UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2022
or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number: 001-37576

Surgery Partners, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**47-3620923**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

310 Seven Springs Way, Suite 500
Brentwood, Tennessee 37027
(Address of principal executive offices and zip code)

(615) 234-5900
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value $0.01 per share	SGRY	The Nasdaq Global Select Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☒	Accelerated filer ☐
Non-accelerated filer ☐	Smaller reporting company ☐
	Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of July 26, 2022, there were 89,935,287 shares of the registrant's common stock outstanding.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

SURGERY PARTNERS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in millions, except per share amounts)

	(Unaudited) June 30, 2022	December 31, 2021
ASSETS		
Current assets:		
Cash and cash equivalents	$ 227.4	$ 389.9
Accounts receivable	412.0	430.2
Inventories	64.0	61.1
Prepaid expenses	37.4	25.6
Other current assets	47.6	39.3
Total current assets	788.4	946.1
Property and equipment, net of accumulated depreciation of $320.7 and $272.3, respectively	789.1	629.7
Goodwill and other intangible assets, net	4,035.6	3,955.5
Investments in and advances to affiliates	159.7	88.7
Right-of-use operating lease assets	277.8	324.1
Long-term deferred tax assets	110.4	114.4
Other long-term assets	130.6	59.1
Total assets	$ 6,291.6	$ 6,117.6
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 126.4	$ 124.9
Accrued payroll and benefits	83.8	77.1
Medicare accelerated payments and deferred governmental grants	21.4	64.4
Other current liabilities	221.8	210.0
Current maturities of long-term debt	68.3	60.4
Total current liabilities	521.7	536.8
Long-term debt, less current maturities	3,019.4	2,878.4
Right-of-use operating lease liabilities	271.8	315.6
Other long-term liabilities	96.4	87.0
Non-controlling interests—redeemable	341.8	330.2
Stockholders' equity:		
Preferred stock, $0.01 par value; shares authorized - 20,310,000; shares issued or outstanding - none	—	—
Common stock, $0.01 par value; shares authorized - 300,000,000; shares issued and outstanding - 89,935,287 and 89,332,557, respectively	0.9	0.9
Additional paid-in capital	1,618.8	1,622.3
Accumulated other comprehensive income (loss)	44.3	(31.5)
Retained deficit	(508.9)	(502.7)
Total Surgery Partners, Inc. stockholders' equity	1,155.1	1,089.0
Non-controlling interests—non-redeemable	885.4	880.6
Total stockholders' equity	2,040.5	1,969.6
Total liabilities and stockholders' equity	$ 6,291.6	$ 6,117.6

See notes to unaudited condensed consolidated financial statements.

SURGERY PARTNERS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited, dollars in millions, except per share amounts, shares in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Revenues	$ 615.4	$ 543.3	$ 1,211.6	$ 1,055.7
Operating expenses:				
Salaries and benefits	181.9	155.3	360.8	307.0
Supplies	173.5	157.5	345.1	304.8
Professional and medical fees	66.7	57.4	130.3	112.9
Lease expense	20.2	22.6	40.2	45.4
Other operating expenses	38.5	32.2	75.8	63.8
Cost of revenues	480.8	425.0	952.2	833.9
General and administrative expenses	26.1	24.5	55.6	51.3
Depreciation and amortization	28.0	25.2	55.4	50.9
Transaction and integration costs	8.2	9.2	15.3	14.5
Grant funds	(0.1)	(4.9)	(1.3)	(20.0)
Loss on disposals and deconsolidations, net	1.1	1.0	1.0	0.1
Equity in earnings of unconsolidated affiliates	(2.6)	(3.0)	(5.7)	(5.6)
Litigation settlement	—	—	(32.8)	—
Loss on debt extinguishment	—	9.6	—	9.6
Other income, net	(2.6)	(2.8)	(5.0)	(2.8)
	538.9	483.8	1,034.7	931.9
Operating income	76.5	59.5	176.9	123.8
Interest expense, net	(56.9)	(53.4)	(113.2)	(106.7)
Income before income taxes	19.6	6.1	63.7	17.1
Income tax (expense) benefit	(4.3)	2.7	(5.6)	2.5
Net income	15.3	8.8	58.1	19.6
Less: Net income attributable to non-controlling interests	(33.7)	(35.7)	(64.3)	(67.5)
Net loss attributable to Surgery Partners, Inc.	(18.4)	(26.9)	(6.2)	(47.9)
Less: Amounts attributable to participating securities	—	—	—	(10.3)
Net loss attributable to common stockholders	$ (18.4)	$ (26.9)	$ (6.2)	$ (58.2)
Net loss per share attributable to common stockholders				
Basic	$ (0.21)	$ (0.39)	$ (0.07)	$ (0.94)
Diluted [(1)]	$ (0.21)	$ (0.39)	$ (0.07)	$ (0.94)
Weighted average common shares outstanding				
Basic	88,900	69,267	88,450	62,060
Diluted [(1)]	88,900	69,267	88,450	62,060

[(1)] The impact of potentially dilutive securities for all periods presented was not considered because the effect would be anti-dilutive.

See notes to unaudited condensed consolidated financial statements.

SURGERY PARTNERS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited, dollars in millions)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	**2021**	**2022**	**2021**
Net income	$ 15.3	$ 8.8	$ 58.1	$ 19.6
Other comprehensive income, net of tax:				
Derivative activity	19.0	0.2	75.8	6.6
Comprehensive income	34.3	9.0	133.9	26.2
Less: Comprehensive income attributable to non-controlling interests	(33.7)	(35.7)	(64.3)	(67.5)
Comprehensive income (loss) attributable to Surgery Partners, Inc.	$ 0.6	$ (26.7)	$ 69.6	$ (41.3)

See notes to unaudited condensed consolidated financial statements.

SURGERY PARTNERS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited, dollars in millions, shares in thousands)

	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive (Loss) Income	Retained Deficit	Non-Controlling Interests—Non-Redeemable	Total
	Shares	Amount					
Balance at December 31, 2020	50,462	$ 0.5	$ 607.9	$ (61.0)	$ (431.8)	$ 766.5	$ 882.1
Net (loss) income	—	—	—	—	(21.0)	21.1	0.1
Equity-based compensation	812	—	(2.8)	—	—	—	(2.8)
Preferred dividends	—	—	(10.3)	—	—	—	(10.3)
Equity offering	8,625	0.1	248.2	—	—	—	248.3
Other comprehensive income	—	—	—	6.4	—	—	6.4
Acquisition and disposal of shares of non-controlling interests, net	—	—	0.3	—	—	2.0	2.3
Distributions to non-controlling interests—non-redeemable holders	—	—	—	—	—	(20.8)	(20.8)
Balance at March 31, 2021	59,899	$ 0.6	$ 843.3	$ (54.6)	$ (452.8)	$ 768.8	$ 1,105.3
Net (loss) income	—	—	—	—	(26.9)	22.0	(4.9)
Equity-based compensation	(29)	—	3.7	—	—	—	3.7
Preferred share conversion	22,609	0.2	439.5	—	—	—	439.7
Other comprehensive income	—	—	—	0.2	—	—	0.2
Acquisition and disposal of shares of non-controlling interests, net	—	—	11.9	—	—	(6.3)	5.6
Distributions to non-controlling interests—non-redeemable holders	—	—	—	—	—	(22.3)	(22.3)
Balance at June 30, 2021	82,479	$ 0.8	$ 1,298.4	$ (54.4)	$ (479.7)	$ 762.2	$ 1,527.3
Balance at December 31, 2021	89,333	$ 0.9	$ 1,622.3	$ (31.5)	$ (502.7)	$ 880.6	$ 1,969.6
Net income	—	—	—	—	12.2	20.0	32.2
Equity-based compensation	572	—	7.7	—	—	—	7.7
Other comprehensive income	—	—	—	56.8	—	—	56.8
Acquisition and disposal of shares of non-controlling interests, net	—	—	(4.8)	—	—	(24.3)	(29.1)
Distributions to non-controlling interests—non-redeemable holders	—	—	—	—	—	(24.6)	(24.6)
Balance at March 31, 2022	89,905	$ 0.9	$ 1,625.2	$ 25.3	$ (490.5)	$ 851.7	$ 2,012.6
Net (loss) income	—	—	—	—	(18.4)	22.7	4.3
Equity-based compensation	30	—	4.4	—	—	—	4.4
Other comprehensive income	—	—	—	19.0	—	—	19.0
Acquisition and disposal of shares of non-controlling interests, net	—	—	(10.8)	—	—	38.7	27.9
Distributions to non-controlling interests—non-redeemable holders	—	—	—	—	—	(27.7)	(27.7)
Balance at June 30, 2022	89,935	$ 0.9	$ 1,618.8	$ 44.3	$ (508.9)	$ 885.4	$ 2,040.5

See notes to unaudited condensed consolidated financial statements.

SURGERY PARTNERS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, dollars in millions)

	Six Months Ended June 30, 2022	Six Months Ended June 30, 2021
Cash flows from operating activities:		
Net income	$ 58.1	$ 19.6
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	55.4	50.9
Non-cash interest expense, net	12.4	5.7
Equity-based compensation expense	8.0	9.3
Loss on disposals and deconsolidations, net	1.0	0.1
Loss on debt extinguishment	—	9.6
Deferred income taxes	4.9	(3.2)
Equity in earnings of unconsolidated affiliates, net of distributions received	(0.4)	(0.4)
Non-cash lease expense	17.1	20.0
Changes in operating assets and liabilities, net of acquisitions and divestitures:		
Accounts receivable	5.4	(3.1)
Medicare accelerated payments and deferred governmental grants	(40.2)	(28.8)
DOJ settlement payments	—	(32.2)
Other operating assets and liabilities	0.2	5.0
Net cash provided by operating activities	121.9	52.5
Cash flows from investing activities:		
Purchases of property and equipment	(40.6)	(28.0)
Payments for acquisitions, net of cash acquired	(74.9)	(15.2)
Proceeds from disposals of facilities and other assets	—	2.5
Purchases of equity investments	(65.8)	—
Proceeds from sales of equity investments	11.5	—
Other investing activities	(11.6)	—
Net cash used in investing activities	(181.4)	(40.7)
Cash flows from financing activities:		
Principal payments on long-term debt	(33.3)	(309.4)
Borrowings of long-term debt	12.4	283.1
Payments of debt issuance costs	—	(8.7)
Payment of premium on debt extinguishment	—	(2.4)
Proceeds from equity offering	—	260.9
Payments of equity offering costs	—	(12.7)
Payment of preferred dividends	—	(5.1)
Distributions to non-controlling interest holders	(75.2)	(63.4)
(Payments) receipts related to ownership transactions with non-controlling interest holders	(4.0)	3.4
Other financing activities	(2.9)	(10.9)
Net cash (used in) provided by financing activities	(103.0)	134.8
Net (decrease) increase in cash and cash equivalents	(162.5)	146.6
Cash and cash equivalents at beginning of period	389.9	318.2
Cash and cash equivalents at end of period	$ 227.4	$ 464.8

See notes to unaudited condensed consolidated financial statements.

