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REPORT OF INDEPENDENT AUDITORS
AND CONSOLIDATED FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION

SKY LAKES MEDICAL CENTER AND AFFILIATES

September 30, 2020 and 2019



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Report of Independent Auditors

To the Board of Directors
Sky Lakes Medical Center and Affiliates

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Sky Lakes Medical Center and Affiliates (the Medical Center), which comprise the consolidated balance sheets as of September 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 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 accounting principles generally accepted in the United States of America; 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.

Auditor's 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 audits 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 auditor's 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 the Medical Center as of September 30, 2020 and 2019, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary consolidating balance sheet, consolidating statement of operations, consolidating changes in net assets, combining balance sheet – obligated group, combining statement of operations – obligated group, and combining statement of changes in net assets – obligated group included on pages 37–44 are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and has not been subjected to the auditing procedures applied in the audit of the consolidated financial statements, and, accordingly, we express no opinion on it.

Moss Adams LLP

Portland, Oregon
January 22, 2021

Sky Lakes Medical Center and Affiliates
Consolidated Balance Sheets

ASSETS

	September 30,	
	2020	2019
CURRENT ASSETS		
Cash and cash equivalents	\$ 71,449,000	\$ 18,547,000
Certificates of deposit	419,000	6,871,000
Patient accounts receivable, net	29,182,000	28,812,000
Other receivables	5,883,000	6,060,000
Risk pool withhold receivable	5,154,000	7,269,000
Supplies inventories	6,366,000	5,985,000
Prepaid expenses	3,652,000	3,561,000
Promises to give, current portion	<u>750,000</u>	<u>750,000</u>
 Total current assets	 <u>122,855,000</u>	 <u>77,855,000</u>
 ASSETS LIMITED AS TO USE	 	
 PROPERTY AND EQUIPMENT, net	 1,578,000	 1,635,000
 INVESTMENTS	 	
 OTHER ASSETS	 <u>1,123,000</u>	 <u>1,180,000</u>
 Total assets	 <u>\$ 438,108,000</u>	 <u>\$ 399,270,000</u>

Sky Lakes Medical Center and Affiliates
Consolidated Balance Sheets

LIABILITIES AND NET ASSETS

	September 30,	
	2020	2019
CURRENT LIABILITIES		
Accounts payable	\$ 6,294,000	\$ 9,337,000
Construction cost payable	-	6,518,000
Accrued payroll	10,416,000	8,296,000
Accrued compensated absences	5,791,000	5,092,000
Accrued interest payable	258,000	369,000
Other accrued expenses	11,821,000	13,703,000
Estimated third-party payor settlements	2,667,000	1,616,000
Current advance and refund liabilities	8,111,000	-
Capital lease obligations, current portion	733,000	605,000
Long-term debt, current portion	<u>4,100,000</u>	<u>3,882,000</u>
 Total current liabilities	 <u>50,191,000</u>	 <u>49,418,000</u>
LONG-TERM LIABILITIES		
Capital lease obligations, net of current portion	4,052,000	4,387,000
Long-term debt, net of current portion and deferred financing costs	68,575,000	72,944,000
Advance and refund liabilities, net of current portion	24,331,000	-
Other long-term liabilities	<u>7,143,000</u>	<u>7,477,000</u>
 Total long-term liabilities	 <u>104,101,000</u>	 <u>84,808,000</u>
 Total liabilities	 <u>154,292,000</u>	 <u>134,226,000</u>
NET ASSETS		
Without donor restrictions		
Sky Lakes Medical Center	276,223,000	257,976,000
Non-controlling interest	<u>1,379,000</u>	<u>1,272,000</u>
 Total without donor restrictions	 <u>277,602,000</u>	 <u>259,248,000</u>
 With donor restrictions	 <u>6,214,000</u>	 <u>5,796,000</u>
 Total net assets	 <u>283,816,000</u>	 <u>265,044,000</u>
 Total liabilities and net assets	 <u>\$ 438,108,000</u>	 <u>\$ 399,270,000</u>

Sky Lakes Medical Center and Affiliates
Consolidated Statements of Operations

	Years Ended September 30,	
	2020	2019
REVENUES		
Patient service revenue, net of contractual adjustments	\$ 242,137,000	\$ 265,165,000
Provision for bad debts	<u>(7,291,000)</u>	<u>(7,941,000)</u>
Net patient service revenue	234,846,000	257,224,000
Other revenue	<u>29,931,000</u>	<u>11,090,000</u>
Total revenues	<u>264,777,000</u>	<u>268,314,000</u>
EXPENSES		
Salaries and benefits	129,378,000	124,217,000
Purchased services	28,370,000	32,502,000
Drugs	18,617,000	19,844,000
Supplies	17,636,000	17,919,000
Building and maintenance	14,845,000	15,450,000
Depreciation and amortization	12,674,000	11,069,000
Provider tax	12,074,000	13,512,000
Physician fees	8,646,000	7,929,000
Other	3,502,000	4,692,000
Interest expense	2,895,000	3,214,000
Insurance	1,898,000	2,004,000
Minor equipment	1,443,000	1,045,000
Professional fees	1,436,000	2,491,000
Rentals and lease expense	<u>1,416,000</u>	<u>1,395,000</u>
Total expenses	<u>254,830,000</u>	<u>257,283,000</u>
OPERATING INCOME	<u>9,947,000</u>	<u>11,031,000</u>
OTHER INCOME (EXPENSE)		
Investment income	6,330,000	8,759,000
Contributions	674,000	647,000
Net assets released from restriction	1,477,000	2,071,000
Other non-operating expense	<u>(1,120,000)</u>	<u>(1,031,000)</u>
Total other income, net	<u>7,361,000</u>	<u>10,446,000</u>
EXCESS OF REVENUES OVER EXPENSES	<u>\$ 17,308,000</u>	<u>\$ 21,477,000</u>

Sky Lakes Medical Center and Affiliates
Consolidated Statements of Changes in Net Assets

	Years Ended September 30,	
	2020	2019
NET ASSETS WITHOUT DONOR RESTRICTIONS		
Excess of revenues over expenses	\$ 17,308,000	\$ 21,477,000
Distributions to non-controlling interest	62,000	107,000
Net change in unrealized gains and losses on other-than-trading securities	<u>984,000</u>	<u>(129,000)</u>
	<u>18,354,000</u>	<u>21,455,000</u>
NET ASSETS WITH DONOR RESTRICTIONS		
Contributions	1,335,000	509,000
Net change in unrealized gains and losses on other-than-trading securities	245,000	(187,000)
Investment income	315,000	425,000
Net assets released from restrictions	<u>(1,477,000)</u>	<u>(2,071,000)</u>
	<u>418,000</u>	<u>(1,324,000)</u>
CHANGE IN NET ASSETS	18,772,000	20,131,000
NET ASSETS, beginning of year	<u>265,044,000</u>	<u>244,913,000</u>
NET ASSETS, end of year	<u>\$ 283,816,000</u>	<u>\$ 265,044,000</u>

Sky Lakes Medical Center and Affiliates
Consolidated Statements of Cash Flows

	Years Ended September 30,	
	2020	2019
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 18,772,000	\$ 20,131,000
Adjustments to reconcile change in net assets to net cash from operating activities		
Depreciation and amortization	12,674,000	11,069,000
Net amortization of premiums and accretion of discounts on investments held-to-maturity	300,000	359,000
Net amortization of premiums and accretion of discounts on bonds	(267,000)	(267,000)
Net amortization of deferred financing costs	53,000	54,000
Net change in unrealized gains and losses on other-than-trading securities	(1,229,000)	316,000
Gain on sale of investments	(2,949,000)	(4,308,000)
Increase in the cash surrender value of corporate owned life insurance	3,000	1,273,000
Contributions to non-controlling interest	(62,000)	(107,000)
(Increase) decrease in		
Patient accounts receivable, net	(370,000)	2,370,000
Other receivables	177,000	(161,000)
Risk pool withhold receivable	2,115,000	(3,474,000)
Supplies inventories	(381,000)	(623,000)
Prepaid expenses	(91,000)	(914,000)
Other assets	57,000	56,000
Receivable related to collaborative healthcare building	57,000	9,443,000
Increase (decrease) in		
Accounts payable	(3,043,000)	3,298,000
Accrued payroll	2,120,000	339,000
Accrued compensated absences	699,000	164,000
Accrued interest payable	(111,000)	72,000
Advance and refund liabilities	32,442,000	-
Other accrued expenses	(1,882,000)	205,000
Estimated third-party payor settlements	1,051,000	599,000
Other long-term liabilities	(334,000)	486,000
Net cash from operations	<u>59,801,000</u>	<u>40,380,000</u>

Sky Lakes Medical Center and Affiliates
Consolidated Statements of Cash Flows

	Years Ended September 30,	
	2020	2019
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale/redemption of investments	\$ 49,644,000	\$ 28,391,000
Purchase of investments	(31,554,000)	(24,559,000)
Purchase of corporate owned life insurance	(6,793,000)	(8,454,000)
Redemption of certificates of deposit	6,452,000	5,839,000
Purchase of property and equipment	<u>(20,137,000)</u>	<u>(36,647,000)</u>
Net cash flows used in investing activities	<u>(2,388,000)</u>	<u>(35,430,000)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of new loan	-	5,000,000
Payments on long-term debt	(3,937,000)	(3,141,000)
Payment on capital lease obligations	(636,000)	(533,000)
Contributions from non-controlling interest	<u>62,000</u>	<u>107,000</u>
Net cash flows from financing activities	<u>(4,511,000)</u>	<u>1,433,000</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	52,902,000	6,383,000
CASH AND CASH EQUIVALENTS, beginning of year	18,547,000	12,164,000
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 71,449,000</u>	<u>\$ 18,547,000</u>

Cash paid for interest, as of September 30, 2020 and 2019, was approximately \$3,006,000 and \$3,142,000, respectively.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies

Organization

Sky Lakes Medical Center (the Medical Center) is a not-for-profit hospital located in south-central Oregon. The Medical Center provides inpatient, outpatient, and emergency care services to the residents of Southern Oregon and Northern California. The Medical Center was incorporated in Oregon in 1963.

