	$ 324
Education	71	55
Buildings and equipment	92	81
Charity care	39	38
Clinical	44	37
Other	9	8
Total expenditure for specified purpose	634	543
Subject to passage of time:		
Pledges and trusts	325	300
Endowments:		
Perpetual in nature:		
Research	920	895
Education	264	256
Charity care	13	13
Clinical	93	90
Other	25	27
Pledges and trusts	311	329
Buildings and equipment	1	1
Total perpetual in nature	1,627	1,611
Subject to endowment spending policy:		
Research	393	395
Education	257	259
Charity care	22	20
Clinical	59	59
Other	28	28
Total subject to endowment spending policy	759	761
Total endowments	2,386	2,372
Total net assets with donor restrictions	$ 3,345	$ 3,215

March 31, 2019 (in Millions)

Note 9. Net Assets with Donor Restrictions (Continued)

Net assets were released from donor restrictions as expenditures were made, which satisfied the following restricted purposes for the periods ended March 31:

	2019	2018
Research	$ 25	$ 30
Education	8	11
Buildings and equipment	3	2
Other	7	7
Total net assets released from donor restrictions	$ 43	$ 50

Note 10. Board-Designated Funds

Board-designated funds are subject to expenditure for the following purpose for the periods:

	March 31, 2019	December 31, 2018
Research	$ 1,086	$ 1,073
Education	200	160
Buildings and equipment	3	3
Charity care	9	9
Clinical	114	114
Other	959	894
Total designation for specified purpose	$ 2,371	$ 2,253

Note 11. Functional Expenses

The condensed consolidated financial statements present certain expenses that are attributed to more than one program or supporting function. Therefore, expenses require allocation on a reasonable basis that is consistently applied. Benefits and payroll taxes are allocated based on factors of either salary expense or hours worked. Overhead costs that include things such as professional services, office expenses, information technology, interest, insurance, and other similar expenses are allocated on a variety of factors including revenues, hours worked, and salary expense. Costs related to space include occupancy, depreciation and amortization, and property taxes are allocated on a square footage basis.

March 31, 2019 (in Millions)

Note 11. Functional Expenses (Continued)

The expenses reported in the condensed consolidated statements of activities for the periods ended March 31, 2019 and 2018, supported the following programs and functions:

	2019							
	Patient care	Lab and technology ventures	Research	Graduate and other education	General and administrative	Development expenses	Other activities	Total expenses
Salaries and benefits	$ 1,565	$ 43	$ 138	$ 68	$ 10	$ 5	$ 86	$ 1,915
Supplies and services	636	202	55	17	18	4	15	947
Depreciation and amortization	119	2	14	3	3	—	1	142
Facilities	56	1	4	2	5	—	—	68
Finance & investment	32	—	4	—	—	—	(2)	34
Total	$ 2,408	$ 248	$ 215	$ 90	$ 36	$ 9	$ 100	$ 3,106

	2018							
	Patient care	Lab and technology ventures	Research	Graduate and other education	General and administrative	Development expenses	Other activities	Total expenses
Salaries and benefits	$ 1,477	$ 43	$ 132	$ 65	$ 55	$ 2	$ 53	$ 1,827
Supplies and services	560	210	48	16	28	4	12	878
Depreciation and amortization	110	2	14	2	8	—	1	137
Facilities	44	1	4	2	11	—	—	62
Finance & investment	31	—	4	—	1	—	(6)	30
Total	$ 2,222	$ 256	$ 202	$ 85	$ 103	$ 6	$ 60	$ 2,934

March 31, 2019 (in Millions)

Note 12. Employee Benefit Programs

The Clinic serves as plan sponsor for several defined-benefit pension funds and other postretirement benefits.

Components of net periodic benefit cost for the three months ended March 31, are as follows for the defined-benefit pension funds:

	Qualified	
	2019	2018
Service cost	$ 112	$ 127
Interest cost	93	88
Expected return on plan assets	(158)	(156)
Amortization of unrecognized:		
Prior service benefit	(13)	(12)
Net actuarial loss	35	52
Net periodic benefit cost	$ 69	$ 99

Components of net periodic benefit cost for the other postretirement benefits are as follows:

	Postretirement Benefits	
	2019	2018
Service cost	$ 2	$ 3
Interest cost	11	10
Amortization of unrecognized:		
Prior service benefit	(5)	(9)
Net actuarial loss	3	5
Net periodic cost (benefit)	$ 11	$ 9

Note 13. Subsequent Events

The Clinic evaluated events and transactions occurring subsequent to March 31, 2019 through May 9, 2019, the date of issuance of the condensed consolidated financial statements. During this period, there were no subsequent events requiring recognition in the condensed consolidated financial statements. Additionally, there were no nonrecognized events requiring disclosure.