1. Organization and Summary of Accounting Policies

Organization

Surgery Partners, Inc., a Delaware corporation, acting through its subsidiaries, owns and operates a national network of surgical facilities and ancillary services. The surgical facilities, which include ambulatory surgery centers ("ASCs") and surgical hospitals, primarily provide non-emergency surgical procedures across many specialties, including, among others, gastroenterology, general surgery, ophthalmology, orthopedics and pain management. The Company's surgical hospitals also provide services such as diagnostic imaging, laboratory, obstetrics, oncology, pharmacy, physical therapy and wound care. Ancillary services are comprised of multi-specialty physician practices, urgent care facilities and anesthesia services. Unless the context otherwise indicates, Surgery Partners, Inc. and its subsidiaries are referred to herein as "Surgery Partners," "we," "us," "our" or the "Company."

As of June 30, 2022, the Company owned or operated a portfolio of 133 surgical facilities, comprised of 115 ASCs and 18 surgical hospitals in 32 states. The Company owns these facilities in partnership with physicians and, in some cases, health care systems in the markets and communities it serves. The Company owned a majority interest in 85 of the surgical facilities and consolidated 109 of the facilities for financial reporting purposes.

Basis of Presentation

The accompanying condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for fair presentation of the Company's financial position and results of operations have been included. The Company’s fiscal year ends on December 31 and interim results are not necessarily indicative of results for a full year or any other interim period. The information contained in these condensed consolidated financial statements should be read in conjunction with the Company’s consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2021 (the "2021 Annual Report on Form 10-K").

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, as well as interests in partnerships and limited liability companies controlled by the Company through its ownership of a majority voting interest or other rights granted to the Company by contract to manage and control the affiliate's business. All significant intercompany balances and transactions are eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and footnotes. Examples include, but are not limited to, estimates of accounts receivable allowances, professional and general liabilities and the estimate of deferred tax assets or liabilities. Actual results could differ from those estimates.

Revenues

The Company's revenues generally relate to contracts with patients in which the performance obligations are to provide health care services. The Company recognizes revenues in the period in which its obligations to provide health care services are satisfied and reports the amount that reflects the consideration the Company expects to be entitled to receive. The contractual relationships with patients, in most cases, also involve a third-party payor (e.g., Medicare, Medicaid and private insurance organizations, including plans offered through the health insurance exchanges) and the transaction prices for the services provided are dependent upon the terms provided by or negotiated with the third-party payors. The payment arrangements with third-party payors for the services provided to the related patients typically specify payments at amounts less than the Company's standard charges. The Company continually reviews the contractual estimation process to consider and incorporate updates to laws and regulations and the frequent changes in managed care contractual terms resulting from contract renegotiations and renewals.

A summary of revenues by service type as a percentage of total revenues follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Patient service revenues:				
Surgical facilities revenues	95.9 %	95.5 %	95.8 %	95.5 %
Ancillary services revenues	2.8 %	3.2 %	2.8 %	3.2 %
Total patient service revenues	98.7 %	98.7 %	98.6 %	98.7 %
Other service revenues	1.3 %	1.3 %	1.4 %	1.3 %
Total revenues	100.0 %	100.0 %	100.0 %	100.0 %

Patient service revenues. This revenue is related to charging facility fees in exchange for providing patient care. The fee charged for health care procedures performed in surgical facilities varies depending on the type of service provided, but usually includes all charges for usage of an operating room, a recovery room, special equipment, medical supplies, nursing staff and medications. The fee does not normally include professional fees charged by the patient's surgeon, anesthesiologist or other attending physician, which are billed directly by such physicians to the patient or third-party payor. However, in several surgical facilities, the Company charges for anesthesia services. Ancillary service revenues include fees for patient visits to the Company's physician practices, pharmacy services and diagnostic tests ordered by physicians.

Patient service revenues are recognized as performance obligations are satisfied. Performance obligations are based on the nature of services provided. Typically, the Company recognizes revenue at a point in time in which services are rendered and the Company has no obligation to provide further patient services. As the Company primarily performs outpatient procedures, performance obligations are generally satisfied same day and revenue is recognized on the date of service.

The Company determines the transaction price based on gross charges for services provided, net of estimated contractual adjustments and discounts from third-party payors. The Company estimates its contractual adjustments and discounts based on contractual agreements, its discount policies and historical experience. Changes in estimated contractual adjustments and discounts are recorded in the period of change.

Other service revenues. Other service revenues include management and administrative service fees derived from the non-consolidated facilities that the Company accounts for under the equity method, management of surgical facilities in which it does not own an interest, and management services provided to physician practices for which the Company is not required to provide capital or additional assets. These agreements typically require the Company to provide recurring management services over a multi-year period, which are billed and collected on a monthly basis. The fees derived from these management arrangements are based on a predetermined percentage of the revenues of each facility or practice and are recognized in the period in which management services are rendered and billed.

The following table sets forth patient service revenues by type of payor and as a percentage of total patient service revenues for the Company's consolidated surgical facilities (dollars in millions):

	Three Months Ended June 30,			
	2022		2021	
	Amount	%	Amount	%
Patient service revenues:				
Private insurance	$ 309.5	51.0 %	$ 273.0	50.9
Government	258.1	42.5 %	226.2	42.2
Self-pay	16.5	2.7 %	17.8	3.3
Other [(1)]	23.2	3.8 %	18.9	3.6
Total patient service revenues	607.3	100.0 %	535.9	100.0
Other service revenues	8.1		7.4	
Total revenues	$ 615.4		$ 543.3	

	Six Months Ended June 30,					
	2022			2021		
		Amount	%		Amount	%
Patient service revenues:						
Private insurance	$	608.6	50.9 %	$	519.1	49.8
Government		507.0	42.4 %		452.6	43.5
Self-pay		33.2	2.8 %		31.0	3.0
Other [(1)]		46.2	3.9 %		38.9	3.7
Total patient service revenues		1,195.0	100.0 %		1,041.6	100.0
Other service revenues		16.6			14.1	
Total revenues	$	1,211.6		$	1,055.7	

(1) Other is comprised of anesthesia service agreements, automobile liability, letters of protection and other payor types.

Accounts Receivable

Accounts receivable from third-party payors are recorded net of estimated implicit price concessions, which are estimated based on the historical trend of the Company's surgical hospitals' cash collections and contractual write-offs, and for the Company's surgical facilities in general, established fee schedules, relationships with payors and procedure statistics. While changes in estimated reimbursement from third-party payors remain a possibility, the Company expects that any such changes would be minimal and, therefore, would not have a material effect on its financial condition or results of operations.

Accounts receivable consists of receivables from federal and state agencies (under the Medicare and Medicaid programs), private insurance organizations, employers and patients. Management recognizes that revenues and receivables from government agencies are significant to the Company's operations, but it does not believe that there is significant credit risk associated with these government agencies. Concentration of credit risk with respect to other payors is limited because of the large number of such payors.

The Company recognizes that final reimbursement of accounts receivable is subject to final approval by each third-party payor. However, because the Company has contracts with its third-party payors and also verifies insurance coverage of the patient before medical services are rendered, the amounts that are pending approval from third-party payors are not considered significant. Amounts are classified outside of self-pay if the Company has an agreement with the third-party payor or has verified a patient's coverage prior to services rendered. The Company's policy is to collect co-payments and deductibles prior to providing medical services. Patient services of the Company are primarily non-emergency, which allows the surgical facilities to control the procedures for which third-party reimbursement is sought and obtained. The Company does not require collateral from self-pay patients.

The Company's collection policies and procedures are based on the type of payor, size of claim and estimated collection percentage for each patient account. The Company analyzes accounts receivable at each of its surgical facilities to ensure the proper collection and aged category. Collection efforts include direct contact with third-party payors or patients, written correspondence and the use of legal or collection agency assistance, as required.

Income Taxes

The Company uses the asset and liability method to account for income taxes. Under this method, deferred income tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. If a carryforward exists, the Company makes a determination as to whether the carryforward will be utilized in the future. A valuation allowance is established for certain carryforwards when their recoverability is deemed to be uncertain. The carrying value of the net deferred tax assets assumes that the Company will be able to generate sufficient future taxable income in certain tax jurisdictions, based on estimates and assumptions. If our expectations for future operating results on a consolidated basis or at the state jurisdiction level vary from actual results due to changes in health care regulations, general economic conditions, or other factors, we may need to adjust the valuation allowance, for all or a portion of our deferred tax assets. Our income tax expense in future periods will be reduced or increased to the extent of offsetting decreases or increases, respectively, in our valuation allowance in the period when the change in circumstances occurs. These changes could have a significant impact on our future earnings.

The Company and certain of its subsidiaries file a consolidated federal income tax return. The partnerships, limited liability companies, and certain non-consolidated physician practice corporations also file separate income tax returns. The Company's allocable portion of each partnership's and limited liability company's income or loss is included in taxable income of the Company. The remaining income or loss of each partnership and limited liability company is allocated to the other owners.

The Company's effective tax rate was 8.8% for the six months ended June 30, 2022 compared to (14.6)% for the six months ended June 30, 2021. For the six months ended June 30, 2022, the effective tax rate differed from the federal corporate tax rate of 21% primarily due to earnings attributable to non-controlling interests, an increase in the Company’s valuation allowance attributable to interest expense limitations, and discrete tax benefits of (a) $4.6 million related to the vesting of restricted stock awards, (b) $1.8 million attributable to non-recurring earnings’ impact on the Company’s valuation allowance, and (c) $1.0 million related to entity divestitures. For the six months ended June 30, 2021, the effective tax rate differed from 21% due to tax benefits of $4.1 million related to the vesting of restricted stock awards, as well as a $3.0 million tax benefit related to entity divestitures. Based upon the application of interim accounting guidance, the tax rate as a percentage of net income after income attributable to non-controlling interests will vary based upon the relative net income from period to period.

Goodwill

Goodwill represents the excess of the fair value of the consideration provided in an acquisition plus the fair value of any non-controlling interests over the fair value of net assets acquired and is not amortized. Additions to goodwill include amounts resulting from new business combinations and incremental ownership purchases in the Company's subsidiaries. A summary of the Company's acquisitions and disposals for the six months ended June 30, 2022 is included in Note 2. "Acquisitions and Disposals."