Principles of consolidation

The consolidated financial statements include the accounts of the Medical Center and all of its wholly-owned and majority-owned subsidiaries. There are four other entities included in these consolidated financial statements:

West Physician Services, LLC dba Sky Lakes Physician Services (WPS) – West Physician Services, LLC dba Sky Lakes Physician Services was established by the Medical Center in 2003 to provide specialty care to patients. The Medical Center is the sole member of WPS.

Sky Lakes Medical Center Foundation, Inc. (the Foundation) – Sky Lakes Medical Center Foundation is a not-for-profit corporation formed to advance the work of the Medical Center through philanthropy. The Foundation is led by a board of directors who serve voluntarily and are elected by the Medical Center.

Klamath Medical Business Center, LLC (KMBC) – In 2004, the Medical Center, together with Cascade Comprehensive Care, Inc. (CCC), formed Klamath Medical Business Center, LLC. The Medical Center directly owns 50% of KMBC. In addition, they indirectly own approximately 17% through their ownership in CCC (Note 5). In addition, the Medical Center performs management functions for KMBC. KMBC exists for the purpose of leasing building facilities to the Medical Center and CCC.

KW Campus, LLC (KW) – In 2015 the Medical Center, together with an unrelated limited liability entity formed KW Campus, LLC. KW was formed to develop a central campus in Klamath Falls, Oregon that is home to a variety of organizations whose purpose is to deliver health care, wellness and safety services, and provide opportunities for those served to improve their lives through effort and reward as part of their journey to self-sufficiency. The Medical Center directly owns 50% of KW and performs some of the management functions for KW.

All significant intercompany transactions have been eliminated.

Basis of presentation

The accompanying consolidated financial statements are prepared under the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America and in accordance with the provisions of the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 958, *Not-for-Profit Entities*. The Medical Center has implemented ASC 958 and has adjusted the presentation in these consolidated financial statements, accordingly, including changes to the presentation of net asset classification on the financial statements, inclusion of information about liquidity and availability of resources (Note 16), and inclusion of information provided about expenses (Note 17). Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

Net Assets Without Donor Restrictions – Net assets available for use in general operations and not subject to donor restrictions.

Net Assets With Donor Restrictions – Net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires; that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

Use of estimates

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States 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 the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Significant estimates are necessary in determining the fair value of investments, the recorded value of the contractual and bad debt allowance, amount due to or from third parties, risk pool withhold receivable and useful lives of fixed assets. Management believes the assumptions used in arriving at these estimates are reasonable.

Fair value measurements

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. Market participants are buyers and sellers, who are independent, knowledgeable, and willing and able to transact in the principal (or most advantageous) market for the asset or liability being measured.

Fair value is based on quoted market prices, when available, for identical or similar assets or liabilities. In the absence of quoted market prices, management determines the fair value of the Medical Center's assets and liabilities using valuation models or third-party pricing services, both of which rely on market-based parameters when available, such as interest rate yield curves, option volatilities, and credit spreads. The valuation techniques used are based on observable and unobservable inputs.

The following methods and assumptions were used by the Medical Center in estimating fair values of each class of financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents – The carrying amount approximates the fair value because of the short maturity of those instruments.

Long-term debt – Long-term debt is estimated by discounting future cash flows at rates currently available for debt with similar terms and remaining maturities. The carrying amount approximates the fair value.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

Cash and cash equivalents

Cash and cash equivalents include certain investments in highly liquid debt instruments with original maturities of three months or less. Financial instruments potentially subjecting the Medical Center to concentrations of credit risk consist primarily of bank demand deposits in excess of FDIC insured limits. The Medical Center has not experienced any losses in such accounts.

Certificates of deposit

Certificates of deposit are held at various financial institutions and range in maturity through September 2021 and bear an interest rate of 0.95%. Certificates of deposit are not subject to withdrawal limitations and are classified as current assets. Early withdrawal may result in a forfeiture of interest earned.

Patient accounts receivable

In evaluating the collectability of receivables, the Medical Center analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts. Patient accounts receivables are reduced by an allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Medical Center analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients, the Medical Center records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts. The Medical Center's allowance for contractual adjustments was approximately \$53,476,000 and \$50,444,000 at September 30, 2020 and 2019, respectively. The Medical Center's bad debt provision was \$15,491,000 and \$13,243,000 at September 30, 2020 and 2019, respectively. There was no change in the methodology used by the Medical Center to estimate the allowance for contractual adjustments and bad debt provision in the current year.

The mix of gross receivables from patients and third-party payors was as follows at September 30:

	<u>2020</u>	<u>2019</u>
Medicare	37%	42%
Medicaid	23%	17%
Other third-party payors	32%	36%
Self-pay	8%	5%
 Total	 <u>100%</u>	 <u>100%</u>

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

Other receivables

Other receivables consist mainly of the receivable from the stock redemption with an affiliate, provider tax receivable, employee loan receivables, physician loan receivables, and other miscellaneous receivables. These receivables are reduced by an allowance for doubtful accounts determined on a specific reserve basis.

Risk pool withhold receivable

The risk pool withhold receivable represents funds withheld from claims paid to the providers. Based upon insurance carrier's performance, the funds are either retained by the insurer or paid to the Medical Center.

Supplies inventories

Supplies inventories consist mainly of patient supplies and pharmaceuticals and are carried at the lower of cost (primarily average cost) or net realizable value.

Promises to give

Unconditional promises to give are recognized as revenues or gains in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the promise becomes unconditional.

Assets limited as to use

Assets limited as to use include assets held by trustees under indenture agreements (Note 4).

Property and equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method. 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. Such amortization is included in depreciation and amortization in the financial statements. Interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

Gifts of long-lived assets such as land, buildings or equipment are reported as unrestricted support, and are excluded from the excess of revenues over expenses, unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained; expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

Investments

Investments in equity securities with readily determinable fair values and all investments that are available-for-sale are measured at fair value on the balance sheet. Investment securities that management has the positive intent and ability to hold until maturity are classified as held-to-maturity and are carried at their remaining unpaid principal balance, net of unamortized premiums or unaccreted discounts. Premiums are amortized and discounts are accreted using the effective interest method over the period remaining until maturity. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in the excess of revenues over expenses unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from the excess of revenues over expenses unless the investments are trading securities.

The Medical Center has purchased various cash-surrender value life insurance policies on key management. The policies are recorded at the estimated cash-surrender value of the policies. Increases in the cash-surrender value are recorded as investment income.

The Medical Center also has various investments in health-related organizations. Generally, when the ownership interest in health-related activities is more than 50%, the activities are consolidated, and a minority interest is recorded if appropriate. When the ownership interest is at least 20%, but not more than 50%, it is typically accounted for on the equity method, and the income or loss is reflected in net revenue. Activities with less than 20% ownership or lacking significant influence over the operations of the related entity are carried at the lower of cost or estimated net realizable value.

Health insurance

The Medical Center offers health insurance (the Employee Benefit Plan) to its active employees and families. The Medical Center pays approximately 80% of the premium and employees contribute the remaining 20% through bi-weekly payroll deductions. The Employee Benefit Plan provides medical, dental, vision, and prescription coverage. The Employee Benefit Plan is self-funded, but is reinsured through HM Life Insurance Company with a specific attachment point of \$270,000 per covered individual annually plus a \$60,000 aggregating specific with an unlimited lifetime maximum. The Medical Center has established reserve amounts based upon information as to the status of claims plus development factors for incurred but not yet reported claims and anticipated future changes in underlying case reserves. Such reserve amounts are only estimates and there can be no assurance that the Medical Center's future Employee Benefit Plan obligations will not exceed the amount of its reserves. The Medical Center's reserve for health insurance was approximately \$2,163,000 and \$2,592,000 at September 30, 2020 and 2019, respectively, and is included in accrued payroll on the consolidated balance sheet.

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

Workers' compensation

The Medical Center is self-funded for workers' compensation insurance, but is reinsured through Safety National Casualty Corporation with a specific attachment point of \$500,000 per claim. The Medical Center has contracted with Tristar Risk Management to act as the third party administrator to process and pay claims. The Medical Center has established reserve amounts based upon information as to the status of claims plus development factors for incurred but not yet reported claims and anticipated future changes in underlying case reserves. Such reserve amounts are only estimates and there can be no assurance that the Medical Center's future workers' compensation obligations will not exceed the amount of its reserves. The Medical Center's reserve for workers' compensation was \$536,000 and \$826,000 at September 30, 2020 and 2019, respectively, and is included in accrued payroll on the consolidated balance sheet. Further, the Department of Consumer and Business Services Workers' Compensation Division requires a security deposit be maintained to support expected future claims and processing costs. As of September 30, 2020, the security deposit requirement was \$878,000. To fulfill the security deposit requirement, the Medical Center has a standby letter of credit with US Bank for \$1,190,000 with an expiration date of July 21, 2021.

Estimated malpractice costs

The provision for estimated medical malpractice claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported. Estimated malpractice costs are included in other accrued expenses on the consolidated balance sheets and were approximately \$240,000 and \$262,000 as of September 30, 2020 and 2019, respectively. The Medical Center estimated no receivable as of September 30, 2020 and 2019.

