

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidated Financial Statements and Supplementary Information

June 30, 2020 and 2019

(With Independent Auditors' Report Thereon)

TUALITY HEALTHCARE AND SUBSIDIARIES

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KPMG LLP
Suite 3800
1300 South West Fifth Avenue
Portland, OR 97201

Independent Auditors' Report

The Board of Directors
Tuality Healthcare:

We have audited the accompanying consolidated financial statements of Tuality Healthcare and its subsidiaries which comprise the consolidated balance sheets, as of June 30, 2020 and 2019, and the related consolidated statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Tuality Healthcare and its subsidiaries as of June 30, 2020 and 2019, and the changes in and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.



Other Matter

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information on pages 35 through 37 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

Portland, Oregon
October 9, 2020

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidated Balance Sheets

June 30, 2020 and 2019

Assets	2020	2019
Current assets:		
Cash and cash equivalents	\$ 6,148,414	3,716,625
Short-term investments	911,589	524,572
Patient accounts receivable, net of allowance for uncollectible accounts of \$1,405,178 and \$3,943,100 as of June 30, 2020 and 2019, respectively	29,340,597	30,624,756
Due from related party	20,950,105	2,732,616
Other receivables	3,484,051	4,980,380
Supplies inventory	3,842,062	3,758,269
Prepaid expenses and other	2,152,604	2,791,320
Current portion of assets whose use is limited	991,582	972,882
Total current assets	67,821,004	50,101,420
Assets whose use is limited:		
Board-designated funds	34,706,362	35,489,400
Under bond indenture agreement – held by Trustee	948	937
Donor-restricted – specific purpose	4,049,056	4,792,697
Donor-restricted – endowment	2,812,317	2,782,197
Required for current liabilities	(991,582)	(972,882)
Total assets whose use is limited	40,577,101	42,092,349
Property and equipment:		
Property and equipment, net of accumulated depreciation and amortization	62,332,436	59,756,126
Other assets:		
Other receivables – noncurrent	1,378,500	1,749,000
Investments in unconsolidated affiliates	1,520,876	2,136,615
Deferred compensation plan	2,357,761	2,357,761
Cash value of life insurance	564,934	529,310
Deferred costs and other	230,187	230,187
Intangible assets	1,610,335	1,687,010
Goodwill	318,500	318,500
Total other assets	7,981,093	9,008,383
Total assets	\$ 178,711,634	160,958,278

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidated Balance Sheets

June 30, 2020 and 2019

Liabilities and Net Assets	2020	2019
Current liabilities:		
Accounts payable	\$ 14,762,403	15,390,907
Accrued payroll and employee benefits	12,863,734	12,301,670
Deferred revenue	16,590,355	—
Estimated liabilities for Medicare and Medicaid settlements	450,057	452,811
Long-term debt due within one year	1,021,001	1,047,012
Accrued bond interest payable	91,582	97,882
Total current liabilities	<u>45,779,132</u>	<u>29,290,282</u>
Long-term liabilities:		
Long-term debt, net of amount due within one year	12,072,581	13,068,958
Liability for pension benefits	66,443,796	51,789,617
Other long-term liabilities	23,884,941	20,509,248
Total long-term liabilities	<u>102,401,318</u>	<u>85,367,823</u>
Total liabilities	<u>148,180,450</u>	<u>114,658,105</u>
Net assets:		
Net assets without donor restrictions	23,264,972	38,542,676
Net assets with donor restrictions	7,266,212	7,757,497
Total net assets	<u>30,531,184</u>	<u>46,300,173</u>
Total liabilities and net assets	<u>\$ 178,711,634</u>	<u>160,958,278</u>

See accompanying notes to consolidated financial statements.

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidated Statements of Operations

For the years ended June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Net patient service revenue:		
Patient service revenue (net of contractual allowances and discounts)	\$ 199,409,821	203,114,838
Provision for bad debts	<u>(5,266,053)</u>	<u>(11,986,876)</u>
Total net patient service revenue	<u>194,143,768</u>	<u>191,127,962</u>
Other revenue:		
OHSU support	25,321,427	7,556,144
Other revenue	<u>11,792,946</u>	<u>10,266,456</u>
Total other revenue	<u>37,114,373</u>	<u>17,822,600</u>
Total revenue	<u>231,258,141</u>	<u>208,950,562</u>
Operating expenses:		
Salaries and wages	88,626,249	85,227,833
Employee benefits	25,264,423	22,035,510
Supplies and other expenses	81,625,041	75,934,715
Professional fees	26,802,774	18,533,899
Depreciation and amortization	8,498,079	8,176,628
Interest	<u>781,179</u>	<u>733,784</u>
Total operating expenses	<u>231,597,745</u>	<u>210,642,369</u>
Loss from operations	<u>(339,604)</u>	<u>(1,691,807)</u>
Other income:		
Realized income on investments whose use is limited by board designation	1,060,462	713,030
Gain on investments in affiliated companies	3,241,541	1,095,760
(Loss) gain on disposal of property and equipment	(35,493)	90,867
Change in net unrealized losses on investments	(317,369)	—
Other operating revenue	<u>302,482</u>	<u>—</u>
Total other income	<u>4,251,623</u>	<u>1,899,657</u>
Excess of revenue over expenses	3,912,019	207,850
Contributions for property and equipment acquisition	909,425	29,129
Change in net unrealized gain on other-than-trading investments	—	623,095
Pension-related changes	<u>(20,099,148)</u>	<u>(17,050,844)</u>
Decrease in net assets without donor restrictions	<u>\$ (15,277,704)</u>	<u>(16,190,770)</u>

See accompanying notes to consolidated financial statements.

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Net assets without donor restrictions:		
Excess of revenue over expenses	\$ 3,912,019	207,850
Contributions for property and equipment acquisition	909,425	29,129
Change in net unrealized gain on other-than-trading securities	—	623,095
Pension-related changes	<u>(20,099,148)</u>	<u>(17,050,844)</u>
Decrease in net assets without donor restrictions	<u>(15,277,704)</u>	<u>(16,190,770)</u>
Net assets with donor restrictions:		
Gifts, grants, and bequests	1,808,800	1,523,300
Investment (loss) income	(190,600)	129,900
Net assets released from restrictions	(2,111,609)	(1,280,816)
Contributions for endowment funds	<u>2,124</u>	<u>28,100</u>
(Decrease) increase in net assets with donor restrictions assets	<u>(491,285)</u>	<u>400,484</u>
Change in net assets	(15,768,989)	(15,790,286)
Net assets, beginning of year	<u>46,300,173</u>	<u>62,090,459</u>
Net assets, end of year	<u><u>\$ 30,531,184</u></u>	<u><u>46,300,173</u></u>

See accompanying notes to consolidated financial statements.

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidated Statements of Cash Flows

For the years ended June 30, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Cash flows from operating activities:		
Change in net assets	\$ (15,768,989)	(15,790,286)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	8,498,079	8,176,628
Net realized and unrealized gain (loss) on investments	99,225	(861,001)
Loss on investment in affiliated companies	(3,241,541)	(1,095,760)
Loss on disposal of property and equipment	(401,867)	(90,867)
Increase in cash value of life insurance	(35,624)	(26,600)
Restricted contributions and investment income received	(1,620,324)	(1,681,401)
Cash distributed from corporate joint venture	3,857,280	1,982,400
Changes in assets and liabilities that provided cash:		
Accounts receivable	(15,066,501)	(7,600,701)
Inventories	(83,793)	(330,401)
Prepaid expenses and other	638,716	(796,800)
Accounts payable	2,875,313	9,878,401
Accrued payroll and employee benefits	15,222,746	11,933,602
Estimated liabilities for Medicare and Medicaid settlements	(2,754)	(109,500)
Deferred revenue	16,590,355	—
Accrued bond interest	(6,300)	(6,201)
Net cash provided by operating activities	<u>11,554,021</u>	<u>3,581,513</u>
Cash flows from investing activities:		
Purchase of property and equipment	(10,595,847)	(20,555,300)
Proceeds from sales of property and equipment	—	1,486,701
Purchases of securities	(12,113,699)	(12,236,900)
Proceeds from sales of securities	13,124,005	15,733,599
Net investment in cash value life insurance	(128,124)	(92,500)
Net cash used in investing activities	<u>(9,713,665)</u>	<u>(15,664,400)</u>
Cash flows from financing activities:		
Proceeds from restricted contributions and investment income	1,620,324	1,681,401
Principal payments on long-term debt	(1,028,891)	(1,083,800)
Net cash provided by financing activities	<u>591,433</u>	<u>597,601</u>
Increase (decrease) in cash cash equivalents and restricted cash	2,431,789	(11,485,286)
Cash, cash equivalents and restricted cash, beginning of year	<u>3,716,625</u>	<u>15,201,911</u>
Cash, cash equivalents and restricted cash, end of year	<u>\$ 6,148,414</u>	<u>3,716,625</u>
Supplementary disclosures of cash flow information:		
Cash paid during the year for interest	\$ 763,962	673,005
Property, plant, and equipment acquired through dissolution of joint venture	—	853,505