A summary of activity related to goodwill for the six months ended June 30, 2022 is as follows (in millions):

Balance at December 31, 2021	$	3,911.8
Acquisitions, including post acquisition adjustments		110.7
Disposals and deconsolidations		(29.4)
Balance at June 30, 2022	$	3,993.1

A detailed evaluation of potential impairment indicators was performed as of June 30, 2022, which specifically considered the ongoing impact of the COVID-19 pandemic, recent increases in interest rates, inflation risk and market volatility. On the basis of available evidence as of June 30, 2022, no indicators of impairment were identified. Future estimates of fair value could be adversely affected if the actual outcome of one or more of the Company's assumptions changes materially in the future, including a material decline in the Company’s stock price and the fair value of its long-term debt, lower than expected surgical case volumes, higher market interest rates or increased operating costs. Such changes impacting the calculation of fair value could result in a material impairment charge in the future.

Derivative Instruments and Hedging Activities

The Company records all derivatives on the balance sheet at fair value and any financing elements treated as debt instruments are recorded at amortized cost. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts that are intended to economically hedge certain of its risk, even though hedge accounting does not apply or the Company elects not to apply hedge accounting.

The Company made an accounting policy election to measure the credit risk of its derivative financial instruments that are subject to master netting agreements on a net basis by counterparty portfolio.

Non-Controlling Interests—Redeemable

Each partnership and limited liability company through which the Company owns and operates its surgical facilities is governed by a partnership or operating agreement, respectively. In certain circumstances, the applicable partnership or operating agreements for the Company's surgical facilities provide that the facilities will purchase all of the physician limited partners’ or physician minority members’, as applicable, ownership if certain adverse regulatory events occur, such as it becoming illegal for the physician(s) to own an interest in a surgical facility, refer patients to a surgical facility or receive cash distributions from a surgical facility. The non-controlling interests—redeemable are reported outside of stockholders' equity in the condensed consolidated balance sheets.

A summary of activity related to non-controlling interests—redeemable is as follows (in millions):

	Six Months Ended June 30,	
	2022	2021
Balance at beginning of period	$ 330.2	$ 306.8
Net income attributable to non-controlling interests—redeemable	21.6	24.4
Acquisition of shares of non-controlling interests, net—redeemable	12.9	1.9
Distributions to non-controlling interest—redeemable holders	(22.9)	(20.3)
Balance at end of period	$ 341.8	$ 312.8

Medicare Accelerated Payments and Deferred Governmental Grants

The Company has received grant funds distributed under the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act") and other governmental assistance programs, including approximately $1 million during the six months ended June 30, 2022. Grant funds received during the three months ended June 30, 2022 were minimal. During the three and six months ended June 30, 2021, the Company received grant funds of approximately $1 million and $8 million, respectively. The recognition of amounts received is conditioned upon attestation with terms and conditions that funds will be used for COVID-19 related healthcare expenses or lost revenues. Amounts received, but not recognized as a reduction to operating expenses, are reflected as a component of Medicare accelerated payments and deferred governmental grants in the condensed consolidated balance sheets. Any unrecognized amounts may be recognized as a reduction in operating expenses in subsequent periods if the underlying conditions for recognition are met. The Company estimates $0.1 million and $1.3 million of grant funds received qualified for recognition as a reduction in operating expenses for the three and six months ended June 30, 2022, respectively. During the three and six months ended June 30, 2021, $4.9 million and $20.0 million, respectively, was recognized as a reduction in operating expenses. As of both June 30, 2022 and December 31, 2021, approximately $4 million of unrecognized grant funds received was reflected within the condensed consolidated balance sheets.

The Company received accelerated payments under the Medicare Accelerated and Advance Payment Program. The payments received were deferred and included in the condensed consolidated balance sheets. During the three and six months ended June 30, 2022, approximately $25 million and $43 million, respectively, has been repaid in accordance with the terms of the program. These repayments are included as a component of the change in Medicare accelerated payments and deferred government grants in the condensed consolidated statements of cash flows. As of June 30, 2022 and December 31, 2021, the remaining deferred accelerated payments was approximately $17 million and $60 million, respectively, which was included as a component of Medicare accelerated payments and deferred governmental grants in the condensed consolidated balance sheets. The Company does not expect to receive additional Medicare accelerated payments.

The Company's accounting policies for relief received under the CARES Act and other governmental assistance programs, including the recognition of grant funds, is unchanged from the policies described in Note 1 to the Company's consolidated financial statements included in the 2021 Annual Report on Form 10-K.

Fair Value of Financial Instruments

The fair value of a financial instrument is the amount at which the instrument could be exchanged in an orderly transaction between market participants to sell the asset or transfer the liability. The Company uses fair value measurements based on inputs classified into the following hierarchy:

- Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These may include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.
- Level 3: Unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions, depending on the nature of the item being valued.

The carrying amounts reported in the condensed consolidated balance sheets for cash and cash equivalents, accounts receivable, restricted invested assets and accounts payable approximate their fair values under Level 3 calculations.

A summary of the carrying amounts and estimated fair values of the Company's long-term debt follows (in millions):

	Carrying Amount		Fair Value	
	June 30, 2022	December 31, 2021	June 30, 2022	December 31, 2021
Senior secured term loan	$ 1,523.3	$ 1,530.7	$ 1,439.5	$ 1,530.7
6.750% senior unsecured notes due 2025	$ 370.0	$ 370.0	$ 339.0	$ 371.9
10.000% senior unsecured notes due 2027	$ 545.0	$ 545.0	$ 531.4	$ 577.0

The fair values in the table above were based on Level 2 inputs using quoted prices for identical liabilities in inactive markets. The carrying amounts related to the Company's other long-term debt obligations, including finance lease obligations, approximate their fair values based on Level 3 inputs.

Variable Interest Entities

The condensed consolidated financial statements include the accounts of variable interest entities ("VIE") in which the Company is the primary beneficiary under the provisions of the Financial Accounting Standards Board's ("FASB") Accounting Standards Codification 810, "*Consolidation*". The Company has the power to direct the activities that most significantly impact a VIE's economic performance. Additionally, the Company would absorb the majority of the expected losses from any of these entities should such expected losses occur. As of June 30, 2022, the Company's consolidated VIEs include six surgical facilities and five physician practices.

The total assets (excluding goodwill and intangible assets, net) of the consolidated VIEs included in the accompanying condensed consolidated balance sheets as of June 30, 2022 and December 31, 2021 were $69.7 million and $48.1 million, respectively, and the total liabilities of the consolidated VIEs were $44.0 million and $20.1 million, respectively.

2. Acquisitions and Disposals

During the six months ended June 30, 2022, the Company acquired a controlling interest in four surgical facilities, two of which were merged into existing surgical facilities, for aggregate cash consideration of $74.9 million, net of cash acquired, and non-cash consideration of $2.6 million, which consisted of a non-controlling interest in one of the Company's existing surgical facilities. In connection with the acquisitions the Company preliminarily recognized non-controlling interests of $41.5 million and goodwill of $114.4 million.

During the six months ended June 30, 2021, the Company acquired a controlling interest in a surgical facility in a new market and two surgical facilities in existing markets that were merged into existing facilities for aggregate cash consideration of $15.2 million, net of cash acquired. In connection with the acquisitions the Company preliminarily recognized non-controlling interests of $7.5 million and goodwill of $20.0 million. During the six months ended June 30, 2022, no significant changes were made to the purchase price allocation of assets and liabilities, existing at the date of acquisition, related to individual acquisitions completed in 2021.

Other Acquisitions

During the six months ended June 30, 2022, the Company acquired non-controlling interests in five surgical facilities and four in-development de novo surgical facilities for an aggregate cash purchase price of $65.8 million. The non-controlling interests were accounted for as equity method investments and recorded as a component of investments in and advances to affiliates in the accompanying condensed consolidated balance sheets.

Disposals and Deconsolidations

During the six months ended June 30, 2022, the Company sold its interests in a surgical facility, which was previously accounted for as an equity method investment, for net cash proceeds of $11.5 million. The Company recognized a pre-tax loss on the sale of $0.4 million included in loss on disposals and deconsolidations, net in the condensed consolidated statements of operations for the six months ended June 30, 2022.

During the six months ended June 30, 2022, the Company contributed its interests in two surgical facilities as non-cash consideration for non-controlling interests in two new separate entities. As a result of these transactions, the Company lost control of the previously controlled surgical facilities but retains a non-controlling interest in each, resulting in the deconsolidation of the previously consolidated entities. The remaining non-controlling interests were accounted for as equity method investments, and initially measured and recorded at fair value as of the dates of the transactions. The fair value measurement utilizes Level 3 inputs, which includes unobservable data, to measure the fair value of the retained non-controlling interests. The fair value determination was based on a combination of multiple valuation methods, which included discounted cash flow and market value approach, which incorporates estimates of future earnings and market valuation multiples for certain guideline companies. The preliminary fair value of the investments of $9.8 million was recorded as a component of investments in and advances to affiliates in the accompanying condensed consolidated balance sheets. Further, based on the preliminary valuation, the transactions resulted in a pretax net loss on deconsolidations of $5.6 million, which is included in loss on disposals and deconsolidations, net, in the accompanying condensed consolidated statement of operations for the six months ended June 30,

2022. The net loss was determined based on the difference between the fair value of the Company's retained interests in the entities and the carrying values of both the tangible and intangible assets of the entities immediately prior to the transactions.

3. Long-Term Debt

A summary of long-term debt follows (in millions):

	June 30, 2022	December 31, 2021
Senior secured term loan (1)	$ 1,523.3	$ 1,530.7
6.750% senior unsecured notes due 2025	370.0	370.0
10.000% senior unsecured notes due 2027	545.0	545.0
Notes payable and other secured loans	160.2	145.0
Finance lease obligations	504.3	364.6
Less: unamortized debt issuance costs and discounts	(15.1)	(16.5)
Total debt	3,087.7	2,938.8
Less: Current maturities	68.3	60.4
Total long-term debt	$ 3,019.4	$ 2,878.4

(1) Includes unamortized fair value discount of $2.7 million and $3.0 million as of June 30, 2022 and December 31, 2021, respectively.

The increase in finance lease obligations is a result of the modification of certain existing facility real estate leases that were previously classified as operating leases. See Note 4. "Leases" for further discussion.

Revolving Credit Facility

As of June 30, 2022, the Company's availability on its revolving credit facility (the "Revolver") was $203.0 million (including outstanding letters of credit of $7.0 million). There were no outstanding borrowings under the Revolver as of both June 30, 2022 and December 31, 2021.