Net patient service revenue

The Medical Center has agreements with third-party payors that provide for payments to the Medical Center at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. For uninsured patients that do not qualify for charity care, the Medical Center recognizes revenue on the basis of its standard rates for services provided. On the basis of historical experience, a significant portion of the Medical Center's uninsured patients will be unable or unwilling to pay for the services provided.

Thus, the Medical Center records a significant provision for bad debts related to uninsured patients in the period the services are provided. Net patient service revenue is reported at 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.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

Charity care

The Medical Center provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Medical Center does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The policy of the Medical Center for charity care includes providing non-elective services to patients whose household income falls at or below 250% of the Federal Poverty Level at no cost. For those patients who fall between 250% and 400% of the Federal Poverty Level and who are unable to pay their bills, patients are eligible for either a partial write-off of their account, annual maximum out of pocket, or both. The policy applies to both insured patients as well as uninsured patients provided the patient meets the eligibility criteria. Total cost of charity care provided by the Medical Center was approximately \$3,573,000 and \$4,444,000 for the years ending September 30, 2020 and 2019, respectively.

Donated restricted gifts

Unconditional promises to give cash and other assets to the Medical Center 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 gift is received.

The gifts are reported as net assets with donor restrictions 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 are reclassified as without donor restrictions and reported in the statement of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as contributions without donor restrictions in the accompanying financial statements.

Excess of revenues over expenses

The consolidated statement of operations includes excess of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include the net change in unrealized gains and losses on investments other-than-trading securities, contributions, and distributions.

Volunteers

A significant portion of the Medical Center's gift shop operations and patient relations functions are conducted by unpaid volunteers. The value of this contributed time is not reflected in the accompanying consolidated financial statements since the volunteers' time does not meet the criteria for recognition.

Income taxes

The Medical Center and Foundation are tax-exempt organizations and are not subject to state or federal income taxes, except on unrelated business income, in accordance with Section 501(c)(3) of the Internal Revenue Code.

The Medical Center and Foundation had no unrecognized tax benefits at September 30, 2020 or 2019. The Medical Center and Foundation recognize interest accrued and penalties related to unrecognized tax benefits as an administrative expense. During the years ended September 30, 2020 and 2019, the Medical Center and Foundation recognized no interest and penalties.

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

The Medical Center files an exempt organization information return and an unrelated business income tax return in the U.S. federal jurisdiction and an unrelated business income tax return with the Oregon Department of Revenue.

The Foundation files an exempt organization information return in the U.S. federal jurisdiction.

WPS, the Medical Center's for-profit corporate subsidiary, accounts for income taxes in accordance with Accounting Standards Codification ("ASC") 740-10, whereby, income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consist of taxes currently due plus deferred taxes. Deferred taxes are recognized for differences between the basis of assets and liabilities for financial statement and income tax purposes. WPS has no history of sustained profitability and any deferred tax assets, net of liabilities, has been fully reserved for at September 30, 2020 and 2019.

KMBC and KW have elected to be taxed under the provisions of the Oregon Limited Liability Company Act. Under those provisions, the LLC's do not pay federal income tax on their taxable income. Instead, the members are liable for income taxes on each LLC's taxable income.

The Klamath Falls Intercommunity Hospital Authority (the Authority) is a municipal corporation under Oregon state law and is not subject to federal income tax.

Accounting standards updates

ASU No. 2016-14 – In August 2016, the FASB issued *Presentation of Financial Statements of Not-for-Profit Entities* (Topic 958), which improves the current net asset classification requirements and the information presented in financial statements and notes about an entity's liquidity, financial performance, and cash flows. The update removes the requirement to present three classes of net assets with two classes, net assets with donor restrictions and net assets without donor restrictions. The update also removes the requirement to present or disclose the indirect method (reconciliation) if using the direct method for the statement of cash flows as well as added several additional enhanced disclosures to the notes. The amendments in this update are effective for fiscal years beginning after December 15, 2017. The Medical Center adopted this standard for the year ended September 30, 2019.

ASU 2014-09 – In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, which creates Topic 606 and supersedes Topic 605, *Revenue Recognition*. The core principle of Topic 606 is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In general, the new guidance requires companies to use more judgment and make more estimates than under current guidance, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. For financial reporting purposes, the standard allows for either full retrospective adoption, meaning the standard is applied to all of the periods presented, or modified retrospective adoption, meaning the standard is applied only to the most current period presented in the financial statements with the cumulative effect of initially applying the standard recognized at the date of initial application.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 1 – Description of Organization and Summary of Significant Accounting Policies (continued)

ASU 2016-02 – In February 2016, the FASB issued ASU No. 2016-02, *Leases* (Topic 842), which increases transparency and comparability among entities by recognizing lease assets and lease liabilities on the statement of financial position and disclosing key information about leasing arrangements in the financial statements of lessees.

Entities were able to elect deferral of these ASU's ASU 2020-05, *Revenue from Contracts with Customers (Topic 606) and Leases (Topic 842): Effective Dates for Certain Entities*. The new effective date for ASU 2014-09 is annual reporting periods beginning after December 15, 2019. The new effective date for ASU 2016-02 is fiscal years beginning after December 15, 2021. Management is currently evaluating the impact of the provisions of ASU No. 2014-09 and 2016-02 on the financial statements.

Subsequent events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. The Medical Center recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing the financial statements. The Medical Center's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before financial statements are issued.

The Medical Center has evaluated subsequent events through January 22, 2021, which is the date the financial statements were issued. See Note 19.

Reclassifications

Certain reclassifications have been made to the 2019 consolidated financial statements to conform to current-year presentations. These reclassifications did not affect previously reported excess of revenues over expenses or net assets.

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 2 – Net Patient Service Revenue

The Medical Center has agreements with third-party payors that provide for payments to the Medical Center at amounts different from its established rates. A summary of the payment arrangements with major third-party payors are as follows:

- *Medicare* – Inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to patient classification systems that are based on clinical, diagnostic, and other factors. Medical education costs and uncollected bad debts on patient accounts related to Medicare beneficiaries are paid based on a modified cost reimbursement methodology. The Medical Center is a Medicare Designated Sole Community Hospital (SCH). As such, the Medical Center receives certain payment enhancements and protections to the hospital. For inpatient services, Sole Community Hospitals receive the higher of payments under 1) the Inpatient Prospective Payment System (IPPS) or 2) an updated hospital-specific rate (HSR), which are payments based on their costs in a base year (1982, 1987 or 1996) updated to the current year and adjusted for changes in their case mix. Since 2006, SCHs also receive an additional adjustment set at 7.1% above the Outpatient Prospective Payment System (OPPS) rate for outpatient services. Additionally, SCHs can qualify for adjustments due to decreases in inpatient volume, participation in the Hospital Value-Based Purchasing Program, and participation in the Hospital Readmissions Reduction Program. The Medical Center is reimbursed for outpatient cost reimbursable items at a tentative rate with final settlement determined after submission of the annual cost report by the Medical Center and audit thereof by the Medicare fiscal intermediary.
- Atrio Health Plans, Inc. is a for-profit Oregon health care service, of which CCC owns a minority interest (Note 5 and 14). Atrio Health Plans, Inc. provides Medicare Advantage Plans to residents primarily of Douglas, Jackson, Klamath, Marion, Josephine and Polk counties.
- *Medicaid* – Inpatient services rendered to Medicaid program beneficiaries are reimbursed at prospectively determined rates and outpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement methodology. The Medical Center is reimbursed at a tentative rate with final settlement determined after submission of the annual cost report by the Medical Center and finalization of the cost report by the Oregon Division of Medical Assistance Programs (DMAP).
- CCC is a local Medicaid claims administrator of which the Medical Center owns 33% (Note 5 and 14). The Medical Center is paid on an interim basis based upon prospectively determined rates. The Medical Center also participates in a risk pool arrangement that encourages cost containment.

Entities doing business with governmental payors, including Medicare and Medicaid, are subject to risks unique to the government-contracting environment that are difficult to anticipate and quantify. Revenues are subject to adjustment as a result of examination by government agencies as well as auditors, contractors, and intermediaries retained by the federal, state, or local governments (collectively “Government Agents”). Resolution of such audits or reviews often extends (and in some cases does not even commence until) several years beyond the year in which services were rendered and/or fees received.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 2 – Net Patient Service Revenue (continued)

Moreover, different Government agencies frequently interpret government regulations or other requirements differently. For example, Government agencies might disagree on a patient's principal medical diagnosis, the appropriate code for a clinical procedure, or many other matters. Such disagreements might have a significant effect on the ultimate payout due from the government to fully recoup sums already paid. Governmental agencies may make changes in program interpretations, requirements, or "conditions of participation," some of which may have implications for amounts previously estimated. In addition to varying interpretation and evolving codification of the regulations, standards of supporting documentation and required data are subject to wide variation.

In accordance with generally accepted accounting principles, to account for the uncertainty around Medicare and Medicaid revenues, the client estimates the amount of revenue that will ultimately be received under the Medicare and Medicaid programs. Amounts ultimately received or paid may vary significantly from these estimates.

The Medical Center has also entered into payment arrangements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to the Medical Center under these agreements includes prospectively determined rates per discharge, discounts and established charges, and prospectively determined daily rates.

Patient service revenue, net of contractual allowances of approximately \$386,811,000 and \$390,911,000 for the years ending September 30, 2020 and 2019, respectively, recognized in the period from major payor sources is as follows:

	<u>2020</u>	<u>2019</u>
Other third-party payors	\$ 82,428,000	\$ 96,111,000
Medicare	88,049,000	97,614,000
Medicaid	51,449,000	56,684,000
Other	18,837,000	13,080,000
Self-pay	1,374,000	1,676,000
Provision for bad debts	<u>(7,291,000)</u>	<u>(7,941,000)</u>
 Total net patient service revenue	 <u>\$ 234,846,000</u>	 <u>\$ 257,224,000</u>

Note 3 – Promises to Give

Unconditional promises to give were \$750,000 as of September 30, 2020 and 2019.