See accompanying notes to consolidated financial statements.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

(1) Summary of Organization and Accounting Policies

Tuality Healthcare and subsidiaries (Tuality), is a licensed 215-bed hospital and health services provider operating in Washington County, Oregon. Tuality operates Tuality Community Hospital in Hillsboro, Oregon. In addition to acute care hospital services, Tuality provides a wide array of outpatient diagnostic and treatment services throughout western Washington County. Tuality is a component unit of Oregon Health & Science University.

Tuality is the parent company and sole member or stockholder of the following companies:

Tuality Management Systems, Inc. (TMSI), which owns taxable affiliated corporation Tuality Medical Equipment & Supply (TMES) that sells and rents medical durable goods.

Tuality Property Management, Inc., holds hospital-related real estate and property acquired for future hospital expansion or investment.

Tuality Healthcare Foundation, Inc., a foundation established to support Tuality by funding projects and programs that enrich the patient experience and wellness of our community.

The organizations are nonprofit corporations under the laws of the State of Oregon, maintaining tax-exempt status, except for Tuality Management Systems, Inc., which is a for-profit, taxable corporation.

(a) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Tuality and all majority-owned or controlled subsidiaries (collectively "Tuality"). Subsidiaries in which Tuality has less than a controlling interest are generally accounted for by the equity method, which approximates Tuality's equity in their underlying net book value. All significant intercompany accounts and transactions have been eliminated.

(b) Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(c) Subsequent Events

Management has evaluated subsequent events through October 9, 2020, the date the consolidated financial statements were available to be issued.

On September 19, 2020, the Department of Health and Human Services (HHS) published its Provider Reporting Guidelines. The Guidelines include the reporting timing and deadlines and methodology for calculating lost revenues attributable to COVID-19. This new guidance is effective on the date of publication. While Tuality has not completed the evaluation of the potential impacts of these guidelines, management expects the guidance to change the calculation methodology that determines the accounting recognition of the Provider Relief Fund distributions.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

On October 1, 2020, as part of the enactment of the extension of United States Government funding through December 11, 2020, Congress delayed the beginning of recoupment of the accelerated Medicare payments under the CARES Act to one year from when the payment was issued. The Advance payments are now required to be repaid in full 29 months from the date of the first accelerated payment.

(d) Patient Accounts Receivable

Accounts receivable are stated at unpaid balances (net of contractual allowances) and are reduced by an allowance for amounts estimated to be uncollectible. Substantially all of Tuality's receivables are related to providing healthcare services to its hospital's patients, except amounts due to from OHSU.

Tuality estimates the allowance for doubtful accounts by reserving a percentage of all self-pay accounts receivable, based on collection history, adjusted for expected recoveries and, if present, anticipated changes in trends. The percentage used to reserve for all self-pay accounts is based on Tuality's recent collection history. Reserves on accounts with third-party payors are set taking into consideration contractually expected amounts.

Collections are impacted by the economic ability of patients to pay and the effectiveness of Tuality's collection efforts. Significant changes in payor mix, business office operations, economic conditions, or trends in federal and state governmental healthcare coverage could affect Tuality's collection of accounts receivable and the estimates of the collectability of current accounts receivable. The allowance for uncollectible accounts is decreased by write-offs (net of recoveries). Accounts receivable are written off after collection efforts have been followed in accordance with Tuality's policies.

(e) Due from Related Party

For the years ending June 30, 2020 and 2019, respectively, Tuality recorded amounts due from related party of \$20,950,105 and \$2,732,616 at June 30, 2020 and 2019, respectively for amounts due from OHSU for operating and cash flow support.

(f) Net Patient Service Revenue

Net patient service revenue is reported as the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

(g) Investments and Assets Whose Use is Limited

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheets. Investments valued utilizing net asset value (NAV) as a practical expedient are excluded from the fair value hierarchy.

Investment income or loss (including realized gains and losses on investments, unrealized gain/loss on trading or equity securities, interest, and dividends) is included in the excess of revenue over expenses unless the income or loss is restricted by donor or law. Investment income on investments of donor-restricted funds are added to the appropriate restricted fund balance.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

(h) Supplies Inventory

Inventories, consisting of supplies, are valued at the lower of cost (first-in, first-out) or net realizable value.

(i) Property and Equipment

Property and equipment are carried at cost. Any purchases of land, buildings, and equipment that have an expected useful life greater than one year and a cost greater than \$5,000 are capitalized. Refurbishments or improvements that extend the useful life of an existing asset are also capitalized subject to the same cost materiality threshold of \$5,000. Donated assets are carried at fair market value at date of donation. Leased assets under capital leases are carried at the present value of future lease payments. The carrying amounts of assets sold, retired, or otherwise disposed of and the related allowances for depreciation are eliminated from the accounts, and any resulting gain or loss is included in operating income or expense. Depreciation of property and equipment is provided by annual charges to expense on a straight-line basis over the expected useful lives of the assets. Equipment under capital lease obligations is amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. The range of annual lives used in computing depreciation is as follows:

- Buildings: 10 – 50 Years
- Fixed Equipment: 15 – 20 Years
- Movable Equipment: 3 – 20 Years

(j) Intangible Assets

Intangible assets are recorded at cost and are amortized on a straight-line basis over the estimated useful life of the asset.

(k) Goodwill

Goodwill is not subject to amortization. Management tests for impairment on an annual basis. No adjustment for impairment was made for the years ended June 30, 2020 or 2019.

(l) Federal and State Income Taxes

Tuality is a nonprofit corporation and it is management's opinion that substantially none of its activities are subject to unrelated business income taxes. Certain subsidiaries, however, are subject to income taxes, although no significant amounts have been incurred to date.

U.S. generally accepted accounting principles require management of Tuality to evaluate tax positions taken by the organization and recognize a tax liability (or asset) if the organization has taken an uncertain position that more likely than not would not be sustained upon examination by the Internal Revenue Service. Management has analyzed tax positions taken by the organization and has concluded that as of June 30, 2020, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the consolidated financial statements. Tuality is subject to routine audits by taxing jurisdictions but no audits are currently in process.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

(m) Cash, Cash Equivalents and Restricted Cash

Tuality considers all highly liquid short-term investments with maturities of three months or less, at date of purchase or acquisition, to be cash equivalents, except for cash equivalents included in its investment portfolios.

(n) Estimated Malpractice Claims

Tuality purchases professional and general liability insurance to cover medical malpractice claims on a claims-made basis. There are known claims and incidents that may result in the assertion of additional claims, as well as claims from unknown incidents that may be asserted arising from services provided to patients. Tuality accrues an estimate of the ultimate costs for both reported claims and claims incurred but not reported, as well as an estimated receivable for expected insurance reimbursements.