4. Leases

The Company's operating leases are primarily for real estate, including medical office buildings, and corporate and other administrative offices. The Company's finance leases are primarily for medical equipment and information technology and telecommunications assets.

The following table presents the components of the Company's right-of-use assets and liabilities related to leases and their classification in the consolidated balance sheets (in millions):

	Classification in Consolidated Balance Sheets	June 30, 2022	December 31, 2021
Assets:			
Operating lease assets	Right-of-use operating lease assets	$ 277.8	$ 324.1
Finance lease assets	Property and equipment, net of accumulated depreciation	460.2	329.6
Total leased assets		$ 738.0	$ 653.7
Liabilities:			
Operating lease liabilities:			
Current	Other current liabilities	$ 35.7	$ 40.1
Long-term	Right-of-use operating lease liabilities	271.8	315.6
Total operating lease liabilities		307.5	355.7
Finance lease liabilities:			
Current	Current maturities of long-term debt	22.7	19.0
Long-term	Long-term debt, less current maturities	481.6	345.6
Total finance lease liabilities		504.3	364.6
Total lease liabilities		$ 811.8	$ 720.3

During the six months ended June 30, 2022, the Company extended certain existing facility real estate leases, resulting in the reclassification of the leases from operating to finance. The modifications resulted in an increase to finance lease liabilities and assets of $146.5 million and $145.0 million, respectively, including the reclassification of existing operating lease liabilities and assets of $60.8 million and $59.3 million, respectively.

The following table presents the components of the Company's lease expense and their classification in the condensed consolidated statement of operations (in millions):

	Six Months Ended June 30,	
	2022	2021
Operating lease costs	$ 32.7	$ 37.5
Finance lease costs:		
Amortization of leased assets	18.9	13.8
Interest on lease liabilities	19.7	12.6
Total finance lease costs	38.6	26.4
Variable and short-term lease costs	8.5	9.8
Total lease costs	$ 79.8	$ 73.7

The following table presents supplemental cash flow information (dollars in millions):

	Six Months Ended June 30,	
	2022	2021
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash outflows from operating leases	$ 31.7	$ 36.7
Operating cash outflows from finance leases	$ 19.6	$ 11.9
Financing cash outflows from finance leases	$ 12.1	$ 10.6
Right-of-use assets obtained in exchange for lease obligations:		
Operating leases	$ 31.1	$ 31.4
Finance leases	$ 91.9	$ 6.6

5. Derivatives and Hedging Activities

The Company’s objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps and interest rate caps as part of its interest rate risk management strategy. During 2022 and 2021, such derivatives have been used to hedge the variable cash flows associated with existing variable-rate debt.

For derivatives designated and that qualify as cash flow hedges of interest rate risk, the gain or loss on the derivative is recorded in accumulated other comprehensive income ("OCI") and subsequently reclassified into interest expense in the same period(s) during which the hedged transaction affects earnings, as documented at hedge inception in accordance with the Company’s accounting policy election. Amounts reported in accumulated OCI related to derivatives will be reclassified to interest expense as interest payments are made on the Company’s variable-rate debt. Over the next 12 months, the Company estimates that an additional $7.2 million will be reclassified as a decrease to interest expense.

As of June 30, 2022, the Company had nine interest rate swaps with a total net hedged notional amount of $1.2 billion and two interest rate caps with a total hedged notional amount of $325.9 million. Of the nine interest rate swaps, three are pay-fixed, receive 1-Month LIBOR (subject to a minimum of 0.75%) interest rate swaps designated in cash flow hedging relationships with a total notional amount of $1.2 billion and a termination date of March 31, 2025. The remaining six interest rate swaps are undesignated and consist of three pay-fixed, receive 1-Month LIBOR (subject to a minimum of 1.00%) interest rate swaps and three pay 1-Month LIBOR (subject to a minimum of 1.00%), receive-fixed interest rate swaps with a termination date of November 30, 2023. The pay-floating, receive-fixed swaps are designed to economically offset the undesignated pay-fixed, receive-floating swaps. The interest rate caps each have a termination date of March 31, 2025.

The pay-fixed, receive floating interest rate swaps did not meet the requirements to be considered derivatives in their entirety as a result of the financing component. Accordingly, the swaps are considered hybrid instruments, consisting of a financing element treated as a debt instrument and an embedded at-market derivative that was designated as a cash flow hedge.

Within the Company’s condensed consolidated balance sheets, the financing elements treated as debt instruments described above are carried at amortized cost and the embedded at-market derivatives and the undesignated swaps are recorded at fair value. The cash flows related to the portion treated as debt are classified as financing activities in the condensed consolidated statements of cash flows while the portion treated as an at-market derivative are classified as operating activities. Cash settlements related to the undesignated swaps will offset and are classified as operating activities in the condensed consolidated cash flows. Within the Company’s condensed consolidated balance sheets, the interest rate caps are recorded at fair value. The cash flows related to the interest rate caps are classified as operating activities in the condensed consolidated statements of cash flows.

The key terms of interest rate swaps and interest rate caps outstanding are presented below:

		June 30, 2022		December 31, 2021		
Description	**Effective Date**	**Notional Amount (in millions)**	**Status**	**Notional Amount (in millions)**	**Status**	**Maturity Date**
Pay-fixed swap	May 7, 2021	$ 435.0	Active	$ 435.0	Active	March 31, 2025
Pay-fixed swap	May 7, 2021	330.0	Active	330.0	Active	March 31, 2025
Pay-fixed swap	May 7, 2021	435.0	Active	435.0	Active	March 31, 2025
Interest rate cap	September 30, 2021	163.0	Active	166.8	Active	March 31, 2025
Interest rate cap	September 30, 2021	162.9	Active	166.8	Active	March 31, 2025
Pay-fixed swap	November 30, 2018	165.0	Active	165.0	Active	November 30, 2023
Pay-fixed swap	November 30, 2018	120.0	Active	120.0	Active	November 30, 2023
Pay-fixed swap	June 28, 2019	150.0	Active	150.0	Active	November 30, 2023
Receive-fixed swap	April 30, 2021	(165.0)	Active	(165.0)	Active	November 30, 2023
Receive-fixed swap	April 30, 2021	(120.0)	Active	(120.0)	Active	November 30, 2023
Receive-fixed swap	April 30, 2021	(150.0)	Active	(150.0)	Active	November 30, 2023
		$ 1,525.9		$ 1,533.6		

Our interest rate swap agreements, excluding the portion treated as debt, are recognized at fair value in the condensed consolidated balance sheets and are valued using pricing models that rely on market observable inputs such as yield curve data, which are classified as Level 2 inputs within the fair value hierarchy. The fair value of the interest rate caps are determined using the market standard methodology of discounting the future expected cash receipts that would occur if variable interest rates rise above the strike rate of the caps. The variable interest rates used in the calculation of projected receipts on the caps are based on an expectation of future interest rates derived from observable market interest rate curves and volatilities. The interest rate caps are classified using Level 2 inputs within the fair value hierarchy.

The following table presents the fair values of our derivatives and their location on the condensed consolidated balance sheets (in millions):

		June 30, 2022		December 31, 2021	
	Location	**Assets**	**Liabilities**	**Assets**	**Liabilities**
Derivatives not designated as hedging instruments					
Interest rate swaps	Other long-term assets	$ 2.9	$ —	$ 12.5	$ —
Interest rate swaps	Other long-term liabilities	—	2.9	—	12.4
Derivatives in cash flow hedging relationships					
Interest rate caps	Other long-term assets	13.5	—	2.9	—
Interest rate swaps	Other long-term assets	62.5	—	8.2	—
Interest rate swaps	Other long-term liabilities [(1)]	—	38.8	—	45.8
Total		$ 78.9	$ 41.7	$ 23.6	$ 58.2

(1) The balance as of June 30, 2022 and December 31, 2021 is related to the financing component of the pay-fixed, receive floating interest rate swaps.

The following table presents the pre-tax effect of the interest rate swaps and caps on the Company's accumulated OCI and condensed consolidated statement of operations (in millions):

		Three Months Ended June 30,		Six Months Ended June 30,	
	Location	**2022**	**2021**	**2022**	**2021**
Derivatives not designated as hedging instruments					
(Gain) loss recognized in income	Other income, net	$ —	$ (0.2)	$ 0.1	$ (0.2)
Derivatives in cash flow hedging relationships					
Gain (loss) recognized in OCI (effective portion)		$ 12.7	$ (5.8)	$ 63.1	$ (4.9)
Loss reclassified from accumulated OCI into income (effective portion) [(1)]	Interest expense, net	$ 6.3	$ 6.0	$ 12.7	$ 11.5

(1) Includes amortization of accumulated OCI related to de-designated and terminated interest rate swaps of $5.3 million and $3.2 million for the three months ended June 30, 2022 and 2021, respectively. Includes amortization of accumulated OCI related to de-designated and terminated interest rate swaps of $10.6 million and $3.2 million for the six months ended June 30, 2022 and 2021, respectively.

6. Earnings Per Share

Basic and diluted earnings per share are calculated based on the weighted-average number of shares outstanding in each period and dilutive stock options, unvested shares and warrants, to the extent such securities exist and have a dilutive effect on earnings per share. The Company computes basic and diluted earnings per share using the two-class method. The two-class method of computing earnings per share is an earnings allocation method that determines earnings per share for common shares and participating securities according to their participation rights in dividends and undistributed earnings.

A reconciliation of the numerator and denominator of basic and diluted earnings per share follows (dollars in millions, except per share amounts; shares in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Numerator:				
Net loss attributable to Surgery Partners, Inc.	$ (18.4)	$ (26.9)	$ (6.2)	$ (47.9)
Less: amounts allocated to participating securities [(1)]	—	—	—	(10.3)
Net loss attributable to common stockholders	$ (18.4)	$ (26.9)	$ (6.2)	$ (58.2)
Denominator:				
Weighted average shares outstanding- basic	88,900	69,267	88,450	62,060
Weighted average shares outstanding- diluted [(2)]	88,900	69,267	88,450	62,060
Loss per share:				
Basic	$ (0.21)	$ (0.39)	$ (0.07)	$ (0.94)
Diluted [(2)]	$ (0.21)	$ (0.39)	$ (0.07)	$ (0.94)
Dilutive securities outstanding not included in the computation of loss per share as their effect is antidilutive:				
Stock options	1,559	2,016	1,599	1,901
Restricted shares	628	1,484	644	1,451

(1) Includes dividends accrued for the Series A Preferred Stock for the six months ended June 30, 2021. The Series A Preferred Stock did not participate in undistributed losses and was converted to common stock during the second quarter of 2021. There were no participating securities for the three and six months ended June 30, 2022 and the three months ended June 30, 2021.

