



SALEM HEALTH HOSPITALS AND CLINICS

Consolidated Financial Statements and Supplemental Schedules

June 30, 2023 and 2022

(With Independent Auditors' Report Thereon)

SALEM HEALTH HOSPITALS AND CLINICS

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KPMG LLP
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Independent Auditors' Report

The Board of Trustees
Salem Health Hospitals and Clinics:

Opinion

We have audited the consolidated financial statements of Salem Health Hospitals and Clinics and its subsidiaries (the Corporation), which comprise the consolidated balance sheets as of June 30, 2023 and 2022, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as of June 30, 2023 and 2022, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are required to be independent of the Corporation and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with U.S. generally accepted accounting principles, and for 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.

In preparing the consolidated financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Corporation's ability to continue as a going concern for one year after the date that the consolidated financial statements are issued.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the consolidated financial statements.



In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Corporation's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the consolidated financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Corporation's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplemental information included in the consolidating schedule of balance sheet information and consolidating schedule of operations information is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with GAAS. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

The lean initiatives footnote included in note 15 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information has not been subject to the auditing procedures applied in the audit of the consolidated financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

KPMG LLP

Portland, Oregon
October 6, 2023

SALEM HEALTH HOSPITALS AND CLINICS

Consolidated Balance Sheets

June 30, 2023 and 2022

(In thousands)

Assets	2023	2022
Current assets:		
Cash and cash equivalents	\$ 44,092	18,568
Patient accounts receivable, net	132,812	128,264
Other receivables	33,439	17,641
Supplies inventory	10,552	11,513
Prepaid expenses and other	15,602	16,948
Total current assets	236,497	192,934
Investments	878,862	917,583
Property and equipment, net	717,705	671,915
Rental and other property held for future development, net of accumulated depreciation of \$5,718 in 2023 and \$5,492 in 2022	38,876	54,685
Investments in health related entities	28,994	27,696
Other noncurrent assets	23,325	26,734
Total assets	\$ 1,924,259	1,891,547
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	\$ 67,053	72,932
Accrued liabilities:		
Payroll, payroll taxes, and withholdings	21,245	15,981
Paid time off	29,526	28,760
Other	19,067	18,847
Estimated third-party payor settlements, net	11,798	7,423
Current portion of long-term debt	12,599	12,215
Current portion of estimated professional liability	2,399	2,245
Total current liabilities	163,687	158,403
Long-term debt, net of current portion	472,222	484,766
Accrued postretirement healthcare benefits	—	2,001
Other long-term liabilities	9,670	6,348
Estimated professional liability, net of current portion	10,958	7,853
Total liabilities	656,537	659,371
Net assets:		
Without donor restrictions	1,257,519	1,222,523
With donor restrictions	10,203	9,653
Total net assets	1,267,722	1,232,176
Total liabilities and net assets	\$ 1,924,259	1,891,547

See accompanying notes to consolidated financial statements.

SALEM HEALTH HOSPITALS AND CLINICS

Consolidated Statements of Operations

Years ended June 30, 2023 and 2022

(In thousands)

	<u>2023</u>	<u>2022</u>
Operating revenue:		
Patient service revenue	\$ 1,027,399	965,254
Other revenue	48,927	51,502
Net assets released from donor restriction used for operations	317	299
Total operating revenue	<u>1,076,643</u>	<u>1,017,055</u>
Operating expenses:		
Labor and benefits	695,736	663,240
Medical and other supplies	145,400	138,399
Purchased services and other	145,012	132,390
Depreciation	53,449	47,295
Professional fees	45,181	27,736
Interest and amortization	17,383	11,178
Total operating expenses	<u>1,102,161</u>	<u>1,020,238</u>
(Deficit) excess of revenue over expenses from operations	<u>(25,518)</u>	<u>(3,183)</u>
Other income (expense):		
Investment income (loss), net	69,986	(118,418)
(Loss) gain on disposal of property and equipment	(171)	4
Other, net	(6,481)	(4,810)
Total other income (expense)	<u>63,334</u>	<u>(123,224)</u>
Excess (deficit) of revenue over expenses	37,816	(126,407)
Change in net unrealized gain or loss on fixed income investments	(161)	(1,307)
Change in postretirement benefit obligation	(2,659)	201
Change in net assets without donor restrictions	\$ <u><u>34,996</u></u>	<u><u>(127,513)</u></u>

See accompanying notes to consolidated financial statements.