At September 30, 2020 and 2019, substantially all unconditional promises to give were from one donor.

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 4 – Assets Limited as to Use

Assets held by trustees under indenture agreements for the bonds outstanding include money market accounts of \$1,424,000 and \$1,483,000 as of September 30, 2020 and 2019, respectively.

As part of its commitment to improving the health of the community, the Medical Center collaborated with Oregon Health & Science University (“OHSU”) through the creation of Oregon Rural Health Initiative (“ORHI”), a nonprofit corporation formed November 2016, to construct a new healthcare building in Klamath Falls. As part of the commitment to ORHI, the Medical Center granted \$25 million that was utilized by ORHI to solicit additional funding towards the project. Distributions were made by ORHI in support of the Medical Center in connection with the healthcare building. All funds were returned to the Medical Center for costs associated with the healthcare building during the year ended September 30, 2019.

Note 5 – Investments

Investments at September 30 include:

	<u>2020</u>	<u>2019</u>
Corporate bonds, held-to-maturity	\$ 39,953,000	\$ 56,220,000
Life insurance	95,996,000	89,206,000
Money market	1,578,000	1,635,000
Common stocks	19,429,000	20,955,000
Certificates of deposit	419,000	6,871,000
Cascade Comprehensive Care, Inc.	6,369,000	4,348,000
Mutual funds	8,702,000	7,179,000
Southern Oregon Linen Services, Inc.	<u>432,000</u>	<u>395,000</u>
	<u><u>\$ 172,878,000</u></u>	<u><u>\$ 186,809,000</u></u>

The reconciliation between investments on the consolidated financial statements and the above table is as follows as of September 30:

	<u>2020</u>	<u>2019</u>
Investments	\$ 170,881,000	\$ 178,303,000
Assets limited as to use	1,578,000	1,635,000
Certificates of deposit	<u>419,000</u>	<u>6,871,000</u>
	<u><u>\$ 172,878,000</u></u>	<u><u>\$ 186,809,000</u></u>

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 5 – Investments (continued)

Southern Oregon Linen Service, Inc. – The Medical Center owns 12.7% of the common stock in Southern Oregon Linen Service (SOLS). SOLS was established in 1996 as a central cooperative laundry to service several regional hospitals. The Medical Center concluded that it could not exert influence over SOLS' operations and financial activities; therefore, the Medical Center is accounting for the investment on the cost method.

Cascade Comprehensive Care, Inc. – The Medical Center owns 33% of the common stock in CCC, which is accounted for using the equity method. CCC is a managed health care company that currently manages a Medicaid contract under the Oregon Health Plan. CCC handles quality assurance, utilization management, claims adjudication, pharmacy management, encounter reporting, financial and solvency reporting, physician and provider contracting, reinsurance/stoploss issues, risk model management etc. for the local community.

The following represents the unaudited summary financial information for CCC for the years ended September 30:

	2020 (unaudited)	2019 (unaudited)
Current assets	\$ 42,017,000	\$ 31,231,000
Noncurrent assets	<u>14,440,000</u>	<u>12,604,000</u>
 Total assets	 <u>\$ 56,457,000</u>	 <u>\$ 43,835,000</u>
 Current liabilities	 \$ 28,324,000	\$ 29,072,000
Noncurrent liabilities	10,551,000	2,140,000
Equity	<u>17,582,000</u>	<u>12,623,000</u>
 Total liabilities and equity	 <u>\$ 56,457,000</u>	 <u>\$ 43,835,000</u>
 Operating revenue	 \$ 108,939,000	\$ 107,730,000
Operating expenses	<u>103,101,000</u>	<u>96,637,000</u>
 Operating income	 <u>\$ 5,838,000</u>	 <u>\$ 11,093,000</u>

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 6 – Fair Value Measurements

Financial Accounting Standards Board ASC 820, Fair Value Measurements and Disclosures, provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurement) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

Basis of fair value measurement

Level 1 – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Medical Center has the ability to access.

Level 2 – Inputs to the valuation methodology are quoted prices in markets that are not considered to be active or financial instruments without quoted market prices, but for which all significant inputs are observable, either directly or indirectly.

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

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at September 30, 2020 and 2019.

Corporate bonds, held-to-maturity – Investment securities that management has the positive intent and ability to hold until maturity are classified as held-to-maturity and are carried at their remaining unpaid principal balance, net of unamortized premiums or unaccreted discounts and therefore excluded from the fair value tables.

Life insurance – Valued at the estimated cash-surrender value of the policies. The carrying amount approximates fair value.

Mutual funds and money market funds – Valued at the net asset value of shares held by the Medical Center at year end using prices quoted by the relevant pricing agent.

Common stocks – Valued at the closing price reported on the active market on which the individual securities are traded.

Certificates of deposit – Valued at fair value by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the credit-worthiness of the issuer.

Sky Lakes Medical Center and Affiliates
Notes to Consolidated Financial Statements

Note 6 – Fair Value Measurements (continued)

The following tables disclose by level, the fair value hierarchy, of the Medical Center's assets at fair value at September 30, 2020:

	Fair Value Measurements			
	Total Fair Value	Level One	Level Two	Level Three
Common stock				
Consumer goods	\$ 2,510,000	\$ 2,510,000	\$ -	\$ -
Other	181,000	181,000	-	-
Healthcare	1,543,000	1,543,000	-	-
Utilities	1,042,000	1,042,000	-	-
Industrial goods	2,954,000	2,954,000	-	-
Services	2,857,000	2,857,000	-	-
Basic materials	2,361,000	2,361,000	-	-
Financial	1,728,000	1,728,000	-	-
Technology	4,253,000	4,253,000	-	-
Life insurance	95,996,000	-	95,996,000	-
Mutual funds				
Equity funds	3,921,000	3,921,000	-	-
Hybrid funds	1,132,000	1,132,000	-	-
Bond funds	1,330,000	1,330,000	-	-
Value funds	545,000	545,000	-	-
Money market funds	1,774,000	1,774,000	-	-
Other funds	1,578,000	1,578,000	-	-
Certificates of deposit	419,000	-	419,000	-
	<u>\$ 126,124,000</u>	<u>\$ 29,709,000</u>	<u>\$ 96,415,000</u>	<u>\$ -</u>

Total investments held-to-maturity, valued at cost, and investments in other healthcare entities accounted for at cost or equity as of September 30, 2020 were approximately \$46,754,000.

Sky Lakes Medical Center and Affiliates
Notes to Consolidated Financial Statements

Note 6 – Fair Value Measurements (continued)

The following tables disclose by level, the fair value hierarchy, of the Medical Center's assets at fair value at September 30, 2019:

	Fair Value Measurements			
	Total Fair Value	Level One	Level Two	Level Three
Common stock				
Consumer goods	\$ 3,649,000	\$ 3,649,000	\$	\$ -
Other	247,000	247,000	-	-
Healthcare	3,624,000	3,624,000	-	-
Utilities	1,396,000	1,396,000	-	-
Industrial goods	1,893,000	1,893,000	-	-
Services	1,155,000	1,155,000	-	-
Basic materials	1,599,000	1,599,000	-	-
Financial	2,398,000	2,398,000	-	-
Technology	4,994,000	4,994,000	-	-
Life insurance	89,206,000	-	89,206,000	-
Mutual funds				
Equity funds	3,001,000	3,001,000	-	-
Hybrid funds	1,303,000	1,303,000	-	-
Bond funds	729,000	729,000	-	-
Value funds	621,000	621,000	-	-
Money market funds	1,723,000	1,723,000	-	-
Other funds	1,437,000	1,437,000	-	-
Certificates of deposit	6,871,000	-	6,871,000	-
	<u>\$ 125,846,000</u>	<u>\$ 29,769,000</u>	<u>\$ 96,077,000</u>	<u>\$ -</u>

Total investments held-to-maturity, valued at cost, and investments in other healthcare entities accounted for at cost or equity as of September 30, 2019 were \$60,963,000.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 7 – Property and Equipment

A summary of property and equipment at September 30 follows:

	2020	2019
Buildings and fixed equipment	\$ 184,438,000	\$ 139,285,000
Moveable equipment	84,999,000	78,182,000
Equipment under capital lease obligations	8,458,000	11,173,000
Land improvements	6,664,000	5,034,000
Land	4,638,000	4,638,000
Leasehold improvements	343,000	343,000
	<hr/>	<hr/>
Less: Accumulated depreciation and amortization	(152,482,000)	(147,463,000)
	<hr/>	<hr/>
Construction in progress	137,058,000	91,192,000
	4,613,000	49,105,000
	<hr/>	<hr/>
Property and equipment, net	<u>\$ 141,671,000</u>	<u>\$ 140,297,000</u>

Depreciation expense from operations for the years ended September 30, 2020 and 2019 was \$11,790,000 and \$9,980,000, respectively. Amortization expense for the years ended September 30, 2020 and 2019 was \$884,000 and \$1,089,000, respectively. Accumulated amortization for equipment under capital lease obligations was \$6,265,000 and \$7,578,000 at September 30, 2020 and 2019, respectively. Construction in Progress was \$4,613,000 and \$49,105,000 at September 30, 2020 and 2019, respectively. Construction in Progress of \$49,105,000 at September 30, 2019, was primarily due to the construction of the collaborative health building (Note 4), which was completed during the year-ended September 30, 2020.