(2) The impact of potentially dilutive securities for all periods presented was not considered because the effect would be anti-dilutive.

7. Other Current Liabilities

A summary of other current liabilities is as follows (in millions):

	June 30, 2022	December 31, 2021
Right-of-use operating lease liabilities	$ 35.7	$ 40.1
Interest payable	28.8	29.2
Amounts due to patients and payors	32.5	26.0
Cost report liabilities	22.1	26.4
Tax receivable agreement liability	20.2	19.7
Accrued expenses and other	82.5	68.6
Total	$ 221.8	$ 210.0

8. Commitments and Contingencies

Professional, General and Workers' Compensation Liability Risks

The Company is subject to claims and legal actions in the ordinary course of business, including claims relating to patient treatment, employment practices and personal injuries. The Company maintains professional, general and workers' compensation liability insurance in excess of self-insured retentions through third party commercial insurance carriers. Although management believes the coverage is sufficient for the Company's operations, some claims may potentially exceed the scope of coverage in effect. Plaintiffs in these matters may request punitive or other damages that may not be covered by insurance. The Company is not aware of any such proceedings that are reasonably possible to have a material adverse effect on the Company's business, financial position, results of operations or liquidity. Total professional, general and workers' compensation claim liabilities as of June 30, 2022 and December 31, 2021 were $18.2 million and $19.8 million, respectively. Expected insurance recoveries of $8.7 million as of both June 30, 2022 and December 31, 2021 are included as a component of other current assets and other long-term assets in the condensed consolidated balance sheets.

Laws and Regulations

Laws and regulations governing the Company's business, including those relating to the Medicare and Medicaid programs, are complex and subject to interpretation. These laws and regulations govern every aspect of how the Company's surgical facilities conduct their operations, from licensing requirements to how and whether the Company's facilities may receive payments pursuant to the Medicare and Medicaid programs. Compliance with such laws and regulations can be subject to future government agency review and interpretation as well as legislative changes to such laws. Noncompliance with such laws and regulations may subject the Company to significant regulatory sanctions including fines, penalties, and exclusion from the Medicare, Medicaid and other federal health care programs. From time to time, governmental regulatory agencies will conduct inquiries of the Company's practices, including, but not limited to, the Company's compliance with federal and state fraud and abuse laws, billing practices and relationships with physicians.

Stockholder Litigation

On December 4, 2017, a purported Company stockholder filed an action in the Delaware Court of Chancery (the "Delaware Action"). That action is captioned Witmer v. H.I.G. Capital, L.L.C., et al., C.A. No. 2017-0862. The plaintiff in the Delaware Action asserted claims against (i) certain current and former members of the Company's Board of Directors (together, the "Directors"); (ii) H.I.G. Capital, LLC and certain of its affiliates (collectively, "H.I.G."); and (iii) Bain Capital Private Equity, L.P. and certain of its affiliates (collectively, "Bain Capital" and, together with the Directors and H.I.G., the "Defendants"). The parties to the Delaware Action negotiated a final stipulation of settlement (the "Settlement Stipulation"), which governs the terms of the settlement of the Delaware Action, and which they filed with the Court of Chancery on November 22, 2021. On February 11, 2022, the Court of Chancery approved the settlement of the Delaware Action as memorialized in the Settlement Stipulation. That decision became final and non-appealable on March 14, 2022. The case is now closed. Pursuant to the settlement, the Company received $32.8 million in March 2022, which was included in litigation settlement in the condensed consolidated statements of operations for the six months ended June 30, 2022.

Acquired Facilities

The Company, through its wholly-owned subsidiaries or controlled partnerships and limited liability companies, has acquired and will continue to acquire surgical facilities with prior operating histories. Such facilities may have unknown or contingent liabilities, including liabilities for failure to comply with health care laws and regulations, such as billing and reimbursement laws and regulations, the Stark Law, the Anti-Kickback Statute, the FCA, and similar fraud and abuse laws. Although the Company attempts to assure that no such liabilities exist, obtain indemnification from prospective sellers covering such matters and institute policies designed to conform centers to its standards following completion of acquisitions, there can be no assurance that the Company will not become liable for past activities that may later be asserted to be improper by private plaintiffs or government agencies. There can be no assurance that any such matter will be covered by indemnification or, if covered, that the liability sustained will not exceed contractual limits or the financial capacity of the indemnifying party.

The Company cannot predict whether federal or state statutory or regulatory provisions will be enacted that would prohibit or otherwise regulate relationships which the Company has established or may establish with other health care providers or have materially adverse effects on its business or revenues arising from such future actions. Management believes, however, that it will be able to adjust the Company's operations so as to be in compliance with any statutory or regulatory provision as may be applicable.

Potential Physician Investor Liability

A majority of the physician investors in the partnerships and limited liability companies which operate the Company's surgical facilities carry general and professional liability insurance on a claims-made basis. Each partnership or limited liability company may, however, be liable for damages to persons or property arising from occurrences at the surgical facilities. Although the various physician investors and other surgeons generally are required to obtain general and professional liability insurance with tail coverage that extends beyond the period of any claims-made policies, such individuals may not be able to obtain coverage in amounts sufficient to cover all potential liability. Since most insurance policies contain exclusions, the physician investors will not be insured against all possible occurrences. In the event of an uninsured or underinsured loss, the value of an investment in the partnership interests or limited liability company membership units and the amount of distributions could be adversely affected.

Tax Receivable Agreement

On May 9, 2017, the Company entered into an agreement to amend that certain Income Tax Receivable Agreement, dated September 30, 2015 (as amended, the "TRA"), by and between the Company, and the other parties referred to therein, which amendment became effective on August 31, 2017. Pursuant to the amendment to the TRA, the Company agreed to make payments to H.I.G., the Company's former controlling shareholder, in its capacity as the stockholders representative pursuant to a fixed payment schedule. The amounts payable under the TRA are calculated as the product of (i) an annual base amount and (ii) the maximum corporate federal income tax rate for the applicable year plus three percent. The amounts payable under the TRA are related to the Company’s projected realized tax savings over the next five years and are not dependent on the Company’s actual tax savings over such period. The calculation of amounts payable pursuant to the TRA is thus dependent on the maximum corporate federal income tax rate. To the extent that the Company is unable to make payments under the TRA, such payments will be deferred and will accrue interest at a rate of the LIBOR plus 500 basis points until paid. If the terms of credit agreements and other debt documents cause the Company to be unable to make payments under the TRA and such terms are not materially more restrictive than those existing as of September 30, 2015, such payments will be deferred and will accrue interest at a rate of LIBOR plus 300 basis points until paid.

Assuming the Company's tax rate is 24%, calculated as the maximum corporate federal tax rate plus three percent, throughout the remaining term of the TRA, the Company estimates the total remaining amounts payable under the TRA was approximately $22.0 million as of both June 30, 2022 and December 31, 2021. As a result of the amendment to the TRA, the Company was required to value the liability under the TRA by discounting the fixed payment schedule using the Company’s incremental borrowing rate. The carrying value of the liability under the TRA, reflecting the discount, was $20.7 million and $19.7 million as of June 30, 2022 and December 31, 2021, respectively. The current portion of the liability was $20.2 million and $19.7 million as of June 30, 2022 and December 31, 2021, respectively, and is included as a component of other current liabilities in the condensed consolidated balance sheets. The long-term portion is included as a component of other long-term liabilities in the condensed consolidated balance sheets.

9. Segment Reporting

The Company currently operates in two major lines of business that are also the Company's reportable operating segments - the operation of surgical facilities and the operation of ancillary services. The Surgical Facility Services segment consists of the operation of ASCs, surgical hospitals and anesthesia services. The Ancillary Services segment consists of multi-specialty physician practices. The "All other" line item primarily consists of the Company's corporate general and administrative functions.

The following tables present financial information for each reportable segment (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Revenues:				
Surgical Facility Services	$ 597.9	$ 525.8	$ 1,176.7	$ 1,021.6
Ancillary Services	17.5	17.5	34.9	34.1
Total	$ 615.4	$ 543.3	$ 1,211.6	$ 1,055.7
Adjusted EBITDA:				
Surgical Facility Services	$ 108.7	$ 95.6	$ 209.7	$ 190.6
Ancillary Services	(0.8)	(0.1)	(0.7)	(1.0)
All other	(21.8)	(19.6)	(45.8)	(40.8)
Total	$ 86.1	$ 75.9	$ 163.2	$ 148.8
Reconciliation of Adjusted EBITDA:				
Income before income taxes	$ 19.6	$ 6.1	$ 63.7	$ 17.1
Net income attributable to non-controlling interests	(33.7)	(35.7)	(64.3)	(67.5)
Depreciation and amortization	28.0	25.2	55.4	50.9
Interest expense, net	56.9	53.4	113.2	106.7
Equity-based compensation expense	4.3	4.1	8.0	9.3
Transaction, integration and acquisition costs (1)	8.2	11.4	15.3	20.8
Loss on disposals and deconsolidations, net	1.1	1.0	1.0	0.1
Loss (gain) on litigation settlement and other litigation costs (2)	1.7	0.8	(29.1)	1.8
Loss on debt extinguishment	—	9.6	—	9.6
Adjusted EBITDA	$ 86.1	$ 75.9	$ 163.2	$ 148.8

(1) This amount includes transaction and integration costs of $8.2 million and $9.2 million for the three months ended June 30, 2022 and 2021, respectively. This amount further includes start-up costs related to a de novo surgical hospital of $2.2 million for the three months ended June 30, 2021.

This amount includes transaction and integration costs of $15.3 million and $14.5 million for the six months ended June 30, 2022 and 2021, respectively. This amount further includes start-up costs related to a de novo surgical hospital of $6.3 million for the six months ended June 30, 2021.

(2) This amount includes other litigation costs of $1.7 million and $0.8 million for the three months ended June 30, 2022 and 2021, respectively.

This amount includes other litigation costs of $3.7 million and $1.8 million for the six months ended June 30, 2022 and 2021, respectively. This amount also includes gain on litigation settlement of $32.8 million for the six months ended June 30, 2022.