SALEM HEALTH HOSPITALS AND CLINICS

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2023 and 2022

(In thousands)

	<u>Without donor restrictions</u>	<u>With donor restrictions</u>	<u>Total</u>
Net assets at June 30, 2021	\$ 1,350,036	7,721	1,357,757
Deficit of revenue over expenses	(126,407)	—	(126,407)
Change in net unrealized gain or loss on fixed income investments	(1,307)	—	(1,307)
Change in postretirement benefit obligation	201	—	201
Contributions with donor restrictions	—	1,803	1,803
Donor restricted investments and other income, net	—	428	428
Net assets released from restrictions for operations	—	(299)	(299)
	<u>(127,513)</u>	<u>1,932</u>	<u>(125,581)</u>
Change in net assets			
Net assets at June 30, 2022	1,222,523	9,653	1,232,176
Excess of revenue over expenses	37,816	—	37,816
Change in net unrealized gain or loss on fixed income investments	(161)	—	(161)
Change in postretirement benefit obligation	(2,659)	—	(2,659)
Contributions with donor restrictions	—	815	815
Donor restricted investments and other income, net	—	52	52
Net assets released from restrictions for operations	—	(317)	(317)
	<u>34,996</u>	<u>550</u>	<u>35,546</u>
Change in net assets			
Net assets at June 30, 2023	\$ <u>1,257,519</u>	<u>10,203</u>	<u>1,267,722</u>

See accompanying notes to consolidated financial statements.

SALEM HEALTH HOSPITALS AND CLINICS

Consolidated Statements of Cash Flows

Years ended June 30, 2023 and 2022

(In thousands)

	<u>2023</u>	<u>2022</u>
Cash flows from operating activities:		
Change in net assets	\$ 35,546	(125,581)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	50,863	46,896
Change in net realized and unrealized losses (gains) on investments	(39,633)	133,441
Cash collections on contributions for long-term purposes	(608)	—
Loss (gain) on disposal of property and equipment	171	(4)
Equity income on joint venture	(525)	(1,732)
Equity distributions from joint venture	2,199	3,149
Changes in operating assets and liabilities:		
Patient accounts receivable	(4,548)	(4,704)
Other receivables	(15,798)	911
Supplies inventory	961	(1,821)
Prepaid expenses	32	(3,130)
Other noncurrent assets	(1,520)	(747)
Accounts payable	1,005	14,099
Accrued liabilities	6,250	(11,253)
Estimated third-party payor settlements, net	4,375	(3,161)
Accrued postretirement healthcare benefits	(2,001)	(1,215)
Other long-term liabilities	(801)	(804)
Estimated professional liability	3,259	(2,249)
Net cash provided by operating activities	<u>39,227</u>	<u>42,095</u>
Cash flows from investing activities:		
Purchases of investments	(51,623)	(98,391)
Investments or acquisitions of health related entities	—	(11,178)
Proceeds from sales of investments	129,977	189,186
Purchases of property and equipment and rental and other property	(83,317)	(130,193)
Net cash used in investing activities	<u>(4,963)</u>	<u>(50,576)</u>
Cash flows from financing activities:		
Proceeds from line of credit	95,000	31,000
Repayment of long-term debt	(8,445)	(8,100)
Repayment of line of credit borrowings	(95,000)	(31,000)
Restricted contributions for long-term purposes	608	—
Payment of principal on long-term debt (non-bond)	(903)	(885)
Net cash used in financing activities	<u>(8,740)</u>	<u>(8,985)</u>
Net increase (decrease) in cash and cash equivalents	25,524	(17,466)
Cash and cash equivalents at beginning of year	<u>18,568</u>	<u>36,034</u>
Cash and cash equivalents at end of year	\$ <u>44,092</u>	\$ <u>18,568</u>
Supplemental disclosure of cash flow information:		
Cash paid for interest, net of amounts capitalized	\$ 20,314	11,208
Decrease in construction related payables	(6,884)	(17,643)
Fixed assets exchanged for note receivable from joint venture investee	5,460	(6,121)
Operating lease right of use assets acquired	4,123	(1,582)

See accompanying notes to consolidated financial statements.

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

(1) Organization, Principles of Consolidation, and Operations

Salem Health Hospitals and Clinics and its subsidiaries (collectively, the Corporation) are Oregon nonprofit corporations providing a comprehensive system of healthcare services to the communities of Salem and Dallas, Oregon, and the surrounding Marion and Polk Counties.