(o) Net Assets with Donor Restrictions

Net assets with donor restrictions are available for the following purposes:

	<u>2020</u>	<u>2019</u>
Net assets with donor restrictions:		
Education	\$ 5,439,425	5,383,497
Patient care	<u>1,826,787</u>	<u>2,374,000</u>
	<u>\$ 7,266,212</u>	<u>7,757,497</u>

Net assets with donor restrictions are those whose use by Tuality has been limited by donors to a specific time period or purpose. Net assets with donor restrictions may have been restricted by donors to be maintained by Tuality in perpetuity or used during a specific time period.

Unconditional promises to give cash and other assets to Tuality are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the condition is met or the intention to give becomes irrevocable. The gifts are reported as donor-restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified as net assets without donor restrictions and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

(p) Loss from Operations

Loss from operations includes income from provision of patient services, as well as other revenue consisting primarily of Oregon Health & Science University (OHSU) support, management fees, rental income, and realized investment income on other than board-designated assets. Loss from operations excludes components of net periodic pension costs other than service cost and certain items that Tuality deems to be outside the scope of its primary business.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

(q) Excess of Revenue over Expenses

The consolidated statements of operations include excess of revenue over expenses. Changes in net assets without donor restrictions, which are excluded from excess of revenue over expenses, consistent with industry practice, include unrealized gains and losses on debt securities, contributions of long-lived assets (including assets acquired using contributions, which by donor restriction were to be used for the purpose of acquiring such assets), and certain pension-related changes.

(r) OHSU Affiliation

On February 1, 2016, Tuality affiliated with OHSU through the execution of a Management Agreement (the Agreement) between the organizations. Under the Agreement, OHSU agrees to oversee the unified and integrated clinical enterprises of OHSU and Tuality as a single, integrated economic unit. OHSU and Tuality remain as separate entities, own their own assets, and continue to be the licensed operators of their own facilities. Per the Agreement, OHSU has guaranteed operating income and operating cash flow support. Operating income support amounted to approximately \$25,321,427 and \$7,556,144 and operating cash flow support amounted to \$4,035,691 and \$6,200,000 for the years ended June 30, 2020 and 2019, respectively. Operating cash flow support is a loan with the balance of \$19,300,157 and \$15,264,466 as of June 30, 2020 and 2019, respectively, and is included in other long-term liabilities the consolidated balance sheets. As of June 30, 2020 there exists on Tuality's financial statements an operating support receivable of \$20,950,105 for June 30, 2020 and \$2,732,616 at June 30, 2019.

As a related party, Tuality utilized \$41,685,862 and \$29,124,782 of services during the years ended June 30, 2020 and 2019, respectively, from OHSU, primarily around providers and their support components, including specialty services that were not available to the community in the past, IT services and access to technology, and revenue cycle services including electronic medical records.

(s) New Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases*. The ASU applies to all leases of tangible assets and the new standard is effective for Tuality on July 1, 2022. Management is evaluating the effect that ASU No. 2016-02 will have on its consolidated financial statements and related disclosures. Management has not yet selected a transition method, nor has it determined the effect of the standard on its ongoing financial reporting. The primary impact of this pronouncement will be for Tuality to record a liability related to future minimum operating lease payments, and an associated right-of-use asset.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (ASC 606)*. The ASU will replace most existing revenue recognition guidance in U.S. generally accepted accounting principles when it becomes effective. During fiscal year 2020, the FASB issued ASU 2020-05, *Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842)*, which defers the implementation date for these standards one year. Management has elected the deferral option for this new standard and will apply ASC 606 July 1, 2020. Management does not anticipate the adoption of the new ASU to have a material impact on Tuality's consolidated financial statements, although certain disclosures and presentation items will be impacted.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

(t) Recently Adopted Accounting Pronouncements

In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*. The ASU requires that changes in the value of equity securities with readily determinable market values be recognized through excess of revenue over expenses. The new standard was adopted prospectively by Tuality on July 1, 2019. Tuality recognized (\$317,369) of unrealized losses related to investments for the year ended June 30, 2020. This amount is included in excess of revenues over expenses as a result of these changes in the current period.

In March 2017, the FASB issued ASU No. 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, to provide income statement classification guidance for components of the net periodic benefit cost. The ASU requires entities to disaggregate the current service cost component from the other components of net periodic benefit cost (the other components) and present it with other current compensation costs for related employees in the income statement. Tuality adopted the ASU on a retrospective basis on July 1, 2019 and recorded \$302,428 of reductions in the net periodic benefit costs in non-operating income.

In June 2018, the FASB issued Accounting Standards Update (ASU) No. 2018-08 – Not-for-Profit Entities (Topic 958): *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. This ASU was issued to clarify and improve the scope and accounting guidance for contributions received and contributions made. The update assists entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal) transactions and (2) determining whether a contribution is conditional. Tuality adopted ASU No. 2018-08 for the period beginning July 1, 2019 and there was no material change to Tuality's financial statements upon adoption.

For the year ended June 30, 2020, Tuality adopted ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*, which requires the statement of cash flows to explain the change during the period in total cash, cash equivalents and restricted cash. Adoption of this standard did not have a material impact on the consolidated financial statements.

(2) COVID-19

The CARES Act, which was enacted on March 27, 2020, authorizes \$100 billion in funding to hospitals and other healthcare providers to be distributed through the Public Health and Social Services Emergency Fund (the "PHSSEF"). Payments from the PHSSEF are intended to compensate healthcare providers for lost revenues and incremental expenses incurred in response to the COVID-19 pandemic and are not required to be repaid, provided the recipients attest to and comply with certain terms and conditions, including limitations on balance billing and not using PHSSEF funds to reimburse expenses or losses that other sources are obligated to reimburse. Tuality received \$5,497,237 in payments from the initial PHSSEF distribution, of which \$3,549,777 was recognized as revenue for the year ended June 30, 2020.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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As a way to increase cash flow to Medicare providers impacted by the COVID-19 pandemic, the CARES Act expanded the Medicare Accelerated and Advance Payment Program. Inpatient acute care hospitals were able to request accelerated payments of up to 100% of the Medicare payment amount for a three month period (not including Medicare Advantage payments), although CMS is now reevaluating pending and new applications in light of direct payments made available through PHSSEF. CMS based payment amounts for inpatient acute care hospitals on the provider's Medicare fee-for-service reimbursements in the last six months of 2019. Such accelerated payments are interest free for inpatient acute care hospitals for 12 months, and the program currently requires CMS to recoup the payments beginning 120 days after receipt by the provider, by withholding future Medicare fee-for-service payments for claims until the full accelerated payment has been recouped. The program currently requires any outstanding balance remaining after 12 months to be repaid by the provider or be subject to an interest rate currently set at 10.25%. Therefore, they will be accounted for as revenue. In April 2020, the Health System received \$14,645,895 of accelerated payments, which have been recorded in the consolidated balance sheet as of June 30, 2020 as deferred revenue. This deferred revenue will be reduced over time as revenue is recognized for claims submitted for services provided after the 120-day period.

Due to the recent enactment of the CARES Act and other legislation, there is still a high degree of uncertainty surrounding their implementation, and the public health emergency continues to evolve. Tuality continues to assess the potential impact of the CARES Act, the PPPHCE Act, the potential impact of future stimulus measures, if any, and the impact of other laws, regulations, and guidance related to COVID-19 on our business, results of operations, financial condition and cash flows.

(3) Investments and Assets Whose Use is Limited

(a) Investments in Unconsolidated Affiliates

Investments in unconsolidated affiliates consisted of the following at June 30, 2020 and 2019:

		June 30, 2020		
	Cost or equity	Percentage of ownership	Investments	Income/(loss)
Raines Dialysis Center	Equity	20 %	\$ 715,506	193,208
Northwest Hospital Partnership, Inc.	Equity	—	—	(465,687)
Mountain States Healthcare	Cost	5	310,181	—
Noble Woods	Equity	22	240,189	261,404
West Coast Sourcing	Cost	1	5,000	—
Tuality Health Alliance	Cost	33.3 %	250,000	3,252,616
			<u>\$ 1,520,876</u>	<u>3,241,541</u>

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June 30, 2019				
	Cost or equity	Percentage of ownership	Investments	Income/(loss)
Raines Dialysis Center	Equity	20 %	\$ 829,302	420,529
Northwest Hospital Partnership, Inc.	Equity	50	465,687	—
Mountain States Healthcare	Cost	5	310,181	—
Noble Woods	Equity	22	276,445	286,778
West Coast Sourcing	Cost	1	5,000	—
Tuality / OHSU Cancer Center	Equity	NA	—	388,453
Tuality Health Alliance	Cost	33.3 %	250,000	—
			<u>\$ 2,136,615</u>	<u>1,095,760</u>

Tuality/OHSU Cancer Center

Tuality owned a 50% equity interest in the Tuality / OHSU Cancer Center (TOCC), an Oregon limited liability company operating a radiation treatment center. The entity was dissolved as of December 31, 2018 and moved to Tuality Community Hospital.