	June 30, 2022	December 31, 2021
Assets:		
Surgical Facility Services	$ 5,691.3	$ 5,552.8
Ancillary Services	44.5	47.5
All other	555.8	517.3
Total assets	$ 6,291.6	$ 6,117.6

	Six Months Ended June 30,	
	2022	2021
Cash purchases of property and equipment:		
Surgical Facility Services	$ 36.9	$ 27.2
Ancillary Services	0.5	0.2
All other	3.2	0.6
Total cash purchases of property and equipment	$ 40.6	$ 28.0

10. Subsequent Events

In July 2022, the Company acquired non-controlling interests in two surgical facilities and three in-development de novo surgical facilities for a combined purchase price of $29.3 million. The non-controlling interests will be accounted for as equity method investments.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and related notes included elsewhere in this report and our 2021 Annual Report on Form 10-K. Unless the context otherwise indicates, the terms "Surgery Partners," "we," "us," "our" or the "Company," as used herein, refer to Surgery Partners, Inc. and its subsidiaries. Unless the context implies otherwise, the term “affiliates” means direct and indirect subsidiaries of Surgery Partners, Inc. and partnerships and joint ventures in which such subsidiaries are partners. The terms “facilities” or “hospitals” refer to entities owned and operated by affiliates of Surgery Partners, Inc. and the term “employees” refers to employees of affiliates of Surgery Partners, Inc.

Cautionary Note Regarding Forward-Looking Statements

This report contains forward-looking statements, which are based on our current expectations, estimates and assumptions about future events. All statements other than statements of current or historical fact contained in this report are forward-looking statements. These statements include, but are not limited to, statements regarding our future financial position, business strategy, budgets, effective tax rate, projected costs and plans and objectives of management for future operations. The words "projections," "believe," "continue," "drive," "estimate," "expect," "intend," "may," "plan," "will," "could," "would" and similar expressions are generally intended to identify forward-looking statements. These statements involve risks, uncertainties and other factors that may cause actual results to differ from the expectations expressed in the statements. Many of these factors are beyond our ability to control or predict. These factors include, without limitation, the effects of the ongoing COVID-19 pandemic in the United States and the regions in which we operate; the impact to the state and local economies of restrictive orders, vaccine and other mandates and the pandemic generally; our ability to respond nimbly to challenging economic conditions, including recent inflationary pressures; the unpredictability of our case volume in the current environment; our ability to preserve or raise sufficient funds to continue operations throughout this period of uncertainty; the impact of our cost-cutting measures on our future performance; our ability to cause distributions from our subsidiaries; the responsiveness of our payors, including Medicaid and Medicare, to the challenging operating conditions, including their willingness and ability to continue paying in a timely manner and to advance payments in a timely manner, if at all; the impact of COVID-19 related stimulus programs, including the CARES Act, and uncertainty in how these programs may be administered, monitored and modified in the future; our ability to execute on our operational and strategic initiatives; the timing and impact of our portfolio optimization efforts; our ability to continue to improve same-facility volume and revenue growth on the timeline anticipated, if at all; our ability to successfully integrate acquisitions; the anticipated impact and timing of our ongoing efficiency efforts; the impact of adverse weather conditions and other events outside of our control; and the risks and uncertainties set forth under the heading "Risk Factors" in our 2021 Annual Report on Form 10-K and discussed from time to time in our reports filed with the SEC.

Considering these risks, uncertainties and assumptions, the forward-looking events and circumstances discussed in this report may not occur, and actual results could differ materially from those anticipated or implied in the forward-looking statements. When you consider these forward-looking statements, you should keep in mind these risk factors and other cautionary statements in this report.

These forward-looking statements speak only as of the date made. Other than as required by law, we undertake no obligation to publicly update or revise any forward-looking statements, whether because of new information, future events or otherwise.

Executive Overview

Total revenues for the second quarter of 2022 increased 13.3% to $615.4 million from $543.3 million for the second quarter of 2021. Days adjusted same-facility revenues for the second quarter of 2022 increased 6.9% from the same period last year, with a 4.9% increase in revenue per case and a 1.9% increase in same-facility cases. For the second quarter of 2022, the Company’s net loss attributable to common stockholders and Adjusted EBITDA was $18.4 million and $86.1 million, respectively. For the second quarter of 2021, the Company’s net loss attributable to common stockholders and Adjusted EBITDA was $26.9 million and $75.9 million, respectively. A reconciliation of non-GAAP financial measures appears below under "Certain Non-GAAP Measures."

We had cash and cash equivalents of $227.4 million and $203.0 million of borrowing capacity under our revolving credit facility at June 30, 2022. Operating cash inflows were $42.1 million in the second quarter of 2022, an increase of $39.8 million compared to the prior year period. Net operating cash flows, including operating cash flows less distributions to non-controlling interests, were an inflow of $3.1 million for the second quarter of 2022, compared to an outflow of $29.8 million for the second quarter of 2021. The increase in operating cash flows and net operating cash flows compared to the same period in 2021 is primarily due to a DOJ settlement payment made in the 2021 period.

COVID-19 Pandemic

The public health and economic effects of the COVID-19 pandemic have significantly affected our facilities, employees, patients, communities, business operations and financial performance, as well as the U.S. economy and financial markets. The impact of the COVID-19 pandemic on our surgical facilities varies based on the market in which the facility operates, the type of surgical facility and the procedures typically performed. We cannot provide any certainty regarding the length and severity of the impact of the COVID-19 pandemic, which is difficult to predict and is dependent on factors beyond our control.

Taking into account the pandemic and other factors, the United States economy has recently experienced general inflationary pressures, significant disruptions to global supply networks, and an extremely competitive labor market. We have incurred, and may continue to incur, certain increased expenses arising from the pandemic and these economic conditions, including additional labor, supply chain, capital and other expenditures. While we have implemented cost containment and other measures to try to counteract these developments, we may be unable to fully offset these increases in our costs and otherwise effectively respond to supply disruptions.

The Company is monitoring legislative actions at federal and state levels, including the impact of the CARES Act and other governmental assistance that might be available.

Revenues

Our revenues consist of patient service revenues and other service revenues. Patient service revenues consist of revenue from our surgical facility services and ancillary services segments. Specifically, patient service revenues include fees for surgical or diagnostic procedures performed at surgical facilities that we consolidate for financial reporting purposes, as well as for patient visits to our physician practices, anesthesia services, pharmacy services and diagnostic screens ordered by our physicians. Other service revenues include management and administrative service fees derived from our non-consolidated facilities that we account for under the equity method, management of surgical facilities and physician practices in which we do not own an interest and management services we provide to physician practices for which we are not required to provide capital or additional assets.

The following table summarizes our revenues by service type as a percentage of total revenues for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Patient service revenues:				
Surgical facilities revenues	95.9 %	95.5 %	95.8 %	95.5 %
Ancillary services revenues	2.8 %	3.2 %	2.8 %	3.2 %
Total patient service revenues	98.7 %	98.7 %	98.6 %	98.7 %
Other service revenues	1.3 %	1.3 %	1.4 %	1.3 %
Total revenues	100.0 %	100.0 %	100.0 %	100.0 %

Payor Mix

The following table sets forth by type of payor the percentage of our patient service revenues generated at the surgical facilities which we consolidate for financial reporting purposes in the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Private insurance payors	51.0 %	50.9 %	50.9 %	49.8 %
Government payors	42.5 %	42.2 %	42.4 %	43.5 %
Self-pay payors	2.7 %	3.3 %	2.8 %	3.0 %
Other payors (1)	3.8 %	3.6 %	3.9 %	3.7 %
Total	100.0 %	100.0 %	100.0 %	100.0 %

(1) Other is comprised of anesthesia service agreements, automobile liability, letters of protection and other payor types.

Surgical Case Mix

We primarily operate multi-specialty surgical facilities where physicians perform a variety of procedures in various specialties. We believe this diversification helps to protect us from adverse pricing and utilization trends in any individual procedure type and results in greater consistency in our case volume.

The following table sets forth the percentage of cases in each specialty performed at the surgical facilities which we consolidate for financial reporting purposes for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Orthopedic and pain management	35.6 %	35.2 %	36.2 %	36.3 %
Ophthalmology	24.5 %	26.9 %	24.5 %	26.2 %
Gastrointestinal	23.2 %	22.3 %	23.0 %	21.9 %
General surgery	3.0 %	2.9 %	3.0 %	3.0 %
Other	13.7 %	12.7 %	13.3 %	12.6 %
Total	100.0 %	100.0 %	100.0 %	100.0 %

Critical Accounting Policies

A summary of significant accounting policies is disclosed in our 2021 Annual Report on Form 10-K under the caption “Critical Accounting Policies” in the Management’s Discussion and Analysis of Financial Condition and Results of Operations section. There have been no material changes in the nature of our critical accounting policies or the application of those policies since December 31, 2021.

Results of Operations

Three Months Ended June 30, 2022 Compared to Three Months Ended June 30, 2021

The following table summarizes certain results from the statements of operations for the three months ended June 30, 2022 and 2021 (dollars in millions):

	Three Months Ended June 30,	
	2022	2021
Revenues	$ 615.4	$ 543.3
Operating expenses:		
Cost of revenues	480.8	425.0
General and administrative expenses	26.1	24.5
Depreciation and amortization	28.0	25.2
Transaction and integration costs	8.2	9.2
Grant funds	(0.1)	(4.9)
Loss on disposals and deconsolidations, net	1.1	1.0
Equity in earnings of unconsolidated affiliates	(2.6)	(3.0)
Loss on debt extinguishment	—	9.6
Other income, net	(2.6)	(2.8)
	538.9	483.8
Operating income	76.5	59.5
Interest expense, net	(56.9)	(53.4)
Income before income taxes	19.6	6.1
Income tax (expense) benefit	(4.3)	2.7
Net income	15.3	8.8
Less: Net income attributable to non-controlling interests	(33.7)	(35.7)
Net loss attributable to Surgery Partners, Inc.	$ (18.4)	$ (26.9)

Overview. During the three months ended June 30, 2022, our revenues increased 13.3% to $615.4 million compared to $543.3 million for the three months ended June 30, 2021. Net loss attributable to Surgery Partners, Inc. was $18.4 million for the 2022 period, compared to a net loss of $26.9 million for the 2021 period. The increase in revenues was primarily attributable to a favorable shift in surgical case mix and acquisitions completed since the prior year period.

Revenues. Revenues for the three months ended June 30, 2022 compared to the three months ended June 30, 2021 were as follows (dollars in millions):

	Three Months Ended June 30,	
	2022	2021
Patient service revenues	$ 607.3	$ 535.9
Other service revenues	8.1	7.4
Total revenues	$ 615.4	$ 543.3

Patient service revenues increased 13.3% to $607.3 million for the 2022 period compared to $535.9 million for the 2021 period, primarily driven by a 4.9% increase in same-facility revenue per case, a 1.9% increase in days adjusted same-facility case volumes and acquisitions completed since the prior year period.

Cost of Revenues. Cost of revenues increased to $480.8 million for the 2022 period compared to $425.0 million for the 2021 period, primarily driven by acquisitions completed since the prior year period. As a percentage of revenues, cost of revenues were 78.1% for the 2022 period compared to 78.2% for the 2021 period.