The accompanying consolidated financial statements include the accounts and transactions of the Corporation and its subsidiaries, of which Salem Health Hospitals and Clinics is the parent holding company and sole member. The subsidiaries consist of Salem Health (Salem) and Salem Health West Valley (West Valley) (collectively, the Hospitals); Salem Health Foundation (SHF) and West Valley Hospital Foundation (WVHF) (collectively, the Foundations); and Willamette Valley Insurance Corporation (WVIC), a captive insurance company domiciled in Hawaii. All significant intercompany accounts and transactions have been eliminated in consolidation. The Corporation has formed an obligated group that is responsible for paying hospital revenue bond debt. The obligated group is comprised of the parent holding company Salem Health Hospitals and Clinics, Salem Health, and Salem Health West Valley. Salem Health West Valley was added to the obligated group during the year ended June 30, 2023.

The Hospitals provide healthcare and healthcare related services to patients in their service areas. The Hospitals' mission is to improve the health and wellbeing of the people and the communities they serve. The Foundations are dedicated to raising, managing, and distributing funds to help the Hospitals achieve their mission.

COVID 19 Pandemic and CARES Act Funding

The Coronavirus Aid, Relief, and Economic Security (CARES) Act was enacted on March 27, 2020 and authorized \$100 billion in funding to hospitals and other healthcare providers to be distributed through the Public Health and Social Services Emergency Fund (the Fund). Payments from the Fund are intended to compensate healthcare providers for lost revenues and incremental expenses incurred in response to the COVID 19 pandemic and are not required to be repaid provided the recipients attest to and comply with certain terms and conditions, including limitations on balance billing and not using the funding to reimburse expenses or losses that other sources are obligated to reimburse. During the years ended June 30, 2023 and 2022, the Corporation recognized payments of \$0 and \$7,765 from the Fund, respectively. The entire amount was recognized as other revenue in each year. The Corporation also recognized \$9,091 of reimbursement from FEMA under the state of emergency during the year ended June 30, 2023, included in other revenue in the consolidated statement of operations.

(2) Summary of Significant Accounting Policies

(a) Use of Estimates

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

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

(b) *Cash and Cash Equivalents*

Cash equivalents include investments in highly liquid instruments with original maturities of three months or less, excluding assets limited as to use. Cash equivalents totaled \$309 and \$472 at June 30, 2023 and 2022, respectively; cash equivalents exclude those balances held as part of the investment portfolio.

The Corporation maintains bank accounts at several financial institutions. The Corporation's bank balances at each financial institution are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250. At June 30, 2023 and 2022, the Corporation's bank balances at certain financial institutions exceeded FDIC coverage.

(c) *Patient Accounts Receivable and Patient Service Revenue*

Patient accounts receivable are recorded at an estimated collectible amount and do not bear interest. Explicit price concessions are established as a result of negotiated reimbursement methodologies with third party payors.

The corporation also records estimated implicit price concessions (based primarily on historical collection experience) related to uninsured accounts to record self-pay revenues at the estimated amounts the corporation expects to collect. The Corporation does not assess credit risk before services are rendered.

The mix of net patient receivables from significant third-party payors as of June 30, 2023 and 2022 was as follows:

	June 30, 2023	
Medicare	36 %	\$ 47,833
Medicaid	10	13,421
Self pay	—	415
Commercial and other payors	54	71,143
Total	100 %	\$ 132,812
	June 30, 2022	
Medicare	35 %	\$ 44,903
Medicaid	11	14,434
Self pay	—	476
Commercial and other payors	54	68,451
Total	100 %	\$ 128,264

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

The mix of patient service revenue from significant third-party payors for the years ended June 30, 2023 and 2022 was as follows:

	<u>Year ended June 30, 2023</u>	
Medicare	36 %	\$ 366,154
Medicaid	19	199,407
Self pay	—	1,359
Commercial and other payors	45	460,479
	<u>100 %</u>	<u>\$ 1,027,399</u>
	<u>Year ended June 30, 2022</u>	
Medicare	35 %	\$ 334,659
Medicaid	19	183,187
Self pay	—	5,277
Commercial and other payors	46	442,131
	<u>100 %</u>	<u>\$ 965,254</u>

The following tables represent patient service revenue by line of business in the years ending June 30, 2023 and 2022, respectively:

	<u>Year ended June 30, 2023</u>			
	<u>Inpatient</u>	<u>Outpatient</u>	<u>Clinics</u>	<u>Total</u>
Patient service revenue	\$ 523,225	429,184	74,990	1,027,399
	<u>Year ended June 30, 2022</u>			
	<u>Inpatient</u>	<u>Outpatient</u>	<u>Clinics</u>	<u>Total</u>
Patient service revenue	\$ 506,825	401,928	56,501	965,254

Performance obligations for healthcare services provided to patients generally relate to contracts of one year or less. Performance obligations for inpatient services are generally completed at the time the patients are discharged. Performance obligations for outpatient services are generally satisfied over a period of less than a day.