Note 8 – Plum Ridge Care Center

Lease value of Plum Ridge Care Center – In 2001, Klamath County, Oregon deeded the Plum Ridge Care Center to the Authority. The Medical Center entered into a long-term lease agreement for a period of 89 years for the sum of \$1 per year. In addition, the Medical Center has the option of purchasing the property at any time for the sum of \$1. The Medical Center recognized the fair value of the lease at the time the agreement with the Authority was entered into. The Medical Center is amortizing the lease value over the life of the lease. The lease value of Plum Ridge Care Center at September 30, 2020 and 2019 was approximately \$1,123,000 and \$1,180,000, respectively, and is included in other assets in the consolidated balance sheet.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 8 – Plum Ridge Care Center (continued)

Deferred rental revenue – In 2001, the Medical Center subleased the Plum Ridge Care Center to Plum Ridge Care Community, LLC, an unrelated third party, on equivalent lease terms as to the Medical Center's lease with the Authority, except the Medical Center did not grant the right to purchase the property to Plum Ridge Care Community, LLC. The Medical Center recognized a liability to Plum Ridge Care Community, LLC, for the lease value of the remaining term of the lease. The revenue is being amortized over the lease term. The deferred rental revenue of Plum Ridge Care Center was approximately \$2,307,000 and \$2,341,000 at September 30, 2020 and 2019, respectively, and is included in other long-term liabilities in the consolidated balance sheet.

Sky Lakes Medical Center and Affiliates
Notes to Consolidated Financial Statements

Note 9 – Capital Leases

Capital leases as of September 30 are as follows:

	<u>2020</u>	<u>2019</u>
Facility lease with a private party with monthly payments of \$36,274 at 8.90% through September 2037.	\$ 3,807,000	\$ 3,899,000
Equipment lease-purchase agreement with CareFusion Solutions, LLC with monthly payments of \$15,500 at 2.64% through May 2021.	324,000	482,000
Equipment lease-purchase agreement with GE Healthcare Financial Services with monthly payments of \$9,632 at 1.50% through May 2021.	77,000	189,000
Equipment lease-purchase agreement with GE Healthcare Financial Services with monthly payments of \$7,778 at 1.50% through May 2021.	62,000	154,000
Equipment lease-purchase agreement with GE Healthcare Financial Services with monthly payments of \$5,574 at 6.73% through March 2021.	136,000	192,000
Equipment lease-purchase agreement with GE Healthcare Financial Services with monthly payments of \$2,022 at 1.50% through May 2021.	14,000	36,000
Equipment lease-purchase agreement with GE Healthcare Financial Services with monthly payments of \$1,707 at 1.50% through September 2021.	20,000	40,000
Equipment lease-purchase agreement with Huntington Financial Services with monthly payments of \$7,175 at 1.62% through August 2024.	<u>345,000</u>	-
Total capital lease obligations	4,785,000	4,992,000
Less current portion	(733,000)	(605,000)
Capital lease obligations, net of current portion	<u>\$ 4,052,000</u>	<u>\$ 4,387,000</u>

Sky Lakes Medical Center and Affiliates
Notes to Consolidated Financial Statements

Note 9 – Capital Leases (continued)

Scheduled payments on capital lease obligations for the years ending September 30 are as follows:

2021	\$ 1,113,000
2022	521,000
2023	521,000
2024	521,000
2025	457,000
Thereafter	<u>5,223,000</u>
Total minimum lease payments	8,356,000
Less amount representing interest	<u>(3,571,000)</u>
Present value of net minimum lease payments	<u><u>\$ 4,785,000</u></u>

Note 10 – Long-Term Debt

Long term debt consisted of the following as of September 30:

	2020	2019
Series 2016 Bonds with interest rates from 2% to 5% and mature in varying amounts through 2046, net of premiums of \$5,003,505 and \$5,195,948 at September 30, 2020 and 2019, respectively.	\$ 53,709,000	\$ 54,866,000
Series 2012 Bonds with interest rates from 3.5% to 5% and mature in varying amounts through 2031, net of premiums of \$817,018 and \$891,292 at September 30, 2020 and 2019, respectively.	10,237,000	11,631,000
Bank of America Loan with a fixed interest rate of 3.9%, due and payable July 2025.	5,393,000	6,388,000
Bank of America Loan with a fixed interest rate of 2.7%, due and payable September 2026.	<u>4,342,000</u>	<u>5,000,000</u>
Total long-term debt	73,681,000	77,885,000
Less deferred financing costs	(1,006,000)	(1,059,000)
Less current portion	<u>(4,100,000)</u>	<u>(3,882,000)</u>
Long-term debt, net of deferred financing costs and current portion	<u><u>\$ 68,575,000</u></u>	<u><u>\$ 72,944,000</u></u>

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 10 – Long-Term Debt (continued)

2016 Bonds – In 2016, the Authority issued \$53,325,000 in Series 2016 Bonds to defease the remaining 2006 Bonds, to pay or to reimburse the Medical Center for capital expenditures, to fund a Reserve Fund for the 2016 Bonds, and to pay costs of issuing the 2016 Bonds. The issuance was structured as a legal defeasance. Adequate amounts of the 2016 Bond issuance were used to purchase U.S. Treasury Securities to fully pay the debt service requirements of the 2006 Bonds. The securities have been placed in an escrow account and the Escrow Agent for the account will pay the debt service requirements as they become due. As the debt for the 2006 Series has been legally defeased, the Medical Center is no longer required to report the liability in the consolidated balance sheet.

The 2016 Bonds are secured by a Deed of Trust on a portion of the Medical Center campus, including the main hospital facility.

2012 Bonds – In 2013, the Authority issued \$17,000,000 in Series 2012 Bonds to defease the remaining 2002 Bonds, to pay or to reimburse the Medical Center for the payment of new equipment, to fund a Reserve Fund for the 2012 Bonds, and to pay costs of issuing the 2012 Bonds. The issuance was structured as a legal defeasance. Adequate amounts of the 2012 Bond issuance were used to purchase U.S. Treasury Securities to fully pay the debt service requirements of the 2002 Bonds. The securities have been placed in an escrow account and the Escrow Agent for the account will pay the debt service requirements as they become due. As the debt for the 2002 Series has been legally defeased, the Medical Center is no longer required to report the liability in the consolidated balance sheet.

The 2012 Bonds are secured by a Deed of Trust on a portion of the Medical Center campus, including the main hospital facility. They are further secured by a Reserve Fund, created by the terms of the Bond Indenture to be held by the Bond Trustee (Note 4) to prevent a payment default on the Bonds. The Reserve Fund is required to maintain a balance equal to the lesser of the maximum annual debt service, 125% of the average annual debt service, or 10% of the bond proceeds. They are also secured by a pledge of the gross revenues.

2018 Loans – In 2018, the Medical Center entered into an Equipment Security Note with the Bank of America for \$7,500,000 for various medical equipment and tenant improvements.

2019 Loans – In 2019, the Medical Center entered into an Equipment Security Note with the Bank of America for \$5,000,000 for various medical equipment and tenant improvements.

The Medical Center must satisfy certain covenants as long as the bonds are outstanding. At September 30, 2020, management is not aware of any violation of the covenants.

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 10 – Long-Term Debt (continued)

Scheduled future principal payments and amortization of premiums for all long-term debt for the years ending September 30 are as follows:

2021	\$ 4,365,000
2022	4,535,000
2023	4,271,000
2024	4,450,000
2025	4,397,000
Thereafter	<u>51,663,000</u>
	<u><u>\$ 73,681,000</u></u>

Deferred financing costs incurred and bond premium received in connection with the issuance of the refunding gross revenue bonds are being amortized over the term of the bond issue by the straight-line method, which approximates the effective interest rate method.

Note 11 – Advance and Refund Liabilities

Provider Relief Funds (PRF) – On March 27, 2020, the United States Congress passed the Coronavirus Aid, Relief, and Economic Securities (CARES) Act. The CARES Act included provisions for health care under the Provider Relief Fund. During April and May 2020, the Medical Center received funds under the Provider Relief Fund, administered by the U.S. Department of Health & Human Services (HHS) of \$20,168,000. The Medical Center was required to and did timely sign attestations agreeing to the terms and conditions of payment. Those terms and conditions include measures to prevent fraud and misuse. Documentation is required to ensure that these funds are to be used for healthcare-related expenses or lost revenue attributable to COVID-19, limitations of out of pocket payments from certain patients, and the acceptance of several other reporting and compliance requirements. It is noted that anti-fraud monitoring and auditing will be performed by HHS and the Office of the Inspector General. The Medical Center's management is currently determining its ability to comply with these terms and conditions. For the year ended September 30, 2020, the Medical Center has recorded \$600,000 as current refund liability. For the year ended September 30, 2020, the Medical Center recognized \$20,168,000 of Provider Relief Funds on its statement of operations included other revenue.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 11 – Advance and Refund Liabilities (continued)

Medicare advance payments – The passage of the CARES Act amended the existing CMS Accelerated Payments Program to provide additional benefits and flexibilities, including extended repayment timeframes, to the subset of providers specifically referenced in the CARES Act, including inpatient hospitals, children's hospitals, certain cancer hospitals, and critical access hospitals. During April 2020, the Medical Center received funds under the Accelerated Payments Program, administered by NORDIAN Medicare of \$32,442,000. Repayment is delayed until one year after payment was issued. After the first year, Medicare will automatically recoup 25 percent of Medicare payments other owed to the provider or supplier for eleven months. At the end of the eleven-month period, recoupment will increase to 50 percent for another six months. If the provider or supplier is unable to repay the total amount of the Accelerated and Advance Payment during this time period (a total of 29 months), CMS will issue letters requiring repayment of any outstanding balance, subject to an interest rate of four percent. For the year ended September 30, 2020, the Medical Center has recorded \$8,111,000 as current advance and refund liability. The remaining \$24,331,000 is included in advance liability, net of current amounts.