Management's Discussion and Analysis

This quarterly report includes the interim unaudited condensed consolidated financial statements and analysis for Mayo Clinic and its affiliates. References to "the Clinic", "we", "our", or "us" in this document are to the Mayo Clinic and all of the affiliates consolidated with it pursuant to accounting principles generally accepted in the United States of America (GAAP).

The financial information should be read together with our interim unaudited condensed consolidated financial statements and related notes included elsewhere in this quarterly report, as well as the audited consolidated financial statements as of and for the year ended December 31, 2018. The audited consolidated financial statements are available from the Municipal Securities Rulemaking Board (the MSRB) on its Electronic Municipal Market Access (EMMA) system, found at http:// emma.msrb.org.

Certain statements included in this quarterly report constitute forward-looking statements that involve risks and uncertainties. Actual results may differ significantly from the results discussed in the forward-looking statements as a result of known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. We do not plan to issue any updates or revisions to those forward-looking statements if or when the expectations, or events, conditions or circumstances on which such statements are based occur.

Mayo Clinic Overview

Mayo Clinic (“Mayo”) is a charitable, nonprofit corporation headquartered in Rochester, Minnesota. Mayo provides comprehensive medical care, education in clinical medicine and the medical sciences, and extensive programs in medical research. The Mayo logo of three interlocking shields symbolizes Mayo's commitment to excellence and interdependence in the three areas of education, clinical practice and research. Mayo Clinic has major campuses in Rochester, Minn.; Scottsdale and Phoenix, Ariz.; and Jacksonville, Fla. The Mayo Clinic Health System has over 70 locations in Minnesota, Wisconsin and Iowa.

Mayo developed from the medical practice of a pioneer physician, Dr. William Worrall Mayo. Born in 1819 near Manchester, England, Dr. Mayo came to America at the age of 25. Dr. Mayo was appointed in 1863 as examining surgeon for the Union Army Enrollment Board in Rochester, Minnesota, and continued to practice there in the years that followed. When a tornado devastated Rochester in 1883, the joint efforts of Dr. Mayo and the Sisters of Saint Francis produced a working relationship that led to the construction of Saint Marys Hospital in 1889. Dr. Mayo, with his sons, William James Mayo and Charles Horace Mayo, comprised the medical staff of the new 27 bed hospital which has operated continuously to the present day and grown to meet the demand for care, currently comprising 2,059 licensed beds of which 1,274 were staffed. In 1919, the Mayo brothers founded the Mayo Properties Association, transferred to it all Mayo Clinic properties and facilities, the name Mayo Clinic, and the right to receive all future earnings. With its more recent expansion into communities surrounding Rochester and the establishment of major campuses in Jacksonville, Florida and Phoenix/Scottsdale, Arizona, Mayo Clinic is one of the world’s largest private medical enterprises.

In addition to their clinical medical practice, the Doctors Mayo established a center for medical education and research. In 1915, with an initial gift of $1,500,000, the Mayo brothers established the Mayo Graduate School of Medicine (now known as Mayo Clinic School of Graduate Medical Education), which offers graduate residency training for physicians and scientists working toward certification as specialists of medicine and surgery, as well as fellowships for those planning research and teaching careers in the medical sciences. Approximately 23,000 physicians, practicing throughout the United States and 75 foreign countries, are members of the alumni association of the Mayo School of Graduate Medical Education.

March 31, 2019 (in Millions)

Acknowledgments and Awards

- Mayo Clinic ranked #1 as best hospital in the world by Newsweek
  Mayo Clinic was recognized for "its peerless educational arm, including the Mayo Clinic Alix School of Medicine that sets it apart, providing vital innovation for the entire medical community (more than 7,200 peer-reviewed publications to date)," *Newsweek* states.

- Mayo Clinic Alix School of Medicine ranked among top 10 best medical schools by U.S. News & World Report
  Mayo Clinic Alix School of Medicine was ranked in a three-way tie at #9 in overall and research.

- Mayo Clinic ranked #9 among "America's Best Large Employers" by Forbes magazine
  The #9 ranking is up from #14 in 2018. Mayo Clinic was also ranked #45 for Best Employers for Diversity 2019, #33 among Large U.S. Charities 2018, #59 among Best Employers for New Grads 2018, and #72 among Best Employers for Women 2018.