General and Administrative Expenses. As a percentage of revenues, general and administrative expenses decreased to 4.2% for the 2022 period compared to 4.5% for the 2021 period.

Depreciation and Amortization. As a percentage of revenues, depreciation and amortization expenses were 4.5% for the 2022 period compared to 4.6% for the 2021 period.

Transaction and Integration Costs. We incurred $8.2 million of transaction and integration costs for the three months ended June 30, 2022 compared to $9.2 million for the three months ended June 30, 2021. The costs for both periods primarily relate to ongoing development initiatives and the integration of acquisitions.

Grant Funds. Based on guidance from HHS and other authorities, the Company updated its estimate of the amount of grant funds received that qualified for recognition, resulting in the recognition of $0.1 million during the three months ended June 30, 2022. Grant funds recognized in the three months ended June 30, 2021 were $4.9 million. For further discussion, see Note 1 to our condensed consolidated financial statements included elsewhere in this report.

Loss on Debt Extinguishment. We incurred a loss on debt extinguishment of $9.6 million for the 2021 period related to an amendment to our credit agreement, which refinanced all of the then existing term loans during the three months ended June 30, 2021. There was no comparable loss during the 2022 period.

Interest Expense, Net. As a percentage of revenues, interest expense, net decreased to 9.2% for the 2022 period compared to 9.8% for the 2021 period.

Income Tax (Expense) Benefit. The income tax expense was $4.3 million for the three months ended June 30, 2022 compared to a benefit of $2.7 million for the three months ended June 30, 2021. The effective tax rate was 21.9% for the three months ended June 30, 2022 compared to (44.3)% for the three months ended June 30, 2021. For the three months ended June 30, 2022, the effective tax rate differed from 21% primarily due to earnings attributable to non-controlling interests and an increase in the Company's valuation allowance attributable to interest expense limitations. For the three months ended June 30, 2021, the effective tax rate differed from 21% primarily due to tax benefits of $3.0 million related to entity divestitures. Based upon the application of interim accounting guidance, the tax rate as a percentage of net income after income attributable to non-controlling interests will vary based upon the relative net income from period to period.

Net Income Attributable to Non-Controlling Interests. As a percentage of revenues, net income attributable to non-controlling interests was 5.5% for the 2022 period and 6.6% for the 2021 period.

Six Months Ended June 30, 2022 Compared to Six Months Ended June 30, 2021

The following table summarizes certain results from the statements of operations for the six months ended June 30, 2022 and 2021 (dollars in millions):

	Six Months Ended June 30,	
	2022	2021
Revenues	$ 1,211.6	$ 1,055.7
Operating expenses:		
Cost of revenues	952.2	833.9
General and administrative expenses	55.6	51.3
Depreciation and amortization	55.4	50.9
Transaction and integration costs	15.3	14.5
Grant funds	(1.3)	(20.0)
Loss on disposals and deconsolidations, net	1.0	0.1
Equity in earnings of unconsolidated affiliates	(5.7)	(5.6)
Litigation settlement	(32.8)	—
Loss on debt extinguishment	—	9.6
Other income, net	(5.0)	(2.8)
	1,034.7	931.9
Operating income	176.9	123.8
Interest expense, net	(113.2)	(106.7)
Income before income taxes	63.7	17.1
Income tax (expense) benefit	(5.6)	2.5
Net income	58.1	19.6
Less: Net income attributable to non-controlling interests	(64.3)	(67.5)
Net loss attributable to Surgery Partners, Inc.	$ (6.2)	$ (47.9)

Overview. During the six months ended June 30, 2022, our revenues increased 14.8% to $1,211.6 million compared to $1,055.7 million for the six months ended June 30, 2021. Net loss attributable to Surgery Partners, Inc. was $6.2 million for the 2022 period, compared to a net loss of $47.9 million for the 2021 period. The increase in revenues was primarily attributable to increases in surgical case volumes, a favorable shift in surgical case mix and acquisitions completed since the prior-year period.

Revenues. Revenues for the six months ended June 30, 2022 compared to the six months ended June 30, 2021 were as follows (dollars in millions):

	Six Months Ended June 30,	
	2022	2021
Patient service revenues	$ 1,195.0	$ 1,041.6
Other service revenues	16.6	14.1
Total revenues	$ 1,211.6	$ 1,055.7

Patient service revenues increased 14.7% to $1,195.0 million for the 2022 period compared to $1,041.6 million for the 2021 period, primarily driven by a 4.0% increase in days adjusted same-facility case volume, a 3.2% increase in same-facility revenue per case and acquisitions completed since the prior year period.

Cost of Revenues. Cost of revenues were $952.2 million for the 2022 period compared to $833.9 million for the 2021 period, primarily driven by acquisitions completed since the prior year period. As a percentage of revenues, cost of revenues decreased to 78.6% for the 2022 period compared to 79.0% for the 2021 period.

General and Administrative Expenses. As a percentage of revenues, general and administrative expenses decreased to 4.6% for the 2022 period compared to 4.9% for the 2021 period.

Depreciation and Amortization. As a percentage of revenues, depreciation and amortization expenses decreased to 4.6% for the 2022 period compared to 4.8% for the 2021 period.

Transaction and Integration Costs. We incurred $15.3 million of transaction and integration costs for the six months ended June 30, 2022 compared to $14.5 million for the six months ended June 30, 2021. The increase primarily relates to costs for ongoing development initiatives and the integration of acquisitions we completed in 2022 and 2021.

Grant Funds. Based on guidance from HHS and other authorities, the Company updated its estimate of the amount of grant funds received that qualified for recognition, resulting in the recognition of $1.3 million during the six months ended June 30, 2022. Grant funds recognized in the six months ended June 30, 2021 were $20.0 million. For further discussion, see Note 1 to our condensed consolidated financial statements included elsewhere in this report.

Litigation Settlement. Gain on litigation settlement was $32.8 million for the six months ended June 30, 2022, related to the resolution of the stockholder litigation matter, as discussed in Note 8. "Commitments and Contingencies" to our condensed consolidated financial statements included elsewhere in this report. There was no comparable activity for the 2021 period.

Loss on Debt Extinguishment. We incurred a loss on debt extinguishment of $9.6 million for the 2021 period related to an amendment to our credit agreement, which refinanced all of the then existing term loans during the six months ended June 30, 2021. There was no comparable loss during the 2022 period.

Interest Expense, Net. As a percentage of revenues, interest expense, net decreased to 9.3% for the 2022 period compared to 10.1% for the 2021 period.

Income Tax (Expense) Benefit. The income tax expense was $5.6 million for the six months ended June 30, 2022 compared to a benefit of $2.5 million for the six months ended June 30, 2021. The effective tax rate was 8.8% for the six months ended June 30, 2022 compared to (14.6)% for the six months ended June 30, 2021. For the six months ended June 30, 2022, the effective tax rate differed from 21% primarily due to earnings attributable to non-controlling interests, an increase in the Company’s valuation allowance attributable to interest expense limitations, and discrete tax benefits of (a) $4.6 million related to the vesting of restricted stock awards, (b) $1.8 million attributable to non-recurring earnings’ impact on the Company’s valuation allowance, and (c) $1.0 million related to entity divestitures. For the six months ended June 30, 2021, the effective tax rate differed from 21% due to tax benefits of $4.1 million related to the vesting of restricted stock awards, as well as a $3.0 million tax benefit related to entity divestitures. Based upon the application of interim accounting guidance, the tax rate as a percentage of net income after income attributable to non-controlling interests will vary based upon the relative net income from period to period.

Net Income Attributable to Non-Controlling Interests. As a percentage of revenues, net income attributable to non-controlling interests was 5.3% for the 2022 period and 6.4% for the 2021 period.

Liquidity and Capital Resources

The primary source of our operating cash flow is the collection of accounts receivable from federal and state agencies (under the Medicare and Medicaid programs), private insurance companies and individuals. During the six months ended June 30, 2022, our cash flow provided by operating activities was $121.9 million compared to $52.5 million in the six months ended June 30, 2021. The increase is primarily due to the receipt of stockholder litigation proceeds of $32.8 million in the 2022 period and a DOJ settlement payment of $32.2 million made during the 2021 period.

Net cash used in investing activities during the six months ended June 30, 2022, was $181.4 million compared to $40.7 million for the six months ended June 30, 2021. The increase in cash used is primarily due to an increase of $12.6 million related to purchases of property and equipment, an increase of $59.7 million for acquisitions (net of cash acquired), an increase of $65.8 million for purchases of equity method investments, a decrease of $2.5 million in cash proceeds from divestitures and an increase in other investing activities of $11.6 million. The increases in cash used in investing activities were partially offset by an increase of $11.5 million related to the sale of equity method investments.

Net cash used in financing activities during the six months ended June 30, 2022 was $103.0 million compared to cash provided by financing activities of $134.8 million for the six months ended June 30, 2021. The decrease is primarily due to $248.2 million of proceeds received from an equity offering, net of related costs in the 2021 period, with no comparable activity in the 2022 period, an increase of $11.8 million for distributions to non-controlling interest holders and an increase of $7.4 million of net payments related to ownership transactions with consolidated affiliates. The increases in cash used in financing activities were partially offset by a decrease of $5.4 million in repayments of long-term debt, net of borrowings, a decrease of $11.1 million related to payments of deferred financing costs and a prepayment premium related to the modification of the term loan in the 2021 period, a decrease of $5.1 million for preferred dividends and a decrease in other financing activities of $8.0 million.

Capital Resources

Net working capital was approximately $266.7 million at June 30, 2022 compared to $409.3 million at December 31, 2021. The decrease is due to a decrease in cash, primarily as a result of payments for acquisitions, a decrease in accounts receivable and an increase in accrued payroll and benefits, offset by a decrease in deferred Medicare accelerated payments.

In addition to cash flows from operations and available cash, other sources of capital include amounts available on our Revolver as well as anticipated continued access to the capital markets.

Material Cash Requirements

In addition to the cash requirements related to our long-term debt, operating lease obligations and the tax receivable agreement, pursuant to the CARES Act, repayment of certain advanced payments and other deferrals received as part of relief during 2020 will continue during 2022.

We received approximately $120 million of accelerated payments during the year ended December 31, 2020. Through June 30, 2022, approximately $103 million has been repaid including approximately $25 million and $43 million during the three and six months ended June 30, 2022, respectively. In addition to the continued repayment of the advanced payments received under the CARES Act, we anticipate additional cash outflows during 2022 for the repayment of the remaining payroll taxes deferred in 2020 pursuant to the CARES Act.

There have been no material changes outside of the ordinary course of business to our upcoming cash obligations during the six months ended June 30, 2022 from those disclosed under “Material Cash Requirements” in Management’s Discussion and Analysis of Financial Condition and Results of Operations in our 2021 Annual Report on Form 10-K.