Note 12 – Net Assets with Donor Restrictions

Net assets with donor restrictions are available for the following purposes at September 30:

	<u>2020</u>	<u>2019</u>
Cancer fund	\$ 3,051,000	\$ 2,709,000
Cares fund	1,141,000	1,025,000
Other funds	2,022,000	2,062,000
 Total net assets with donor restrictions	 <u>\$ 6,214,000</u>	 <u>\$ 5,796,000</u>

Note 13 – Commitments and Contingencies

Operating leases

Lessee leases – The Medical Center leases equipment and facilities under operating leases which expire through July 2023. Total rental expense for all operating leases in the fiscal years ending September 30, 2020 and 2019 was approximately \$1,416,000 and \$1,395,000, respectively.

Minimum future payments on non-cancelable leases as of September 30 are:

2021	\$ 441,000
2022	327,000
2023	30,000
Thereafter	-
	 <u>\$ 798,000</u>

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 13 – Commitments and Contingencies (continued)

Lessor leases – The Medical Center is the lessor of the office space to various entities under operating leases expiring in various years through September 2057.

Following is a summary of property on or held for lease at September 30:

	<u>2020</u>	<u>2019</u>
Buildings and improvements	\$ 8,656,000	\$ 9,618,000
Less accumulated depreciation	<u>(6,753,000)</u>	<u>(6,535,000)</u>
	<u><u>\$ 1,903,000</u></u>	<u><u>\$ 3,083,000</u></u>

Minimum future rentals to be received on non-cancelable leases as of September 30 are:

2021	\$ 291,000
2022	236,000
2023	138,000
2024	47,000
2025	6,000

Litigation

The Medical Center is involved in litigation and regulatory investigations arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the Medical Center's future financial position or results from operations.

Note 14 – Risks and Uncertainties

On March 11, 2020, the World Health Organization officially declared COVID-19, the disease caused by the novel coronavirus, a pandemic. Management is closely monitoring the evolution of this pandemic, including how it may affect the economy and general population. The pandemic did impact the Medical Center's revenue in the initial months as a result of a restriction of elective services by the State of Oregon. The Medical Center was able to restore and provide most services by year-end. Management has not yet determined the full financial impact of these events.

The Medical Center's management has been closely monitoring the impact of COVID-19 on the Medical Center's operations, including the impact on its patients and employees. The duration and intensity of the pandemic is uncertain but may influence patient decisions, donor decisions, and may also negatively impact collections of the Medical Center's receivables.

As a result of the pandemic, the Medical Center received federal funds as described in Note 11.

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 15 – Related-Party Transactions

The following is a summary of transactions between the Medical Center and related parties:

Atrio Health Plans – The Medical Center received \$16,962,000 and \$14,039,000 in Medicare reimbursement from Atrio Health Plans, Inc. in fiscal year 2020 and 2019, respectively.

Southern Oregon Linen Services – The Medical Center purchased laundry services of approximately \$503,000 and \$505,000 from Southern Oregon Linen Services in fiscal years 2020 and 2019, respectively.

Cascade Comprehensive Care, Inc. – The Medical Center received approximately \$34,685,000 and \$32,642,000 in Medicaid reimbursements from CCC in fiscal years 2020 and 2019, respectively.

Note 16 – Liquidity and Availability

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the statement of financial position date, comprise the following as of September 30:

	<u>2020</u>	<u>2019</u>
Cash and cash equivalents	\$ 71,123,000	\$ 18,221,000
Certificates of deposit	-	6,452,000
Patient accounts receivable, net	29,182,000	28,812,000
Other receivables	5,883,000	6,060,000
Risk pool withhold receivable	<u>5,154,000</u>	<u>7,269,000</u>
 Total	 <u>\$ 111,342,000</u>	 <u>\$ 66,814,000</u>

The Medical Center has established an operating reserve and reviews its funding level on an ongoing basis to ensure it is adequate. The Medical Center invests cash in excess of daily requirements in U.S. government securities and other short-term investments, certificates of deposit, and money market funds.

Due to the uncertainty of the pandemic and the need to refund the advanced payment of Provider Relief Funds, the Medical Center increased the amount of cash on hand as a precaution.

Sky Lakes Medical Center and Affiliates
Notes to Consolidated Financial Statements

Note 17 – Functional Expenses

The Medical Center provides general health care services to residents within its geographic location. Expenses related to providing these services for the Medical Center for the year ended September 30, 2020 are as follows:

	Program Activities	Supporting Activities		Total Expenses
	Healthcare Services	Management and General		
Salaries and benefits	\$ 110,728,000	\$ 18,650,000	\$ 129,378,000	
Purchased services	26,236,000	2,134,000	28,370,000	
Supplies	17,520,000	116,000	17,636,000	
Drugs	18,617,000	-	18,617,000	
Depreciation and amortization	7,549,000	5,125,000	12,674,000	
Building and maintenance	4,069,000	10,776,000	14,845,000	
Provider tax	12,074,000	-	12,074,000	
Physician fees	8,629,000	17,000	8,646,000	
Interest expense	10,000	2,885,000	2,895,000	
Minor equipment	928,000	515,000	1,443,000	
Professional fees	42,000	1,394,000	1,436,000	
Rentals	1,172,000	244,000	1,416,000	
Insurance	591,000	1,307,000	1,898,000	
Other	1,372,000	2,130,000	3,502,000	
 Total	 \$ 209,537,000	 \$ 45,293,000	 \$ 254,830,000	

Expenses related to providing these services for the Medical Center for the year ended September 30, 2019 are as follows:

	Program Activities	Supporting Activities		Total Expenses
	Healthcare Services	Management and General		
Salaries and benefits	\$ 107,222,000	\$ 16,995,000	\$ 124,217,000	
Purchased services	29,580,000	2,922,000	32,502,000	
Supplies	17,846,000	73,000	17,919,000	
Drugs	19,844,000	-	19,844,000	
Depreciation and amortization	10,727,000	342,000	11,069,000	
Building and maintenance	3,457,000	11,993,000	15,450,000	
Provider tax	13,512,000	-	13,512,000	
Physician fees	7,910,000	19,000	7,929,000	
Interest expense	3,133,000	81,000	3,214,000	
Other	6,062,000	5,565,000	11,627,000	
 Total	 \$ 219,293,000	 \$ 37,990,000	 \$ 257,283,000	

Sky Lakes Medical Center and Affiliates

Notes to Consolidated Financial Statements

Note 17 – Functional Expenses (continued)

The consolidated financial statements report certain categories of expenses that are attributed to more than one program or supporting function. Therefore, expenses require allocation on a reasonable basis that is consistently applied. The Medical Center allocates expenses on the basis of estimates of time and effort.

Note 18 – Retirement Plans

401(a) – Money Purchase Pension Plan

The Medical Center has established a defined contribution retirement plan for all employees who have at least one year of service, are age 21 or older, and have completed 1,000 hours of service in the plan year. The Medical Center is required to contribute 5% of an employee's eligible compensation to the plan each plan year. The Medical Center accrued \$-0- and \$3,133,000 to the plan on behalf of employees for fiscal years ended September 30, 2020 and 2019, respectively, which was included in other accrued expenses in the consolidated balance sheets.

In May 2018, the Medical Center's Board of Directors decided to terminate this plan and offer the employees the opportunity to participate in the Medical Center 401(k) plan instead. The Medical Center will shift the 5% contribution to the 401(k) plan effective October 1, 2019. As part of the termination, participants will have their balances in this plan rolled into the Medical Center 401(k) plan in 2020.

403(b) – Elective Deferral Plan

The Medical Center has established a 403(b) retirement plan covering substantially all employees under the guidelines of Internal Revenue Code 403(b) Tax Deferred Annuity Plan. The employees may elect to contribute, according to a salary reduction agreement, a percentage of their annual compensation and are eligible for the plan on the first day of employment with the Medical Center. The Plan is a 'Custodial Account Plan' invested in mutual funds.

In May 2018, the Medical Center's Board of Directors decided to terminate this plan and offer the employees the opportunity to participate in the Medical Center 401(k) plan instead. During 2019, most participants rolled their balances into the 401(k) plan and the plan was terminated.

401(k) – Retirement Plan

WPS established the West Physician Services 401(k) Retirement Plan, which is a qualified retirement plan under Section 401(k) of the Internal Revenue Code. Effective January 1, 2019, the Plan was modified to include the Medical Center employees. The Medical Center matched one-third of a percent per 1% of the employee's contribution up to a maximum Medical Center contribution of 1%, except for WPS and supplemental employees. Effective October 1, 2019, the Medical Center began making bi-weekly required contributions of 5% of an employee's eligible compensation to the plan each plan year. The Medical Center made non-discretionary matching employer contributions of \$5,267,000 and \$586,000 for the years ended September 30, 2020 and 2019, respectively.

Sky Lakes Medical Center and Affiliates **Notes to Consolidated Financial Statements**

Note 18 – Retirement Plans (continued)

409(a) – Retirement Plan

WPS established the West Physician Services Nonqualified Retirement Plan, for the purposes of providing nonqualified retirement benefits to a select group of its employees. The Medical Center is required to contribute 5% of an employee's compensation to the plan each plan year. In addition, the plan permits eligible employees to defer a portion of their compensation. The participant balances are distributable in cash after retirement or termination of employment. The Medical Center contributed \$191,000 and \$147,000 to the plan on behalf of employees for fiscal years ended September 30, 2020 and 2019, respectively.

457(b) – Deferred Compensation Plan

The Medical Center established the Sky Lakes Medical Center 457(b) Plan. The Plan is a 457(b) qualified deferred compensation plan that permits eligible employees to defer a portion of their compensation. The participant balances are distributable in cash after retirement, unforeseeable emergencies, or termination of employment. Employer contributions to the plan approximated \$69,000 and \$66,000 for the years ended September 30, 2020 and 2019, respectively. The Medical Center may hold the participant balances in cash or invest it in assets selected by the Plan Administrator. The Plan Administrator has elected to invest the participant balances in mutual funds.