- Mayo Clinic Hospitals earn CMS star ratings for Overall Hospital Quality
  Fifteen hospitals across Mayo Clinic received star ratings from the Centers for Medicare and Medicaid Services for Overall Hospital Quality. Six of the 15 hospitals earned five stars - the best score possible. The national average is three of five stars. The star ratings measure seven broad categories: Mortality, Safety of Care, Readmission, Patient Experience, Effectiveness of Care, Timeliness of Care, and Efficient Use of Imaging. Hospitals that receive five-star ratings are among the top 8 percent of hospitals in the U.S. The star rating provides patients with information about multiple dimensions of quality in a single score. Star ratings are assigned based on a hospital's composite score of 64 quality metrics from the Inpatient Quality Reporting and Outpatient Quality Reporting programs.

Operating Highlights

Financial performance during the quarter ended March 31, 2019 was strong, continuing the trajectory of recent periods. Total revenue of $3.376 billion grew by $295 million over the year ago period. Net medical service revenue (NMSR) represented 83% of total revenue and grew slightly slower (7.7%) than total revenue, producing net operating income of $241 million, a 7.2% operating margin, and net income of $639 million, a 19.1% net margin. All indicators represent significant improvements from the same period in the prior year:

	Q1 2019		Q1 2018		% Change
Net medical service revenue	$	2,789	$	2,590	7.7%
Total operating revenue	$	3,376	$	3,110	8.5%
Net operating income	$	241	$	176	37.1%
Net income	$	639	$	163	289.6%

Revenue from clinical practice was $2.991 billion, up 7.0% from the prior year quarter with positive growth at Rochester, Jacksonville and Phoenix sites as well as the Mayo Clinic Health System. Year over year growth was 6.8% in Rochester, 16.0% in Florida, and 7.6% in Arizona and was driven primarily by inpatient surgical patients and service mix. Mayo Clinic Health System revenue grew by 3.0%, despite significant weather-related volume disruptions in the quarter. First quarter revenue was positively impacted by two items:

– a recovery of revenue from 2015 through 2018 that had been withheld by a Medicare administrative contractor and previously written off, resulting in $25 million of additional revenue.
– an acceleration in revenue recognition for external funding in support of research which resulted in a one-time recognition of approximately $30 million in research revenue. This is a result of implementing “Accounting Standards Update 2018-08- Not-for-Profit Entities (Topic 958) - Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made”

Revenue largely tracked with volumes although historical comparisons of volume metrics continue to be challenged by the new metric definitions that accompanied the Epic implementation. On a consolidated basis, hospital admissions increased slightly (0.5%) over prior year and surgical patients declined 0.7%. Payer mix was stable and in line with expectations as shown in the table below:

(NMSR, $ in millions)	**Q1 2019**	**%**	**Q1 2018**	**%**
Medicare	$ 684	24.5%	$ 629	24.3%
Medicaid	97	3.5%	80	13.1%
Contract	1,644	58.9%	1,498	57.8%
Other, incl Self Pay	364	13.1%	383	14.8%
Total	$ 2,789		$ 2,590	

Operating expenses were well-managed with year-over-year growth of 5.8%. Labor expense of $1.915 billion represented an increase of 4.8% over the prior year period and comprised 61.7% of operating expenses, slightly below the 62.3% reported in the year ago quarter. Supplies and services expense increased by 7.9% with pharmaceuticals comprising the largest driver with a 8.7% increase over the prior year period. Allied health and consulting staff grew in line with volumes, increasing 2.4% to 53,599 and 2.0% to 4,304 full time equivalents, respectively.

Financial markets rebounded in the first quarter 2019 after a challenging fourth quarter 2018. The Mayo Clinic Long Term Investment Fund (LTF) generated a 4.6% return for the quarter and returned 5.6% for the trailing 12 month period. On a three-year and 10-year basis, the LTF’s returns continue to meet investment objectives and exceed benchmark performance, with annualized returns of 9.7% and 10.2% respectively.

Investment returns yielded non-operating income of $310 million and another $63 million in contributions for endowments and capital projects. Combined with smaller non-operating amounts for income taxes and other items, non-operating income totaled $398 million compared with a $13 million non-operating loss in the year ago period.

March 31, 2019 (in Millions)

Cash and investments of $9.9 billion at March 31, 2019 represent an increase of $1.3 billion from a year ago. Improvement in cash and investments during the past 12 months are the result of both strong cash flow from operations and investment gains.

Key balance sheet ratios are either unchanged or slightly improved from last report as follows, suggesting stability in credit rating:

	3/31/2019	**12/31/2018**	**3/31/2018**
Days Revenue Outstanding	66.2	61.0	66.3
Days Cash on Hand*	249	240	230.0
Cash to Debt*	231%	220%	229%
Debt to Capitalization	29%	30%	30%
MADS Coverage Ratio	6.8x	6.3x	7.0x

*Includes temporarily restricted cash and investment in the calculation