The Corporation elected the practical expedient option allowed under FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Corporation's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, the Corporation does, in certain instances,

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Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Services are rendered to patients under contractual arrangements with the Medicare and Medicaid programs and various other payors, including preferred provider organizations (PPOs) and health maintenance organizations (HMOs), which provide for payment or reimbursement at amounts different from established rates. Contractual adjustments represent the difference between established rates for services and amounts reimbursed by these third-party payors and represent explicit price concessions in the consolidated statement of operations.

The Medicare program reimburses Salem at prospectively determined rates for the majority of inpatient and outpatient services rendered to patients, primarily on the basis of Medicare severity diagnosis-related groups and Ambulatory Payment Classification Groups, respectively. West Valley is a "critical access hospital" (CAH) for Medicare and Medicaid program purposes. As a CAH, West Valley may not operate more than 25 beds and the average length of stay for acute care patients may not exceed 96 hours. The Medicare and Medicaid programs reimburse West Valley on the basis of its current allowable costs. When paid under cost reimbursement, the Hospitals are reimbursed at an interim rate with final settlement determined after submission of annual cost reports and audits thereof by the fiscal intermediaries, subjecting the Hospitals to retroactive settlements for prior year cost reports. Actual settlements historically approximated management's expectations.

Salem's cost reports have been audited and final settled by the Medicare fiscal intermediaries and the Medicaid administrators through June 30, 2018 and June 30, 2016, respectively. West Valley's cost reports have been audited and final settled by the Medicare fiscal intermediaries and the Medicaid administrators through June 30, 2017.

The Hospitals have also entered into payment agreements with certain commercial insurance carriers, HMOs, and PPOs to provide medical services to subscribing participants. The basis for payment to the Hospitals under these agreements includes prospectively determined rates per discharge, actual charges, and fee schedules.

(d) Supplies Inventory

Supplies inventory is stated at the lower of cost (as determined by the first-in, first-out method) or market.

(e) Investments

Investments consist of investments designated by the Corporation's board of trustees for future capital acquisitions and other purposes, investments held by the Foundations whose use has been restricted by donors, and assets held by a trustee under a bond indenture agreement (notes 5 and 6). Funds held by trustee are set aside in separate trust accounts for future capital projects and debt service reserve funds.

Investments in equity and debt securities are reported at fair value in the accompanying consolidated balance sheets. The fair values are based on quoted market prices at the reporting date for those or similar investments. Investment income or loss (including realized gains and losses on investments,

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Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

unrealized gains and losses on equity investments, interest, and dividends) is included in the excess of revenue over expenses unless the income or loss is restricted by the donor or law. The Corporation's debt investments are classified as other-than-trading securities at June 30, 2023 and 2022. Unrealized gains and losses on other-than-trading debt investments are excluded from excess of revenue over expenses unless they are considered other-than-temporarily impaired.

For each of the investment categories accounted for as other-than-trading, the Corporation continually monitors investment performance and the potential need for recording an impairment on investments. A number of criteria are considered during this process including, but not limited to, whether the Corporation intends to sell the security, the current fair value as compared to cost of the security, the length of time the security's fair value has been below cost, the likelihood that the Corporation will be required to sell the security before recovery of its cost basis, objective information supporting recovery in a reasonable period of time, specific credit issues related to the issuer, and current economic conditions.

For debt securities that the Corporation does intend to sell or is more likely than not to be required to sell prior to recovery of the cost basis, the Corporation recognizes other-than-temporary losses in accordance with the provisions of the ASC Topic 320 *Investments – Debt and Equity Securities*. The amount of the other-than-temporary loss is separated into the amount that is credit related (credit loss component) and the amount due to all other factors. The credit loss component is recognized in earnings and is the difference between a security's cost basis and the present value of expected future cash flows discounted at the security's effective interest rate. The amount due to all other factors is recognized in other changes in net assets. For the year ended June 30, 2023 or 2022, the Corporation recognized no other-than-temporary losses.