Note 19 – Subsequent events

Cyber security

Health care providers and insurers are highly dependent upon integrated electronic medical record and other information systems to deliver high quality, coordinated and cost-effective care. These systems necessarily hold large quantities of highly sensitive protected health information. As a result, the electronic systems and networks of health care providers are considered likely targets for cyberattacks and other potential breaches of their systems. In addition to regulatory fines and penalties, health care entities subject to breaches may be liable for the costs of remediating the breaches, damages to individuals (or classes) whose information has been breached, reputational damage and business loss, and damage to the information technology infrastructure.

The Medical Center has taken and continues to take measures to protect its information technology system against such cyberattacks, but there can be no assurance that the Medical Center will not experience a significant breach. The Medical Center was subject to a ransomware attack on October 27, 2020. The Medical Center was able to restore its core clinical systems within three weeks of the attack and minimized the impact on patient services, primarily with a partial reduction on some elective and outpatient services. The Medical Center is also expected to replace about 2,000 computers and purchase new information technology servers, incurred additional labor expenses during and subsequent to the attack and encountered delays in access to e-mail and billing systems as a result. Management is unable to estimate the full cost of this attack at this time. The Medical Center is currently assessing whether any information was compromised and accessed by the third parties. The impact of the ransomware attack is not expected to have a material impact on the Medical Center.

Supplementary Information

Sky Lakes Medical Center and Affiliates
Consolidating Balance Sheet
September 30, 2020

ASSETS								
	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Klamath Medical Business Center	KW Campus	Total	Eliminating Entries	Consolidated	
CURRENT ASSETS								
Cash and cash equivalents	\$ 70,321,000	\$ 529,000	\$ 578,000	\$ 21,000	\$ 71,449,000	\$ -	\$ 71,449,000	
Certificates of deposit	419,000	-	-	-	419,000	-	419,000	
Patient accounts receivable, net	29,182,000	-	-	-	29,182,000	-	29,182,000	
Other receivables	8,648,000	-	-	-	8,648,000	(2,765,000)	5,883,000	
Risk pool withhold receivable	5,154,000	-	-	-	5,154,000	-	5,154,000	
Supplies inventories	6,366,000	-	-	-	6,366,000	-	6,366,000	
Prepaid expenses	3,652,000	-	-	-	3,652,000	-	3,652,000	
Promises to give, current portion	-	750,000	-	-	750,000	-	750,000	
Total current assets	<u>123,742,000</u>	<u>1,279,000</u>	<u>578,000</u>	<u>21,000</u>	<u>125,620,000</u>	<u>(2,765,000)</u>	<u>122,855,000</u>	
ASSETS LIMITED AS TO USE	1,578,000	-	-	-	1,578,000	-	1,578,000	
PROPERTY AND EQUIPMENT, net	139,512,000	-	664,000	1,495,000	141,671,000	-	141,671,000	
INVESTMENTS	152,657,000	19,756,000	-	-	172,413,000	(1,532,000)	170,881,000	
OTHER ASSETS	1,133,000	-	-	-	1,133,000	(10,000)	1,123,000	
Total assets	<u>\$ 418,622,000</u>	<u>\$ 21,035,000</u>	<u>\$ 1,242,000</u>	<u>\$ 1,516,000</u>	<u>\$ 442,415,000</u>	<u>\$ (4,307,000)</u>	<u>\$ 438,108,000</u>	

Sky Lakes Medical Center and Affiliates
Consolidating Balance Sheet
September 30, 2020

LIABILITIES AND NET ASSETS										
	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Klamath Medical Business Center	KW Campus	Total	Eliminating Entries	Consolidated			
CURRENT LIABILITIES										
Accounts payable	\$ 6,185,000	\$ 137,000	\$ -	\$ -	\$ 6,322,000	\$ (28,000)	\$ 6,294,000			
Accrued payroll	10,416,000	-	-	-	10,416,000	-	-	10,416,000		
Accrued compensated absences	5,791,000	-	-	-	5,791,000	-	-	5,791,000		
Accrued interest payable	258,000	-	-	-	258,000	-	-	258,000		
Other accrued expenses	14,568,000	-	-	-	14,568,000	(2,747,000)	(2,747,000)	11,821,000		
Estimated third-party payor settlements	2,667,000	-	-	-	2,667,000	-	-	2,667,000		
Current advance and refund liabilities	8,111,000	-	-	-	8,111,000	-	-	8,111,000		
Capital lease obligations, current portion	733,000	-	-	-	733,000	-	-	733,000		
Long-term debt, current portion	4,100,000	-	-	-	4,100,000	-	-	4,100,000		
Total current liabilities	52,829,000	137,000	-	-	52,966,000	(2,775,000)	50,191,000			
LONG-TERM LIABILITIES										
Capital lease obligations, net of current portion	4,052,000	-	-	-	4,052,000	-	-	4,052,000		
Long-term debt, net of current portion and deferred financing costs	68,575,000	-	-	-	68,575,000	-	-	68,575,000		
Advance and refund liabilities, net of current portion	24,331,000	-	-	-	24,331,000	-	-	24,331,000		
Other long-term liabilities	7,143,000	-	-	-	7,143,000	-	-	7,143,000		
Total long-term liabilities	104,101,000	-	-	-	104,101,000	-	-	104,101,000		
Total liabilities	156,930,000	137,000	-	-	157,067,000	(2,775,000)	154,292,000			
NET ASSETS										
Without donor restrictions – Sky Lakes Medical Center	261,692,000	14,684,000	1,242,000	1,516,000	279,134,000	(2,911,000)	276,223,000			
Without donor restrictions – non-controlling interest	-	-	-	-	-	1,379,000	1,379,000			
With donor restrictions	-	6,214,000	-	-	6,214,000	-	-	6,214,000		
Total net assets	261,692,000	20,898,000	1,242,000	1,516,000	285,348,000	(1,532,000)	283,816,000			
Total liabilities and net assets	\$ 418,622,000	\$ 21,035,000	\$ 1,242,000	\$ 1,516,000	\$ 442,415,000	\$ (4,307,000)	\$ 438,108,000			

Sky Lakes Medical Center and Affiliates
Consolidating Statement of Operations
For the Year Ended September 30, 2020

	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Klamath Medical Business Center	KW Campus	Total	Eliminating Entries	Consolidated
REVENUES							
Patient service revenue, net contractual adjustments	\$ 242,137,000	\$ -	\$ -	\$ -	\$ 242,137,000	\$ -	\$ 242,137,000
Provision for bad debts	<u>(7,291,000)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(7,291,000)</u>	<u>-</u>	<u>(7,291,000)</u>
Net patient service revenue	234,846,000	-	-	-	234,846,000	-	234,846,000
Other revenue	30,426,000	-	299,000	-	30,725,000	(794,000)	29,931,000
Total revenues	265,272,000	-	299,000	-	265,571,000	(794,000)	264,777,000
EXPENSES							
Salaries and benefits	129,172,000	206,000	-	-	129,378,000	-	129,378,000
Purchased services	28,396,000	-	5,000	-	28,401,000	(31,000)	28,370,000
Supplies	18,095,000	-	-	-	18,095,000	(459,000)	17,636,000
Drugs	18,623,000	-	-	-	18,623,000	(6,000)	18,617,000
Depreciation and amortization	12,635,000	-	39,000	-	12,674,000	-	12,674,000
Building and maintenance	14,764,000	-	93,000	-	14,857,000	(12,000)	14,845,000
Provider tax	12,074,000	-	-	-	12,074,000	-	12,074,000
Physician fees	8,650,000	-	-	-	8,650,000	(4,000)	8,646,000
Interest expense	2,895,000	-	-	-	2,895,000	-	2,895,000
Professional fees	1,459,000	-	9,000	(24,000)	1,444,000	(8,000)	1,436,000
Rentals and lease expense	1,416,000	-	-	-	1,416,000	-	1,416,000
Insurance	1,893,000	-	5,000	-	1,898,000	-	1,898,000
Minor equipment	1,443,000	-	-	-	1,443,000	-	1,443,000
Other	3,502,000	-	20,000	-	3,522,000	(20,000)	3,502,000
Total expenses	255,017,000	206,000	171,000	(24,000)	255,370,000	(540,000)	254,830,000
OPERATING INCOME (LOSS)	10,255,000	(206,000)	128,000	24,000	10,201,000	(254,000)	9,947,000
OTHER INCOME (EXPENSE)							
Investment income	5,364,000	966,000	-	-	6,330,000	-	6,330,000
Contributions	1,960,000	74,000	-	-	2,034,000	(1,360,000)	674,000
Net assets released from restriction	-	1,477,000	-	-	1,477,000	-	1,477,000
Other non-operating income (expense)	43,000	(2,656,000)	-	-	(2,613,000)	1,493,000	(1,120,000)
Total other income, net	7,367,000	(139,000)	-	-	7,228,000	133,000	7,361,000
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	\$ 17,622,000	\$ (345,000)	\$ 128,000	\$ 24,000	\$ 17,429,000	\$ (121,000)	\$ 17,308,000

Sky Lakes Medical Center and Affiliates
Consolidating Statement of Changes in Net Assets
For the Year Ended September 30, 2020