Summary

Broad economic factors resulting from the ongoing COVID-19 pandemic could negatively affect our payor mix, increase the relative proportion of lower margin services we provide and reduce patient volumes, as well as diminish our ability to collect outstanding receivables. Additionally, while we have received grants and accelerated payments under the CARES Act and other government assistance programs and may receive additional amounts in the future, there is no assurance regarding the extent to which anticipated negative impacts arising from the COVID-19 pandemic will be offset by amounts and benefits received under the CARES Act or future legislation. Business closings and layoffs in the areas in which we operate may lead to increases in the uninsured and underinsured populations and adversely affect demand for our services, as well as the ability of payors to pay for services as rendered. Any increase in the amount or deterioration in the collectability of patient accounts receivable will adversely affect our cash flows and results of operations, requiring an increased level of working capital.

If general economic conditions, including recent increases in interest rates, inflation risk and market volatility continue to deteriorate or remain uncertain for an extended period of time, our ability to access capital could be harmed, which could negatively affect our liquidity and ability to repay our outstanding debt.

Based on our current level of operations, we believe cash flows from operations, available cash, available capacity on our Revolver and continued anticipated access to capital markets, will be adequate to meet our short-term (i.e., 12 months) and long-term (beyond 12 months) liquidity needs.

Certain Non-GAAP Measures

Adjusted EBITDA and Adjusted EBITDA excluding grant funds are not measurements of financial performance under GAAP and should not be considered in isolation or as a substitute for net income, operating income or any other measure calculated in accordance with GAAP. The items excluded from these non-GAAP metrics are significant components in understanding and evaluating our financial performance. We believe such adjustments are appropriate, as the magnitude and frequency of such items can vary significantly and are not related to the assessment of normal operating performance. Our calculation of Adjusted EBITDA and Adjusted EBITDA excluding grant funds may not be comparable to similarly titled measures reported by other companies. We use Adjusted EBITDA and Adjusted EBITDA excluding grant funds as measures of financial performance. Adjusted EBITDA and Adjusted EBITDA excluding grant funds are key measures used by our management to assess operating performance, make business decisions and allocate resources.

The following table reconciles Adjusted EBITDA and Adjusted EBITDA excluding grant funds to income before income taxes, the most directly comparable GAAP financial measure (in millions and unaudited):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2022	2021	2022	2021
Condensed Consolidated Statements of Operations Data:				
Income before income taxes	$ 19.6	$ 6.1	$ 63.7	$ 17.1
Plus (minus):				
Net income attributable to non-controlling interests	(33.7)	(35.7)	(64.3)	(67.5)
Depreciation and amortization	28.0	25.2	55.4	50.9
Interest expense, net	56.9	53.4	113.2	106.7
Equity-based compensation expense	4.3	4.1	8.0	9.3
Transaction, integration and acquisition costs (1)	8.2	11.4	15.3	20.8
Loss on disposals and deconsolidations, net	1.1	1.0	1.0	0.1
Loss (gain) on litigation settlement and other litigation costs (2)	1.7	0.8	(29.1)	1.8
Loss on debt extinguishment	—	9.6	—	9.6
Adjusted EBITDA	$ 86.1	$ 75.9	$ 163.2	$ 148.8
Less: Impact of grant funds (3)	(0.1)	(2.9)	(1.1)	(13.7)
Adjusted EBITDA excluding grant funds	$ 86.0	$ 73.0	$ 162.1	$ 135.1

(1) This amount includes transaction and integration costs of $8.2 million and $9.2 million for the three months ended June 30, 2022 and 2021, respectively. This amount further includes start-up costs related to a de novo surgical hospital of $2.2 million for the three months ended June 30, 2021.

This amount includes transaction and integration costs of $15.3 million and $14.5 million for the six months ended June 30, 2022 and 2021, respectively. This amount further includes start-up costs related to a de novo surgical hospital of $6.3 million for the six months ended June 30, 2021.

(2) This amount includes other litigation costs of $1.7 million and $0.8 million for the three months ended June 30, 2022 and 2021, respectively.

This amount includes other litigation costs of $3.7 million and $1.8 million for the six months ended June 30, 2022 and 2021, respectively. This amount also includes gain on litigation settlement of $32.8 million for the six months ended June 30, 2022.

(3) Represents the impact of grant funds recognized, net of amounts attributable to non-controlling interests.

We use Credit Agreement EBITDA as a measure of liquidity and to determine our compliance under certain covenants pursuant to our credit facilities. Credit Agreement EBITDA is determined on a trailing twelve-month basis. We have included it because we believe that it provides investors with additional information about our ability to incur and service debt and make capital expenditures. Credit Agreement EBITDA is not a measurement of liquidity under GAAP and should not be considered in isolation or as a substitute for any other measure calculated in accordance with GAAP. The items excluded from Credit Agreement EBITDA are significant components in understanding and evaluating our liquidity. Our calculation of Credit Agreement EBITDA may not be comparable to similarly titled measures reported by other companies.

When we use the term “Credit Agreement EBITDA,” we are referring to Adjusted EBITDA, as defined above, further adjusted for acquisitions and synergies. These adjustments do not relate to our historical financial performance and instead relate to estimates compiled by our management and calculated in conformance with the definition of “Consolidated EBITDA” used in the credit agreements governing our credit facilities.

The following table reconciles Credit Agreement EBITDA to cash flows from operating activities, the most directly comparable GAAP financial measure (in millions and unaudited):

	Twelve Months Ended June 30, 2022
Cash flows from operating activities	$ 156.5
Plus (minus):	
Non-cash interest expense, net	(28.7)
Non-cash lease expense	(36.2)
Deferred income taxes	(17.0)
Equity in earnings of unconsolidated affiliates, net of distributions received	(0.2)
Changes in operating assets and liabilities, net of acquisitions and divestitures	156.8
Income tax expense	18.6
Net income attributable to non-controlling interests	(138.4)
Interest expense, net	227.5
Transaction, integration and acquisition costs	40.6
Litigation settlement and other litigation costs	(25.3)
Hurricane-related impacts (1)	(0.2)
Acquisitions and synergies (2)	84.7
Credit Agreement EBITDA	$ 438.7

(1) Reflects the impact of insurance proceeds received net of operating losses incurred in the six months ended December 31, 2021, at a surgical facility that was closed following Hurricane Ida.

(2) Represents impact of acquisitions as if each acquisition had occurred on July 1, 2021. Further this includes revenue and cost synergies from other business initiatives and de novo facilities and an adjustment for the effects of adopting the new lease accounting standard, as defined in the credit agreement governing the Senior Secured Credit Facilities.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risk primarily from exposure to changes in interest rates based on our financing, investing and cash management activities. We utilize a balanced mix of maturities along with both fixed rate and variable rate debt to manage our exposures to changes in interest rates. Additionally, we periodically enter into interest rate swap and cap agreements to manage our exposure to interest rate fluctuations. Our interest rate swap and cap agreements involve the exchange of fixed and variable rate interest payments between two parties, based on common notional principal amounts and maturity dates. The notional amounts of the interest rate swap and cap agreements represent balances used to calculate the exchange of cash flows and are not our assets or liabilities. Our credit risk related to these agreements is considered low because the interest rate swap and cap agreements are with creditworthy financial institutions. The interest payments under these agreements are settled on a net basis. These derivatives have been recognized in the financial statements at their respective fair values. Changes in the fair value of these derivatives, which are designated as cash flow hedges, are included in other comprehensive income.

Our variable rate debt instruments are primarily indexed to the prime rate or LIBOR. Without derivatives, interest rate changes would result in gains or losses in the market value of our fixed rate debt portfolio due to differences in market interest rates and the rates at the inception of the debt agreements. Based on our indebtedness and the effectiveness of our interest rate swap and cap agreements at June 30, 2022, we do not expect changes in interest rates to have a material effect on our net earnings or cash flows in 2022.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation was performed under the supervision and with the participation of our management, including the chief executive officer and the chief financial officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended) as of June 30, 2022. Based on that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2022 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. ***Legal Proceedings***

Stockholder Litigation. Please refer to the disclosure in Note 8. "Commitments and Contingencies - Stockholder Litigation" to our condensed consolidated financial statements included elsewhere in this report, which is incorporated into this item by reference.

Other Litigation. In addition, we are, from time to time, subject to claims and suits, or threats of claims or suits, relating to our business, including claims for damages for personal injuries, breach of management contracts and employment related claims. In certain of these actions, plaintiffs request payment for damages, including punitive damages, which may not be covered by insurance or may otherwise have a material adverse effect on our business or results of operations.

Item 1A. ***Risk Factors***

There have been no material changes with respect to the risk factors discussed in our 2021 Annual Report on Form 10-K.

Item 2. ***Unregistered Sales of Equity Securities and Use of Proceeds***

The Company did not repurchase any shares of common stock during the six months ended June 30, 2022. At June 30, 2022, the Company continued to have authority to repurchase up to $46.0 million of shares of common stock under its Board-authorized share repurchase program.

Item 3. ***Defaults Upon Senior Securities***

None.

Item 4. ***Mine Safety Disclosures***

Not applicable.

Item 5. ***Other Information***

None.

Item 6. ***Exhibits***

No.	Description
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	Inline XBRL Taxonomy Extension Instance Document - the instance document does not appear in the interactive data file because its XBRL tags are embedded within the inline XBRL document.
101.SCH	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	The cover page from the Company’s Quarterly Report on Form 10-Q for the quarter ended June 30, 2022, formatted in Inline XBRL (included in Exhibit 101).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SURGERY PARTNERS, INC.

By: /s/ David T. Doherty
David T. Doherty
Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

Date: August 2, 2022

Exhibit 31.1

CERTIFICATIONS

I, J. Eric Evans, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Surgery Partners, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

By: /s/ J. Eric Evans
J. Eric Evans
Chief Executive Officer

Date: August 2, 2022

Exhibit 31.2

CERTIFICATIONS

I, David T. Doherty, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Surgery Partners, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

By: /s/ David T. Doherty
David T. Doherty
Executive Vice President and Chief Financial Officer

Date: August 2, 2022

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the quarterly report of Surgery Partners, Inc. (the “Company”) on Form 10-Q for the period ended June 30, 2022, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), each of the undersigned certifies, pursuant to 18 U.S.C. Sec. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company for the periods presented therein.

By: /s/ J. Eric Evans
J. Eric Evans
Chief Executive Officer

Date: August 2, 2022

By: /s/ David T. Doherty
David T. Doherty
Executive Vice President and Chief Financial Officer

Date: August 2, 2022