The Corporation holds investments in mutual funds, equities and common stock, corporate bonds, U.S. Treasury and government agency securities, money market funds, and mutual funds. Management believes that the Corporation's credit risk with respect to these investments is minimized due to the diversity of the individual investments and the financial strength of the entities, which have issued the securities or instruments. However, due to changes in economic conditions, interest rates, and common stock prices, the market value of the Corporation's investments can be volatile. Consequently, the fair value of the Corporation's investments could change significantly in the near term as a result of such volatility.

(f) Property and Equipment

Property and equipment (including rental and other property held for future development) are stated at cost. Donated property and equipment are recorded at estimated fair value on the date of donation. Improvements and replacements of property and equipment are capitalized. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is computed using the straight-line method over the shorter of the lease term or estimated useful life of each class of depreciable asset. The estimated useful life of buildings and improvements is 5 to 50 years while the estimated useful life of equipment is 2 to 20 years. Net 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.

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

(g) Long-Lived Assets

Management reviews property and equipment and other long-term assets for possible impairment whenever events or circumstances indicate the carrying amount of such assets may not be recoverable. If there is an indication of impairment, management would prepare an estimate of future cash flows (undiscounted and without interest charges) expected to result from the use of the asset and its eventual disposal. If these cash flows were less than the carrying amount of the asset, an impairment loss would be recognized to write down the asset to its estimated fair value. In addition to consideration of impairment due to the events or changes in circumstances described above, management regularly evaluates the remaining lives of its long-lived assets. If estimates are revised, the carrying value of affected assets is depreciated or amortized over the remaining lives.

(h) Investments in Health Related Entities

Investments in health related entities are not consolidated. The Corporation would consolidate such investees if it (a) owns a majority of the investee's stock, controls a majority voting interest in the investee's board of directors and has an economic interest in the such investee, or (b) is the sole member of the investee. If these criteria are not met, or if the Corporation owns 50% or less of the voting stock of an investee and can exercise significant influence over the investee's operating and financial policies (generally presumed when the Corporation owns more than 20% of the voting stock), the Corporation accounts for such investments under the equity method of accounting, whereby the Corporation records its proportionate share of the investee's income or loss in the consolidated statements of operations and records distributions received from the investee as a reduction in the related investment balance.

(i) Net Assets With Donor Restrictions

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

(j) Consolidated Statements of Operations

(Deficit) excess of revenue over expenses from operations includes amounts generated from direct patient care, other revenue related to the operation of the Hospitals' facilities, and contributions without donor restrictions received by the Foundations. Other activities that result in income or expenses unrelated to the Hospitals' and the Foundations' primary missions are excluded from excess of revenue over expenses from operations. Other income (expense) includes net investment income, earnings on joint ventures, change in unrealized gains and losses on equity investment securities, any other-than-temporary impairment losses on debt investment securities, rental income and expenses related to nonoperating real estate properties, gain on disposals of property and equipment, and other incidental transactions.

Changes in net assets without donor restrictions that are excluded from the excess (deficit) of revenue over expenses, consistent with industry practice, include the change in net unrealized gains (losses) on other-than-trading debt securities, change in net benefit obligation related to postretirement benefits, and contributions of long-lived assets (including assets acquired using contributions, which, by donor restriction, are to be used for the purpose of acquiring such assets).

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

(k) Contributions Received

Unconditional promises to give cash and other assets to the Corporation are recorded as other revenue and other receivables at fair value on the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value on the date the gift is received or at which point the conditions have been substantially met. Gifts are reported as contributions with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When the terms of a donor restriction are met, net assets with donor restrictions are reclassified as net assets without donor restrictions and reported in the consolidated statements of operations and consolidated statements of changes in net assets as net assets released from restrictions.

Contributions of long-lived assets, such as property and equipment, are reported as net assets without donor restrictions and are excluded from the excess of revenue over expenses. Contributions of long-lived assets with explicit restrictions that specify how the assets are to be used and contributions of cash or other assets that must be used to acquire long-lived assets are reported as net assets with donor restrictions. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Corporation reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

SHF is a beneficiary under various wills and trust agreements, the total realizable amounts of which are not presently estimable. SHF's share of such bequests is recorded when the probate court has declared the testamentary instrument valid and the proceeds are measurable.

(l) Income Taxes

The Corporation, Salem, West Valley, SHF, WVH, SHPS, and WVIC are tax-exempt organizations pursuant to Internal Revenue Code Section 501(c)(3). As such, only unrelated business income is subject to federal or state income taxes. The provision for unrelated business income taxes is immaterial to the consolidated financial statements.