Tuality charged TOCC management fees of \$373,100 for the six months ended December 31, 2018.

TOCC leased its building from Tuality with total rents received on this property amounting to \$70,200 for the six months ended December 31, 2018. Rent payments were discontinued on January 1, 2019 after the joint venture was dissolved and the cancer center was moved to the main hospital entity at Tuality.

Summarized financial information of TOCC is below, as of and for the six months ended December 31, 2018:

	Tuality/OHSU Cancer Center Six months ended December 31, 2018
Current assets	\$ —
Noncurrent assets	—
Current liabilities	—
Noncurrent liabilities	—
Partners' equity	3,142,800
Revenues	<u>1,989,600</u>
Net income/(loss)	<u>\$ 1,153,200</u>

TUALITY HEALTHCARE AND SUBSIDIARIES

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Tuality Health Alliance

Tuality contributed initial capital of \$250,000 to Tuality Health Alliance (the Alliance), an Oregon taxable, not-for-profit corporation organized to create an association of hospitals and physicians to coordinate the delivery of comprehensive, affordable, quality integrated healthcare services to communities served by the incorporator's hospital and physician members, as well as other corporate purposes. The Alliance is an unconsolidated affiliate, presented on a cost basis, in Tuality's consolidated financial statements. The Alliance distributed \$3,252,616 to Tuality during the year ended June 30, 2020.

Tuality charged the Alliance management fees of \$1,944,300 and \$3,910,700 for the years ended June 30, 2020 and 2019, respectively. Management fees receivable were \$0 and \$320,800 at June 30, 2020 and 2019, respectively.

The Alliance members provide medical care under the Oregon Health Plan to certain patients who qualify under criteria established by the State of Oregon. The agreement under which these services are provided requires the Alliance to maintain certain levels of net worth. Based on interim financial statements for the year ended June 30, 2020, management believes the net worth requirements have been met.

As of December 31, 2019, the Alliance is no longer contracted with Health Share to provide new services to the Medicaid population. Existing funds within the Alliance must be dispositioned appropriately, with full dissolution of the Alliance anticipated by December 31, 2020.

(b) Investment Income

Investment income on board-designated funds including unrealized gains and losses, is included in other operating activities.

Investments made by the Tuality Healthcare Foundation shall be managed in accordance with the laws of the State of Oregon, and in ways that maximize overall return on investment with minimal risk to the investment, while promoting stability, flexibility, diversification, and liquidity. The Foundation is the recipient of many donor-restricted gifts, the expenditure of which occurs over time for a variety of charitable purposes. These funds, in addition to miscellaneous unrestricted funds, shall not be pooled with the endowed funds for investment purposes, as the investment objectives for these funds differ from the long-term objective of the endowed funds. These funds will be individually accounted for and will accrue pro rata investment income until the principal amounts are distributed for their specific purposes. Non-endowed funds shall be invested in a combination of bonds and cash, with the goal of exposing the funds to very low risk. For non-endowed funds, any bonds held will be subject to limited maturity (three years). It is the Foundation's intention to hold these bonds as trading securities.

The Foundation will spend up to 6% of a three-year moving average of the total fair value of the endowment assets annually to support community education programs and specific scholarships as designated by the various endowments. For purposes of determining the amount available to spend, the average will be calculated from the fair value of the endowments on June 30 of each year.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

Changes in endowment net assets for the years ended June 30, 2020 and 2019 are as follows:

	Net assets with donor restriction
Balance as of June 30, 2018	\$ 5,292,301
Investment income	79,601
Contributions	28,201
Appropriated for expenditure	<u>(251,402)</u>
Balance as of June 30, 2019	5,148,701
Investment loss	(190,600)
Contributions	2,124
Appropriated for expenditure	<u>(256,001)</u>
Balance as of June 30, 2020	<u><u>\$ 4,704,224</u></u>

(4) Liquidity and Availability

As of June 30, 2020, Tuality Healthcare has working capital of \$22,041,872. As of June 30, 2019, Tuality had working capital of \$20,811,100.

Financial assets available for general expenditure within one year of the balance sheet date, consist of the following:

	2020	2019
Cash and cash equivalents	\$ 6,148,414	3,716,625
Short term investments	911,589	524,572
Patient accounts receivable, net	29,340,597	30,624,756
Due from related party	20,950,105	2,732,616
Other receivables	3,484,051	4,980,380
Assets limited to use, current portion	991,582	972,882
Board designated funds	<u>34,706,362</u>	<u>35,489,400</u>
	<u><u>\$ 96,532,700</u></u>	<u><u>79,041,231</u></u>

Certain board-designated and donor-restricted assets limited to use are available for general expenditure within one year in the normal course of operations. Other assets limited to use are for donor-restricted purposes and debt service. Additionally, certain board-designated assets are designated for future purposes beyond the next year. However, the board-designated amounts may be made available, if necessary.

As part of Tuality's liquidity management plan, cash in excess of daily requirements are invested in short term investments and money market funds.

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(5) Fair Value Measurements

Generally accepted accounting principles define fair value, establish a framework for measuring fair value, and establish a fair value hierarchy that prioritizes the inputs to valuation techniques. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market. Valuation techniques that are consistent with the market, income, or cost approach are used to measure fair value.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities Tuality has the ability to access.
- Level 2 inputs are inputs (other than quoted prices included within Level 1) that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

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June 30, 2020 and 2019

Fair values of assets measured on a recurring basis at June 30, 2020 are as follows:

Fair value measurements at reporting date using				
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	Fair value			
Short term investments:				
Cash equivalents and restricted cash	\$ 49,773	49,773	—	—
Equity securities	506,422	506,422	—	—
Fixed income securities	355,394	—	355,394	—
Assets whose use is limited board designated funds:				
Cash equivalents	800,061	800,061	—	—
Equity securities	10,887,496	10,887,496	—	—
Fixed income mutual funds	16,373,306	16,373,306	—	—
Under bond indenture:				
Cash equivalents	948	948	—	—
Donor restricted:				
Cash equivalents	380,651	380,651	—	—
Equity securities	3,907,439	3,907,439	—	—
Fixed income securities	2,717,948	—	2,717,948	—
Deferred compensation plan:				
Cash equivalents	462,001	462,001	—	—
Equity securities	1,018,263	1,018,263	—	—
Fixed income securities	877,497	877,497	—	—
	38,337,199	\$ 35,263,857	3,073,342	—
Investments valued at NAV as a practical expedient	6,500,834			
Total	\$ 44,838,033			

TUALITY HEALTHCARE AND SUBSIDIARIES

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Fair values of assets measured on a recurring basis at June 30, 2019 are as follows:

Fair value measurements at reporting date using				
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
	Fair value			
Short term investments:				
Cash, cash equivalents and restricted cash	\$ 18,501	18,501	—	—
Equity securities	296,268	296,268	—	—
Fixed income securities	209,803	—	209,803	—
Assets whose use is limited board designated funds:				
Cash and cash equivalents	162,904	162,904	—	—
Equity securities	7,980,605	7,980,605	—	—
Fixed income mutual funds	17,539,911	17,539,911	—	—
Under bond indenture:				
Cash and cash equivalents	937	937	—	—
Donor restricted:				
Cash and cash equivalents	269,207	269,207	—	—
Equity securities	4,253,808	4,253,808	—	—
Fixed income securities	3,051,909	—	3,051,909	—
Deferred compensation plan:				
Cash and cash equivalents	462,001	462,001	—	—
Equity securities	1,018,257	1,018,257	—	—
Fixed income securities	877,503	877,503	—	—
	36,141,614	\$ 32,879,902	3,261,712	—
Investments valued at NAV as a practical expedient	9,805,950			
Total	\$ 45,947,564			