	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Klamath Medical Business Center	KW Campus	Total	Eliminating Entries	Consolidated
NET ASSETS WITHOUT DONOR RESTRICTIONS							
Excess (deficiency) of revenues over expenses	\$ 17,622,000	\$ (345,000)	\$ 128,000	\$ 24,000	\$ 17,429,000	\$ (121,000)	\$ 17,308,000
Contributions	-	-	13,000	49,000	62,000	-	62,000
Net change in unrealized gains and losses on other-than-trading securities	377,000	607,000	-	-	984,000	-	984,000
Increase (decrease) in net assets without donor restrictions	<u>17,999,000</u>	<u>262,000</u>	<u>141,000</u>	<u>73,000</u>	<u>18,475,000</u>	<u>(121,000)</u>	<u>18,354,000</u>
NET ASSETS WITH DONOR RESTRICTIONS							
Contributions	-	1,335,000	-	-	1,335,000	-	1,335,000
Net change in unrealized gains and losses on other-than-trading securities	-	245,000	-	-	245,000	-	245,000
Investment income	-	315,000	-	-	315,000	-	315,000
Net assets released from restrictions	-	(1,477,000)	-	-	(1,477,000)	-	(1,477,000)
Decrease in net assets with donor restrictions	-	418,000	-	-	418,000	-	418,000
CHANGE IN NET ASSETS	17,999,000	680,000	141,000	73,000	18,893,000	(121,000)	18,772,000
NET ASSETS, beginning of year	<u>243,693,000</u>	<u>20,218,000</u>	<u>\$1,101,000</u>	<u>\$1,443,000</u>	<u>266,455,000</u>	<u>(\$1,411,000)</u>	<u>265,044,000</u>
NET ASSETS, end of year	<u>\$ 261,692,000</u>	<u>\$ 20,898,000</u>	<u>\$ 1,242,000</u>	<u>\$ 1,516,000</u>	<u>\$ 285,348,000</u>	<u>\$ (1,532,000)</u>	<u>\$ 283,816,000</u>

Sky Lakes Medical Center and Affiliates – Obligated Group
Combining Balance Sheet
September 30, 2020

ASSETS						Total Obligated Group
	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Total	Eliminating Entries		
CURRENT ASSETS						
Cash and cash equivalents	\$ 70,321,000	\$ 529,000	\$ 70,850,000	\$ -	\$ 70,850,000	
Certificates of deposit	419,000	-	419,000	-	419,000	
Patient accounts receivable, net	29,182,000	-	29,182,000	-	29,182,000	
Other receivables	8,648,000	-	8,648,000	(2,765,000)	5,883,000	
Risk pool withhold receivable	5,154,000	-	5,154,000	-	5,154,000	
Supplies inventories	6,366,000	-	6,366,000	-	6,366,000	
Prepaid expenses	3,652,000	-	3,652,000	-	3,652,000	
Promises to give, current portion	-	750,000	750,000	-	750,000	
 Total current assets	 123,742,000	 1,279,000	 125,021,000	 (2,765,000)	 122,256,000	
ASSETS LIMITED AS TO USE	1,578,000	-	1,578,000	-	1,578,000	
PROPERTY AND EQUIPMENT, net	139,512,000	-	139,512,000	-	139,512,000	
INVESTMENTS	152,657,000	19,756,000	172,413,000	(194,000)	172,219,000	
OTHER ASSETS	1,133,000	-	1,133,000	-	1,133,000	
 Total assets	 \$ 418,622,000	 \$ 21,035,000	 \$ 439,657,000	 \$ (2,959,000)	 \$ 436,698,000	

Sky Lakes Medical Center and Affiliates – Obligated Group
Combining Balance Sheet
September 30, 2020

LIABILITIES AND NET ASSETS						
	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Total	Eliminating Entries	Total Obligated Group	
CURRENT LIABILITIES						
Accounts payable	\$ 6,185,000	\$ 137,000	\$ 6,322,000	\$ (28,000)	\$ 6,294,000	
Accrued payroll	10,416,000	-	10,416,000	-	10,416,000	
Accrued compensated absences	5,791,000	-	5,791,000	-	5,791,000	
Accrued interest payable	258,000	-	258,000	-	258,000	
Other accrued expenses	14,568,000	-	14,568,000	(2,747,000)	11,821,000	
Estimated third-party payor settlements	2,667,000	-	2,667,000	-	2,667,000	
Current advance and refund liabilities	8,111,000	-	8,111,000	-	8,111,000	
Capital lease obligations, current portion	733,000	-	733,000	-	733,000	
Long-term debt, current portion	4,100,000	-	4,100,000	-	4,100,000	
 Total current liabilities	 52,829,000	 137,000	 52,966,000	 (2,775,000)	 50,191,000	
LONG-TERM LIABILITIES						
Capital lease obligations, net of current portion	4,052,000	-	4,052,000	-	4,052,000	
Long-term debt, net of current portion and deferred financing costs	68,575,000	-	68,575,000	-	68,575,000	
Advance and refund liabilities, net of current portion	24,331,000	-	24,331,000	-	24,331,000	
Other long-term liabilities	7,143,000	-	7,143,000	-	7,143,000	
 Total long-term liabilities	 104,101,000	 -	 104,101,000	 -	 104,101,000	
 Total liabilities	 156,930,000	 137,000	 157,067,000	 (2,775,000)	 154,292,000	
NET ASSETS						
Without donor restrictions – Sky Lakes Medical Center	261,692,000	14,684,000	276,376,000	(184,000)	276,192,000	
With donor restrictions	-	6,214,000	6,214,000	-	6,214,000	
 Total net assets	 261,692,000	 20,898,000	 282,590,000	 (184,000)	 282,406,000	
 Total liabilities and net assets	 \$ 418,622,000	 \$ 21,035,000	 \$ 439,657,000	 \$ (2,959,000)	 \$ 436,698,000	

Sky Lakes Medical Center and Affiliates – Obligated Group
Combining Statement of Operations
For the Year Ended September 30, 2020

	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Total	Eliminating Entries	Total Obligated Group
REVENUES					
Patient service revenue, net contractual adjustments	\$ 242,137,000	\$ -	\$ 242,137,000	\$ -	\$ 242,137,000
Provision for bad debts	(7,291,000)	-	(7,291,000)	-	(7,291,000)
Net patient service revenue	234,846,000	-	234,846,000	-	234,846,000
Other revenue	30,426,000	-	30,426,000	(786,000)	29,640,000
Total revenues	265,272,000	-	265,272,000	(786,000)	264,486,000
EXPENSES					
Salaries and benefits	129,172,000	206,000	129,378,000	-	129,378,000
Purchased services	28,396,000	-	28,396,000	(31,000)	28,365,000
Supplies	18,095,000	-	18,095,000	(510,000)	17,585,000
Drugs	18,623,000	-	18,623,000	(6,000)	18,617,000
Depreciation and amortization	12,635,000	-	12,635,000	-	12,635,000
Building and maintenance	12,074,000	-	12,074,000	(12,000)	12,062,000
Provider tax	14,764,000	-	14,764,000	-	14,764,000
Physician fees	8,650,000	-	8,650,000	(4,000)	8,646,000
Interest expense	2,895,000	-	2,895,000	-	2,895,000
Professional fees	1,893,000	-	1,893,000	-	1,893,000
Rentals and lease expense	1,416,000	-	1,416,000	-	1,416,000
Insurance	1,459,000	-	1,459,000	-	1,459,000
Minor equipment	1,443,000	-	1,443,000	-	1,443,000
Other	3,502,000	-	3,502,000	(20,000)	3,482,000
Total expenses	255,017,000	206,000	255,223,000	(583,000)	254,640,000
OPERATING INCOME (LOSS)	10,255,000	(206,000)	10,049,000	(203,000)	9,846,000
OTHER INCOME (EXPENSE)					
Investment income	5,364,000	966,000	6,330,000	-	6,330,000
Contributions	1,960,000	74,000	2,034,000	-	2,034,000
Net assets released from restriction	-	1,477,000	1,477,000	-	1,477,000
Other non-operating income (expense)	43,000	(2,656,000)	(2,613,000)	(2,163,000)	(4,776,000)
Total other income, net	7,367,000	(139,000)	7,228,000	(2,163,000)	5,065,000
EXCESS (DEFICIENCY) OF REVENUE OVER EXPENSES	\$ 17,622,000	\$ (345,000)	\$ 17,277,000	\$ (2,366,000)	\$ 14,911,000

Sky Lakes Medical Center and Affiliates – Obligated Group
Combining Statement of Changes in Net Assets
For the Year Ended September 30, 2020

	Sky Lakes Medical Center	Sky Lakes Medical Center Foundation	Total	Eliminating Entries	Total Obligated Group
NET ASSETS WITHOUT DONOR RESTRICTIONS					
Excess (deficiency) of revenues over expenses	\$ 17,622,000	\$ (345,000)	\$ 17,277,000	\$ (2,366,000)	\$ 14,911,000
Net change in unrealized gains and losses on other-than-trading securities	377,000	607,000	984,000	-	984,000
Increase (decrease) in net assets without donor restrictions	17,999,000	262,000	18,261,000	(2,366,000)	15,895,000
NET ASSETS WITH DONOR RESTRICTIONS					
Contributions	-	1,335,000	1,335,000	-	1,335,000
Net change in unrealized gains and losses on other-than-trading securities	-	245,000	245,000	-	245,000
Investment income	-	315,000	315,000	-	315,000
Net assets released from restrictions	-	(1,477,000)	(1,477,000)	-	(1,477,000)
Decrease in net assets with donor restrictions	-	418,000	418,000	-	418,000
CHANGE IN NET ASSETS	17,999,000	680,000	18,679,000	(2,366,000)	16,313,000
NET ASSETS, beginning of year	243,693,000	20,218,000	263,911,000	-	263,911,000
NET ASSETS, end of year	<u>\$ 261,692,000</u>	<u>\$ 20,898,000</u>	<u>\$ 282,590,000</u>	<u>\$ (2,366,000)</u>	<u>\$ 280,224,000</u>