Accounting principles generally accepted in the United States of America require the Corporation to evaluate tax positions taken by the Corporation and recognize a tax liability (or an asset) if the Corporation has taken an uncertain position that more likely than not would not be sustained upon examination by the Internal Revenue Service. Management has analyzed tax positions taken by the Corporation and has concluded that as of June 30, 2023, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the consolidated financial statements. The Corporation is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The Corporation's management believes it is no longer subject to income tax examinations for years prior to fiscal year 2020.

(m) State of Oregon Provider Tax

The state of Oregon assesses a provider tax on certain qualifying hospitals. The Corporation recorded provider taxes of \$55,502 and \$54,253 for the years ended June 30, 2023 and 2022, respectively, which are included in purchased services and other expense in the accompanying consolidated statements of operations. In addition, the Corporation has entered into an agreement with the Hospital Association of Oregon (the Association), which provides that all payments owed to the Corporation

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(In thousands)

related to beneficiaries of the Oregon Department of Medical Assistance Program are to be remitted directly to the Association. The Association aggregates these payments, returning a portion to the Corporation. The remaining funds are pooled by the Association with like amounts received on behalf of other hospitals subject to the provider tax, and the Association redistributes such funds to qualifying hospitals on a quarterly basis. The Corporation received \$55,165 and \$53,800 for the years ended June 30, 2023 and 2022, respectively, from the Association, which are reflected as a component of patient service revenue in the accompanying consolidated statements of operations.

(3) Benefits to the Community

The Corporation provides services to the community both for people in need and to enhance the health status of the broader community as part of its charitable mission.

(a) Services for People in Need

The following tables represent the estimated cost of providing certain services to the community, where the related revenues do not fully cover cost of services along with a description of selected activities sponsored by the Hospitals during 2023 and 2022:

	Year ended June 30, 2023		
	Estimated costs to provide care	Offsetting revenue	Estimated net cost
Services for people in need:			
Charity care	\$ 19,221	—	19,221
Medicaid	275,149	206,423	68,726
Medicare	511,675	380,439	131,236
	\$ 806,045	586,862	219,183
Percentage of total operating expenses			19.5 %

	Year ended June 30, 2022		
	Estimated costs to provide care	Offsetting revenue	Estimated net cost
Services for people in need:			
Charity care	\$ 26,857	—	26,857
Medicaid	252,171	182,797	69,374
Medicare	487,653	354,714	132,939
	\$ 766,681	537,511	229,170
Percentage of total operating expenses			21.9 %

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In support of its mission, the Hospitals voluntarily provide medically necessary patient care services that are discounted or free of charge to persons who have insufficient resources and/or who are uninsured. The criteria for charity care are determined based on eligibility for insurance coverage, household income, qualified assets, catastrophic medical events, or other information supporting a patient's inability to pay for services provided. Specifically, the Hospitals provide an uninsured discount of 51% to all uninsured patients. Further discounts are available for patients, on a sliding scale, whose household income is less than 400% of the federal poverty level, or roughly \$111 for a family of four in Salem, Oregon. For patients whose household income is at or below 300% of the federal poverty level, a full subsidy is available. In addition to the household income criteria, the patients' qualified assets (e.g., assets and investments excluding patient's primary residence) and other catastrophic or economic circumstances are considered in determining eligibility for charity care.

In addition to charity care, the Hospitals provide services under various states' Medicaid programs for financially needy patients and to Medicare beneficiaries. The aggregate cost of providing services to Medicaid and Medicare beneficiaries exceeds the aggregate reimbursements from these programs.

The cost of services provided to beneficiaries of the Medicaid and Medicare programs and cost of charity care is estimated based on the relationship of costs (excluding the costs associated with medical education, research, community health services, and other contributions) to billed charges for Medicaid and Medicare patient accounts and for patient charges written off as charity deductions.

The Hospitals employ financial counselors and social workers, who assist patients in obtaining coverage for their healthcare needs. This includes assistance with workers compensation, motor vehicle accident policies, Consolidated Omnibus Budget Reconciliation Act (COBRA), veterans' assistance, and public assistance programs, such as Medicaid.

(b) Benefits to Community

Community health services include classes provided to the community at minimal or no cost, health education for children and parents with young families, resource centers, support groups, health screenings, senior wellness, volunteer programs, caregivers respite, and support for parish nursing programs.

Community benefit activities include activities that develop community health programs and partnerships.

Donations to charitable organizations include direct support provided to community organizations through cash or in-kind donations that support organizations' missions of supporting health and human services, civic and community causes, and business development efforts.