Investments valued using the NAV per share (or its equivalent) as a practical expedient are considered “alternative investments” and, unlike more traditional investments, generally do not have readily obtainable market values and take the form of limited partnerships. Tuality values these investments based on the partnerships’ June 30 financial statements. The following table presents the investments valued at NAV per

TUALITY HEALTHCARE AND SUBSIDIARIES

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share, redemption frequency (if currently eligible), and the redemption notice period, and excluded from the fair value hierarchy tables above:

		June 30		Redemption frequency	Redemption notice period
		2020	2019		
Limited partnerships	\$	6,500,834	9,805,950	Monthly to annual	45–185 days

(6) Community Benefits

Tuality's mission is to provide quality healthcare services and leadership in promoting health improvement to all persons in its service area on a nondiscriminatory basis and without regard to ability to pay. Tuality recognizes that not all individuals possess the ability to purchase essential medical services and that its mission includes serving the community with respect to providing healthcare service and healthcare education. In keeping with its commitment to serve all members of its community, the following are considered in the context of the individual's ability to pay and/or community need:

- Free and/or subsidized care
- Care provided to persons covered by governmental programs at below cost
- Health activities and programs to support the community

These activities include wellness programs, community education programs, health screenings, and special programs for the elderly, handicapped, and medically underserved, and a wide variety of broad community support activities.

Through its hospitals, Tuality provides care to patients covered by governmental programs, such as Medicare and Medicaid, which reimburse at levels below the actual cost to provide this care. The amount of unpaid cost due to inadequate reimbursement under these programs was approximately \$49,846,670 and \$41,180,700 during the years ended June 30, 2020 and 2019, respectively. Tuality also provides additional free or discounted care under its charity care policy. The cost of care provided under Tuality's charity policy was estimated to be \$5,064,641 and \$4,016,200 during the years ended June 30, 2020 and 2019, respectively. The cost of charity care provided is based on Tuality's estimated relationship of cost to charges.

(7) Net Patient Service Revenue and Patient Receivables

Tuality has agreements with third-party payors that provide for payments to Tuality at amounts different from their established rates. A summary of the payment arrangements with major third-party payors follows:

(a) Medicare

Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient non-acute services and defined capital costs related to beneficiaries are paid based on a cost reimbursement methodology. Tuality is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by Tuality and audits thereof by the Medicare fiscal intermediary.

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Notes to Consolidated Financial Statements

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Tuality's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with Tuality. Tuality's Medicare cost reports have received final settlement notification by the Medicare fiscal intermediary through June 30, 2015.

(b) Medicaid

Inpatient and outpatient services rendered to the Medicaid program beneficiaries are paid based on prospective payment rates with final settlement determined after submission of annual cost reports by Tuality and audits thereof by the Department of Medical Assistance Programs (DMAP).

Tuality's Medicaid cost reports have been reviewed by DMAP through June 30, 2015.

Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

There were no material effects on net patient service revenues for the years ended June 30, 2020 and 2019 due to changes in prior year estimated Medicare and Medicaid settlements.

(c) Other

Tuality has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to Tuality under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates and outpatient service fee schedules.

(8) Property and Equipment

A summary of property and equipment at June 30, 2020 and 2019 follows:

	<u>2020</u>	<u>2019</u>
Land and land improvements	\$ 8,090,009	8,338,475
Building and fixed equipment	108,955,730	99,474,839
Moveable equipment	96,125,523	91,867,754
Equipment under capital leases	<u>9,666,668</u>	<u>9,666,668</u>
	222,837,930	209,347,736
Less: accumulated depreciation and amortization	<u>(172,448,222)</u>	<u>(164,262,213)</u>
	50,389,708	45,085,523
Construction in progress	<u>11,942,728</u>	<u>14,670,603</u>
Property and equipment, net	<u>\$ 62,332,436</u>	<u>59,756,126</u>

TUALITY HEALTHCARE AND SUBSIDIARIES

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(9) Intangible Assets

During the year ended September 30, 2009, Tuality exchanged a parcel of land for parking rights in that same location for a period of 50 years. The value of the license of \$1,928,629 is based on the estimated fair value of the transferred land plus cash that was paid as part of the transaction. A gain of \$1,724,200 was recognized on the transaction. Tuality began amortizing the license over the 50-year period once the parking spaces became available in August 2010.

Intangibles and accumulated amortization at June 30, 2020 and 2019 are as follows:

	<u>2020</u>	<u>2019</u>
Parking license	\$ 1,928,629	1,928,629
Noncompete covenant and other	<u>380,500</u>	<u>380,500</u>
	2,309,129	2,309,129
Less: accumulated amortization	<u>(698,794)</u>	<u>(622,119)</u>
	<u>\$ 1,610,335</u>	<u>1,687,010</u>

Amortization expense related to intangible assets was \$76,695 for the years ended June 30, 2020 and 2019.

Estimated aggregate amortization expense for the next five fiscal years is as follows:

2021	\$ 60,201
2022	54,702
2023	54,702
2024	54,702
2025	54,702

(10) Long-Term Debt

Hospital Revenue Refunding Bond, Series 2015, amounting to \$16,125,000, was issued by the Hospital Facility Authority of Hillsboro, Oregon (The Authority) to fund an irrevocable trust to defease scheduled principal and interest payments on the Hospital Revenue Bonds, Series 2001. These bonds were issued as private placement with a single financial institution for the life of the bond. Funds were also provided for bond issue costs and establishing a project fund of \$3,578,300 for hospital capital purchases.

Under the terms of the loan agreements created pursuant to these issuances, Tuality Obligated Group (The Obligated Group), which only includes the Tuality Healthcare legal entities, agreed to provide funds sufficient to pay the principal and interest on the bonds as they become due and to pay any expenses of the Trustee. The Obligated Group recorded liabilities in the amount of the bonds payable to reflect these agreements. In order to secure the bonds, the Obligated Group granted security interests in the gross revenue from operations, equipment owned or leased located in Tuality facilities, and on Tuality's real property.

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Under the Original Master Indenture, as amended, Tuality agreed to a number of covenants and conditions, which management believes have been met.

Long-term debt at June 30, 2020 and 2019 consists of the following:

	<u>2020</u>	<u>2019</u>
2015 series bonds, variable annual payments, including principal and interest at a rate of 2.88% from \$1,262,700 to \$1,270,600, beginning October 2016 to October 2031	\$ 12,540,812	13,409,301
Present value of net minimum capital lease obligations	<u>552,770</u>	<u>706,669</u>
Total debt	13,093,582	14,115,970
Less: amounts due within one year	<u>(1,021,001)</u>	<u>(1,047,012)</u>
Long term debt, due after one year	<u>\$ 12,072,581</u>	<u>13,068,958</u>

Long-term debt maturing in the next five years consists of:

	<u>Long term debt</u>	<u>Capital leases</u>	<u>Total</u>
Fiscal years ending:			
2021	\$ 900,000	121,001	1,021,001
2022	925,000	128,065	1,053,065
2023	955,000	135,541	1,090,541
2024	980,000	143,453	1,123,453
2025	1,010,000	24,710	1,034,710
Thereafter	<u>7,770,812</u>	<u>—</u>	<u>7,770,812</u>
	<u>\$ 12,540,812</u>	<u>552,770</u>	<u>13,093,582</u>

(11) Long-Term Leases

All non-cancelable leases have been categorized as capital or operating leases. Tuality leases equipment and buildings under non-cancelable operating leases, which expire at various dates between March 2021 and 2028.