In-kind contributions provided by the Corporation include the following: facility space, staff availability for training and education opportunities, supplies, and professional services in collaboration with charitable, educational, and government organizations throughout the community.

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(c) Other Benefits

In furtherance of its mission, the Corporation also commits significant time and resources to endeavors and critical services that meet unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include hospice; mental and behavioral health; primary care clinics in underserved neighborhoods; free patient transportation, lodging, meals, and medications for transient patients when needed; participation in blood drives; and the provision of educational opportunities for students interested in pursuing medical-related careers.

The Corporation also provides additional benefits to the community through the advocacy of community service by employees. Employees of the Corporation serve numerous organizations through board representation, membership in associations, and other related activities.

(4) Liquidity and Availability

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

	2023	2022
Financial assets at year end:		
Cash and cash equivalents	\$ 44,092	18,568
Patient accounts receivable, net	132,812	128,264
Other receivables	33,439	17,641
Investments	878,862	917,583
Total financial assets	1,089,205	1,082,056
Less amounts not available to be used within one year:		
Funds held by Trustees	42	27,972
Donor-restricted endowed funds	2,277	2,277
Financial assets not available to meet general expenditures within one year	2,319	30,249
Financial assets available to meet general expenditures within one year	\$ 1,086,886	1,051,807

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(In thousands)

(5) Investments

The composition of investments as of June 30, 2023 and 2022 is set forth in the following table. The following breakout indicates management's methodology for managing its investment portfolio. Investments are carried at fair value.

	2023	2022
Internally designated for operating and capital expenditures:		
Cash equivalents	\$ 16,706	10,955
Common stocks and equity mutual funds	467,706	444,889
Fixed-income mutual funds	371,607	412,864
Corporate bonds	4,431	3,223
U.S. government agency securities	2,253	2,386
U.S. Treasury securities	5,549	7,862
Total internally designated for operating and capital expenditures	868,252	882,179
Held by the Foundations:		
Cash equivalents	685	192
Common stocks and equity mutual funds	5,846	4,996
Fixed-income mutual funds	1,456	2,244
U.S. Treasury Securities	2,581	—
Total held by the Foundations	10,568	7,432
Held by trustee:		
Cash equivalents	42	27,972
Total held by trustee	42	27,972
Total investments	\$ 878,862	917,583

(6) Fair Value Measurements

(a) Fair Value of Financial Instruments

The fair values of the financial instruments, as discussed below, represent management's best estimates of the amounts that would be received to sell those assets or that would be paid to transfer those liabilities in an orderly transaction among market participants at the measurement date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Corporation's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Corporation based on the best information available in the circumstances.

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The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Investments: All equity and debt securities are measured using quoted market prices at the reporting date multiplied by the quantity held when quoted market prices are available. If quoted market prices for those debt securities are not available, the fair value is determined using matrix pricing, which is based on quoted prices for securities with similar coupons, ratings, and maturities, rather than on specific bids and offers for the designated security.

(b) Fair Value Hierarchy

FASB ASC Subtopic 820-10, *Fair Value Measurement*, establishes 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) and the lowest priority to measurements involving significant unobservable inputs (Level 3). The three levels of the fair value hierarchy are as follows:

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

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest-level input that is significant to the fair value measurement in its entirety. There was no reclassification of securities between Level 1 and Level 2 during the fiscal year ended June 30, 2023 or 2022. There were no Level 3 securities at June 30, 2023 or 2022.

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(In thousands)

The following table presents assets that were measured at fair value on a recurring basis at June 30, 2023:

		Fair value measurements at reporting date using	
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)
	June 30, 2023		
Assets:			
Cash equivalents	\$ 17,432	17,432	—
Common stocks and equity mutual funds	473,552	473,552	—
Fixed-income mutual funds	373,063	373,063	—
Corporate bonds	4,431	—	4,431
U.S. government agency securities	2,253	—	2,253
U.S. Treasury securities	8,131	8,131	—
Total	\$ 878,862	872,178	6,684

The following table presents assets and liabilities that were measured at fair value on a recurring basis at June 30, 2022:

		Fair value measurements at reporting date using	
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)
	June 30, 2022		
Assets:			
Cash equivalents	\$ 39,119	39,119	—
Common stocks and equity mutual funds	449,885	449,885	—
Fixed-income mutual funds	415,108	415,108	—
Corporate bonds	3,223	—	3,223
U.S. government agency securities	2,386	—	2,386
U.S. Treasury securities	7,862	7,862	—
Total	\$ 917,583	911,974	5,609