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Minimum future obligations on leases in effect at June 30, 2020 are:

	Capital leases	Operating leases
Fiscal years ending:		
2021	\$ 149,302	3,635,201
2022	149,302	3,646,801
2023	149,302	3,539,301
2024	149,302	1,065,901
2025	12,490	295,100
Thereafter	<u>—</u>	<u>—</u>
Total minimum lease payments	609,698	\$ <u><u>12,182,304</u></u>
Less: amounts representing interest	<u>56,928</u>	
Present value of net minimum lease payments	\$ <u><u>552,770</u></u>	

Rental expense under non-cancelable operating leases with initial terms of one year or greater was \$3,603,095 and \$3,467,900 for the years ended June 30, 2020 and 2019, respectively.

(12) Retirement Plans

Tuality has a defined-benefit pension plan covering substantially all of its employees. Tuality makes contributions to the plan in amounts sufficient to fund the plan's current service cost and the actuarially computed past service costs over a period of 10 years. In August of 2012, the board of directors approved an amendment to freeze the defined-benefit pension plan effective August 31, 2012. In conjunction with the freeze, the plan is now closed to new entrants and compensation no longer accrues. Current participants who are not yet vested will continue to accrue accumulated years of service for hours worked to become vested if they continue working for Tuality.

Effective September 1, 2012, Tuality established a cash balance retirement plan that covers substantially all of its employees. The plan benefits are based on compensation and years of service. Tuality makes annual contributions and interest credits to each employee's account.

The defined-benefit pension plan and the cash balance retirement plan are collectively "the defined-benefit plans."

Tuality also has a 457(b) salary deferral plan for key executives. Tuality reports assets and liabilities of equal amounts attributable to the amount deferred and the related investment earnings. Tuality's invested assets of deferred compensation consist of mutual funds and fixed income. The balance in the deferred compensation plan at June 30, 2020 and 2019 was \$2,357,761 and is included in other long-term liabilities in the accompanying consolidated balance sheets.

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The following table sets forth the funded status of the defined-benefit plans and amounts recognized in Tuality's consolidated balance sheets as of June 30, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Change in benefit obligation:		
Projected benefit obligation at July 1	\$ 133,881,500	115,976,650
Service cost	3,950,790	3,568,694
Interest cost	4,599,804	5,196,161
Actuarial (gain)/loss	15,368,316	15,738,842
Expenses paid	(1,590,599)	(1,841,835)
Benefits paid	<u>(6,422,884)</u>	<u>(4,756,946)</u>
Projected benefit obligation at June 30	<u>149,786,927</u>	<u>133,881,566</u>
Change in plan assets:		
Fair value of assets at July 1	82,091,949	74,555,966
Actual return on plan assets	171,388	3,865,764
Employer contribution	9,093,277	10,269,000
Expenses paid	(1,590,599)	(1,841,835)
Benefits paid	<u>(6,422,884)</u>	<u>(4,756,946)</u>
Fair value of assets at June 30	<u>83,343,131</u>	<u>82,091,949</u>
Funded status	<u>\$ (66,443,796)</u>	<u>(51,789,617)</u>

Amounts recognized in the consolidated balance sheets and the statement of changes in net assets as of and for the years ended June 30, 2020 and 2019 consist of:

	<u>2020</u>	<u>2019</u>
Liability for pension benefits	\$ 66,443,796	51,789,617
Pension-related changes	(20,099,148)	(17,050,844)

Amounts recognized as changes in net assets without donor restrictions but not yet included in net periodic pension cost as of June 30, 2020 and 2019 consist of:

	<u>2020</u>	<u>2019</u>
Net loss	\$ 87,296,887	68,296,600
Prior service cost	<u>(2,472,441)</u>	<u>(3,571,300)</u>
Total	<u>\$ 84,824,446</u>	<u>64,725,300</u>

TUALITY HEALTHCARE AND SUBSIDIARIES

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The accumulated benefit obligation for the defined-benefit plans was \$149,749,622 and \$133,881,500 at June 30, 2020 and 2019, respectively.

	Year ended June 30	
	2020	2019
Components of net periodic benefit cost:		
Service Cost	\$ 3,950,790	3,568,694
Interest cost	4,599,804	5,196,161
Expected return on plan assets	(5,773,511)	(5,360,084)
Amortization of prior service cost	(1,098,847)	(1,098,847)
Amortization of net actuarial gain	1,970,072	1,281,144
Net periodic pension cost	<u>\$ 3,648,308</u>	<u>3,587,068</u>

The estimated net loss and prior service cost that will be amortized from changes in net assets without donor restrictions into net periodic pension cost over the next fiscal year are \$2,686,839 and \$(1,098,847), respectively.

(a) Assumptions

	June 30,	
	2020	2019
Weighted average assumptions used to determine benefit obligations at June 30:		
Discount rate	2.69 %	3.51 %
Weighted average assumptions used to determine net periodic benefit cost for period ended:		
Discount rate	3.51 %	4.65 %
Expected long-term return on plan assets	6.75	6.75

The expected long-term rate of return on plan assets reflected the weighted average expected return for the broad categories of investments currently held in the defined-benefit plans (adjusted for expected changes), based on historical rates of return for each broad category, as well as factors that may constrain or enhance returns in the broad categories in the future.

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(b) Plan Assets

Tuality's investment policy is to manage the defined-benefit plans with long-term (five years and more) objectives, with little concern for high current income or the need to maintain ready-cash reserves other than as required for current participant distributions, and with the intent to achieve the highest practicable long-term rate of return without taking excessive risk that could jeopardize the funding policy or cause undue funding volatility. In consideration of this policy, the defined-benefit plans will invest in a variety of asset classes (including short term money-market securities, large-company common stocks, smaller-company common stocks, international common stocks and fixed income securities) and will diversify sufficiently within each asset class or may invest in index funds to minimize the risk of large losses.

Target allocation percentages for each major category of plan assets are as follows:

	<u>Cash balance</u>	<u>Defined benefit</u>
Non-Traded Alternative	2 %	2 %
Cash	8	11
Equity	47	52
Fixed	20	20
Hedged	23	15
Total	<u>100 %</u>	<u>100 %</u>

(c) Cash Flows

Tuality expects to contribute \$7,935,000 to its pension plans in fiscal year 2021.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

Fiscal year ending June 30:	
2021	\$ 6,211,442
2022	6,043,338
2023	6,181,392
2024	6,463,649
2025	6,653,094
Following five years	35,031,310

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

The following table presents Tuality's pension plan assets measured at fair value at June 30, 2020:

Fair value measurements at reporting date using				
	Fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Interest bearing cash	\$ 1,595,489	1,595,489	—	—
Corporate bonds and debentures	668,950	—	668,950	—
Registered investment companies:				
Fixed income	27,829,124	27,829,124	—	—
Large cap	33,083,675	33,083,675	—	—
Mid cap	4,532,284	4,532,284	—	—
Small cap	6,034,637	6,034,637	—	—
	73,744,159	\$ 73,075,209	668,950	—
Investments valued at NAV as a practical expedient	9,598,972			
Total	\$ 83,343,131			

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

The following table presents Tuality's pension plan assets measured at fair value at June 30, 2019:

	Fair value measurements at reporting date using			
	Fair value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Interest bearing cash	\$ 3,956,701	3,956,701	—	—
Equity securities:				
Fixed income	233,402	233,402	—	—
Corporate bonds and debentures	1,125,303	—	1,125,303	—
Municipal bonds	170,904	—	170,904	—
U.S. government securities	1,553,005	1,553,005	—	—
Registered investment companies:				
Fixed income	24,239,506	24,239,506	—	—
Large cap	33,342,670	33,342,670	—	—
Mid cap	5,961,608	5,961,608	—	—
Small cap	4,616,209	4,616,209	—	—
	75,199,308	\$ 73,903,101	1,296,207	—
Investments valued at NAV as a practical expedient	6,892,641			
Total	\$ 82,091,949			

Investments valued using the NAV per share (or its equivalent) are considered "alternative investments" and, unlike more traditional investments, generally do not have readily obtainable market values and take the form of limited partnerships. Tuality values these investments based on the partnerships' June 30 financial statements. The following table presents the investments valued at NAV per share, redemption frequency (if currently eligible), and the redemption notice period, and excluded from the fair value hierarchy tables above:

	June 30		Redemption frequency	Redemption notice period
	2020	2019		
Alternative investments	\$ 9,598,972	6,892,641	Event driven	NA

(d) Healthcare Performance Retirement Plan

In addition, during 1994, Tuality established the Tuality Healthcare Performance Retirement Plan under which eligible employees may defer a portion of their annual compensation pursuant to Sections 403(b) and 401(k) of the Internal Revenue Code. Tuality matches a portion of employee contributions on a

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

discretionary basis. Tuality accrued contributions of \$361,044 and \$322,093 for the years ended June 30, 2020 and 2019, respectively.

(13) Functional Expenses

Tuality provides general healthcare services to residents within its geographic location. Expenses related to providing these services are as follows for the years ended June 30, 2020 and 2019:

Year ended June 30, 2020				
	Tuality program service	Tuality Management and general	Affiliated entities	Total
Salaries and wages	\$ 86,250,275	2,002,801	373,173	88,626,249
Employee benefits	24,553,594	552,802	158,027	25,264,423
Supplies and other expense	78,653,610	784,003	2,187,428	81,625,041
Professional fees	26,735,870	66,904	—	26,802,774
Depreciation and amortization	7,404,838	822,765	270,476	8,498,079
Interest	781,179	—	—	781,179
Total	\$ <u>224,379,366</u>	<u>4,229,275</u>	<u>2,989,104</u>	<u>231,597,745</u>

Year ended June 30, 2019				
	Tuality program service	Tuality Management and general	Affiliated entities	Total
Salaries and wages	\$ 83,300,928	1,353,301	573,604	85,227,833
Employee benefits	21,479,605	341,602	214,303	22,035,510
Supplies and other expense	73,045,710	1,000,303	1,888,702	75,934,715
Professional fees	18,463,995	69,904	—	18,533,899
Depreciation and amortization	7,118,522	790,905	267,201	8,176,628
Interest	733,784	—	—	733,784
Total	\$ <u>204,142,544</u>	<u>3,556,015</u>	<u>2,943,810</u>	<u>210,642,369</u>

The financial statements report certain expense categories that are attributable to more than one healthcare service or management and support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including depreciation, amortization, and other occupancy costs, are allocated to a functional region based on a square-footage or units-of-service basis. In some instances, costs are allocated according to reasonable estimates of general overhead.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

(14) Concentrations of Credit Risk

Financial instruments, which potentially subject Tuality to concentrations of credit risk consist of the following:

(a) Cash

Tuality maintains its cash balances at several financial institutions located in Washington County, Oregon. As of June 30, 2020, accounts at each institution are insured by the Federal Deposit Insurance Corporation up to \$250,000. At June 30, 2020, Tuality's uninsured cash balances totaled \$442,790.

(b) Patient Receivables

The mix of net patient receivables was as follows at June 30, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Medicare and Medicare Managed Care	\$ 35 %	39 %
Medicaid and Medicaid Managed Care	13	15
Managed Care Plans	31	29
Workers Compensation	1	1
Other	20	16
	<u>\$ 100 %</u>	<u>100 %</u>

(15) Commitments and Contingencies

During the normal course of its operations, Tuality becomes involved in litigation and regulatory investigations.

Tuality has different insurance arrangements with Mountain States Healthcare Reciprocal Retention Group (MSH) along with other member hospitals. All claims under the MSH policy are subject to a \$25,000 deductible indemnity payment per claim. The limits provided in the primary policy issued by MSH shall be \$1,000,000 per claim and \$3,000,000 annual aggregate for general and hospital professional liability, and \$1,000,000 per claim and \$3,000,000 or \$2,000,000 per claim and \$5,000,000 annual aggregate for physician professional liability. An excess/umbrella insurance program exists for general and hospital professional liability and provides limits in four separate layers and is reinsured by CNA (first excess layer), Zurich (next two excess layers), and Chartis (last excess layer) insurance companies. Each layer provides limits of \$5,000,000 per claim and \$5,000,000 annual aggregate per hospital and \$15,000,000 annual aggregate for all hospitals participating in that layer. Total limits for the hospitals that participate in all four layers are \$20,000,000 per claim, \$20,000,000 annual aggregate per hospital, and \$60,000,000 annual aggregate for all hospitals combined. After January 1, 2011, all four excess layers apply. The insurance is on a claims-made basis.

TUALITY HEALTHCARE AND SUBSIDIARIES

Notes to Consolidated Financial Statements

June 30, 2020 and 2019

Effective January 1, 2018 Tuality entered into an insurance program with UMIA. All professional liability and general liability claims under the policy are subject to a \$25,000 deductible indemnity payment per claim. All personal property claims are subject to a \$250 deductible. All Employee Benefits Administration Liability Claims are subject to a \$1,000 deductible. This policy is on a claims-made basis. For stop loss, the claims that Tuality pays (after out of pocket share) are capped per person at \$215K. Any claims paid after \$215K during the year is reimbursed by the stop loss carrier. There is no maximum on the reimbursements.

General and professional liability costs, as well as related expected insurance recoveries, have been accrued based on actuarial determination. The amount accrued, including the tail liability, at June 30, 2020 and 2019 for general and professional liability risks was \$2,148,227 and \$2,887,026, respectively, and is recorded in accounts payable. The related insurance receivable at June 30, 2020 and 2019 was \$1,378,501 and \$1,749,006, respectively and recorded in other receivables.

Tuality has an employee medical benefit plan to self-insure claims. This self-insured medical benefit plan operates on a calendar year basis and is administered by a third-party administrator. Tuality has entered into a stop-loss insurance arrangement in an effort to limit its exposure. Tuality and its covered employee dependents contribute to the fund to pay medical claims and reinsurance premiums. At June 30, 2020, management has made provisions, which it believes to be sufficient to cover estimated claims, including claims incurred but not yet reported. The total of this expected liability, inclusive of deductibles, is \$2,227,022 as of June 30, 2020, and \$2,887,022 as of June 30, 2019.

SUPPLEMENTARY INFORMATION

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidating Schedule of Balance Sheet Information

June 30, 2020 and 2019

Assets	Tuality Healthcare	TMSI/TMES	Tuality Property Management Co.	Tuality Healthcare Foundation	Total	Intercompany Eliminations	Consolidated	
							June 30, 2020	June 30, 2019
Current assets:								
Cash and cash equivalents	\$ 4,524,557	1,110,850	79,269	433,738	6,148,414	—	6,148,414	3,716,625
Short-term investments	—	—	—	911,589	911,589	—	911,589	524,572
Patient accounts receivable	30,065,399	680,376	—	—	30,745,775	—	30,745,775	34,567,856
Allowance for uncollectible accounts	(1,523,347)	—	—	118,169	(1,405,178)	—	(1,405,178)	(3,943,100)
Due from related party	29,340,597	—	—	—	29,340,597	—	29,340,597	—
Other receivables	3,194,950	—	(1,988)	291,089	3,484,051	—	3,484,051	7,712,996
Inventory of supplies	3,284,128	557,934	—	—	3,842,062	—	3,842,062	3,758,269
Prepaid expenses and other	2,137,885	(36)	14,755	—	2,152,604	—	2,152,604	2,791,320
Assets whose use is limited:	991,582	—	—	—	991,582	—	991,582	—
Required for current liabilities	—	—	—	—	—	—	—	972,882
Due from subsidiaries	1,976,878	—	7,759,194	55,863	9,791,935	(9,791,935)	—	—
Total current assets	73,992,629	2,349,124	7,851,230	1,810,448	86,003,431	(9,791,935)	76,211,496	50,101,420
Assets whose use is limited:								
Board-designated funds	34,706,362	—	—	—	34,706,362	—	34,706,362	35,489,400
Under bond indenture agreement – held by Trustee	948	—	—	—	948	—	948	937
Donor-restricted – specific purpose	—	—	—	4,049,056	4,049,056	—	4,049,056	4,792,697
Donor-restricted – endowment	—	—	—	2,812,317	2,812,317	—	2,812,317	2,782,197
Less amount required for current liabilities	(991,582)	—	—	—	(991,582)	—	(991,582)	(972,882)
Total assets whose use is limited	33,715,728	—	—	6,861,373	40,577,101	—	40,577,101	42,092,349
Property and equipment:								
Property and equipment	213,775,983	162,259	20,842,416	—	234,780,658	—	234,780,658	224,018,339
Accumulated depreciation and amortization	(156,967,877)	(113,547)	(15,366,798)	—	(172,448,222)	—	(172,448,222)	(164,262,213)
Total property and equipment	56,808,106	48,712	5,475,618	—	62,332,436	—	62,332,436	59,756,126
Other assets:								
Other receivables – noncurrent	1,378,500	—	—	—	1,378,500	—	1,378,500	1,749,000
Investments in subsidiaries	16,803,605	—	—	—	16,803,605	(16,803,605)	—	—
Investments in unconsolidated affiliates	1,520,876	—	—	—	1,520,876	—	1,520,876	2,136,615
Deferred compensation plan	2,357,761	—	—	—	2,357,761	—	2,357,761	2,357,761
Cash value of life insurance	564,934	—	—	—	564,934	—	564,934	529,310
Deferred costs and other	230,187	—	—	—	230,187	—	230,187	230,187
Intangible assets	61,675	—	1,548,660	—	1,610,335	—	1,610,335	1,687,010
Goodwill	318,500	—	—	—	318,500	—	318,500	318,500
Total other assets	23,236,038	—	1,548,660	—	24,784,698	(16,803,605)	7,981,093	9,008,383
Total assets	\$ 187,752,501	2,397,836	14,875,508	8,671,821	213,697,666	(26,595,540)	187,102,126	160,958,278

TUALITY HEALTHCARE AND SUBSIDIARIES
Consolidating Schedule of Balance Sheet Information
June 30, 2020 and 2019

Liabilities and Net Assets	Tuality Healthcare	TMSI/TMES	Tuality Property Management Co.	Tuality Healthcare Foundation	Total	Intercompany Eliminations	Consolidated	
							June 30, 2020	June 30, 2019
Current liabilities:								
Accounts payable	\$ 22,318,411	1,207,024	99,284	929,619	24,554,338	(9,791,935)	14,762,403	15,390,907
Accrued payroll and employee benefits	12,842,087	21,647	—	—	12,863,734	—	12,863,734	12,301,670
Deferred Revenue COVID CARES	16,590,355	—	—	—	16,590,355	—	16,590,355	—
Estimated liabilities for Medicare and Medicaid settlements	450,057	—	—	—	450,057	—	450,057	452,811
Long-term debt due within one year	1,021,001	—	—	—	1,021,001	—	1,021,001	1,047,012
Accrued bond interest payable	91,582	—	—	—	91,582	—	91,582	97,882
Total current liabilities	53,313,493	1,228,671	99,284	929,619	55,571,067	(9,791,935)	45,779,132	29,290,282
Long-term liabilities:								
Long-term debt, net of amount due within one year	12,072,581	—	—	—	12,072,581	—	12,072,581	13,068,958
Liability for pension benefits	66,443,796	—	—	—	66,443,796	—	66,443,796	51,789,617
Other long-term liabilities	23,884,941	—	—	—	23,884,941	—	23,884,941	20,509,248
Total long-term liabilities	102,401,318	—	—	—	102,401,318	—	102,401,318	85,367,823
Total liabilities	155,714,811	1,228,671	99,284	929,619	157,972,385	(9,791,935)	148,180,450	114,658,105
Net assets:								
Net assets without donor restrictions	23,647,198	1,169,165	14,776,224	475,990	40,068,577	(16,803,605)	23,264,972	38,542,676
Net assets with donor restrictions	—	—	—	7,266,212	7,266,212	—	7,266,212	7,757,497
Total net assets	23,647,198	1,169,165	14,776,224	7,742,202	47,334,789	(16,803,605)	30,531,184	46,300,173
Total liabilities and net assets	\$ 179,362,009	2,397,836	14,875,508	8,671,821	205,307,174	(26,595,540)	178,711,634	160,958,278

See accompanying independent auditors' report.

TUALITY HEALTHCARE AND SUBSIDIARIES

Consolidating Schedule of Operations

Years ended June 30, 2020 and 2019

	Tuality Healthcare	TMSI/TMES	Tuality Property Management Co.	Tuality Healthcare Foundation	Total	Intercompany Eliminations	Consolidated	
							June 30, 2020	June 30, 2019
Net patient service revenue:								
Patient service revenue (net of contractual allowances and discounts)	\$ 209,210,747	2,281,552	—	—	211,492,299	—	211,492,299	213,133,074
Charity care	(12,082,478)	—	—	—	(12,082,478)	—	(12,082,478)	(10,018,236)
Provision for bad debts	(5,203,308)	(62,745)	—	—	(5,266,053)	—	(5,266,053)	(11,986,876)
Total net patient service revenue	191,924,961	2,218,807	—	—	194,143,768	—	194,143,768	191,127,962
Other revenue COVID Cares	34,452,630	9,067	2,820,296	53,066	37,335,059	(3,762,772)	33,572,287	17,822,600
Other revenue	3,542,086	—	—	—	3,542,086	—	3,542,086	—
Total revenue	229,919,677	2,227,874	2,820,296	53,066	235,020,913	(3,762,772)	231,258,141	208,950,562
Operating expenses:								
Salaries and wages	88,253,076	373,173	—	—	88,626,249	—	88,626,249	85,227,833
Employee benefits	25,106,396	158,027	—	—	25,264,423	—	25,264,423	22,035,510
Supplies and other expenses	82,182,393	1,587,499	597,112	2,907	84,369,911	(2,744,870)	81,625,041	75,934,715
Professional fees	26,802,774	—	—	—	26,802,774	—	26,802,774	18,533,899
Management fees	—	223,512	491,724	—	715,236	(715,236)	—	—
Depreciation and amortization	8,227,603	24,525	245,951	—	8,498,079	—	8,498,079	8,176,628
Interest	781,179	—	—	—	781,179	—	781,179	733,784
Total operating expenses	231,353,421	2,366,736	1,334,787	2,907	235,057,851	(3,460,106)	231,597,745	210,642,369
(Loss)income from operations	(1,433,744)	(138,862)	1,485,509	50,159	(36,938)	(302,666)	(339,604)	(1,691,807)
Other income:								
Other operating revenue (expenses)	302,482	—	—	—	302,482	—	302,482	—
Realized income on investments whose use is limited by board designation	1,060,462	—	—	—	1,060,462	—	1,060,462	713,030
Change on Unrealized Gains (Losses) on Investments	(278,071)	—	—	(39,298)	(317,369)	—	(317,369)	—
Gain (loss) on investments in affiliated companies	4,572,807	(465,687)	—	(302,665)	3,804,455	(562,914)	3,241,541	1,095,760
Gain on disposal of property and equipment	(35,493)	—	—	—	(35,493)	—	(35,493)	90,867
Other nonoperating expenses	—	—	—	—	—	—	—	—
Total other income	5,622,187	(465,687)	—	(341,963)	4,814,537	(562,914)	4,251,623	1,899,657
Revenue in excess of expenses	4,188,443	(604,549)	1,485,509	(291,804)	4,777,599	(865,580)	3,912,019	207,850
Contributions for property and equipment acquisition	909,425	—	—	—	909,425	—	909,425	29,129
Change in Net Unrealized Gains (losses) on other than trading securities	—	—	—	—	—	—	—	623,095
Pension-related changes	(20,099,148)	—	—	—	(20,099,148)	—	(20,099,148)	(17,050,844)
(Decrease) increase in net assets with donor restrictions	\$ (15,001,280)	(604,549)	1,485,509	(291,804)	(14,412,124)	(865,580)	(15,277,704)	(16,190,770)

See accompanying independent auditors' report.