SALEM HEALTH HOSPITALS AND CLINICS

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(In thousands)

(7) Property and Equipment, Net

Property and equipment consisted of the following at June 30, 2023 and 2022:

	<u>2023</u>	<u>2022</u>
Land and improvements	\$ 41,773	38,771
Buildings and improvements	914,046	641,561
Equipment	383,909	346,689
Finance lease right-of-use assets	<u>17,582</u>	<u>17,582</u>
	1,357,310	1,044,603
Less accumulated depreciation	<u>(704,897)</u>	<u>(652,084)</u>
	652,413	392,519
Construction in progress	<u>65,292</u>	<u>279,396</u>
Property and equipment, net	<u>\$ 717,705</u>	<u>671,915</u>

Interest costs incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of acquiring those assets. The Corporation capitalized \$253 and \$3,579 in the years ending June 30, 2023 and 2022, respectively.

(8) Investments in Health-Related Activities

The following is a summary of the Corporation's related-party investments which are included in other noncurrent assets in the accompanying consolidated balance sheets at June 30, 2023 and 2022:

<u>Entity</u>	<u>Basis of accounting</u>	<u>Investment balance included in the accompanying consolidated balance sheets as of June 30, 2023 and 2022</u>		<u>The corporation's share of income (losses) included in the accompanying consolidated statements of operations for the fiscal years ended June 30, 2023 and 2022</u>	
SOSC	Equity method \$	—	(233)	(2,324)	(532)
WSC Building Group	Equity method	7,525	7,110	—	—
WSC	Equity method	<u>21,469</u>	<u>20,819</u>	<u>2,849</u>	<u>2,264</u>
	\$	<u>28,994</u>	<u>27,696</u>	<u>525</u>	<u>1,732</u>

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(a) Willamette Surgery Center, LLC

Willamette Surgery Center, LLC (WSC) is a limited liability company whose members are the Corporation and community physician partners. Equity is allocated 54.2% and 45.8%, respectively, although voting rights are allocated 42.9% and 57.1%, respectively, to the Corporation and the community physician partners. As a result, the Corporation accounts for the investment under the equity method of accounting. WSC operates and manages an outpatient orthopedic surgery center located in Salem, Oregon. The Corporation received member distributions of \$2,199 and \$2,369 in the years ending June 30, 2023 and 2022, respectively. The Corporation made an additional contribution of \$415 during the year ended June 30, 2023 of additional equity interest to WSC Building Group for future expansions. WSC Building Group LLC is a limited liability company whose members are the Corporation and community physician partners. Equity is allocated 51% and 49%, respectively. WSC Building Group LLC is solely responsible for holding the surgery center real estate. Furthermore, as of September 29, 2023 the Corporation had completed purchases of all ownership shares of both Willamette Surgery Center, LLC and WSC Building Group.

(b) The Salem Ambulatory Surgery Center, LLC

The Salem Ambulatory Surgery Center, LLC dba Salem Outpatient Surgery Center (SOSC) is a limited liability company whose members are the Corporation and various community physician partners. Equity is allocated 51.0% and 49.0%, respectively, although voting rights are allocated 44.5% and 55.5%, respectively, to the Corporation and the community physician partners. As a result, the Corporation accounts for the investment under the equity method of accounting. SOSC was formed to own, operate, and manage an outpatient surgery center to be located in Salem, Oregon. As of June 30, 2023 the surgery center has ceased operations and the full ownership was assumed by the Corporation. Salem has issued a notes receivable of \$0 and \$6,121 to SOSC for the years ending June 30, 2023 and 2022, respectively.

SALEM HEALTH HOSPITALS AND CLINICS

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(9) Long-Term Debt

Long-term debt consisted of the following at June 30, 2023 and 2022:

	2023	2022
Hospital Revenue Bonds, Series 2016A; payable in installments from \$2,010 to \$15,490 beginning in 2017 through 2046; interest at rates ranging from 2.00% to 5.00%	\$ 174,870	177,085
Hospital Revenue Bonds, Series 2019A; payable in installments from \$5,725 to \$14,710 beginning in 2020 through 2049; interest at rates ranging from 3.00% to 5.00%	260,230	266,460
Finance lease liability (a)	6,521	7,424
Unamortized cost of issuance	(1,314)	(1,369)
Unamortized premium on bonds, net	44,514	47,381
	484,821	496,981
Less current portion	(12,599)	(12,215)
	\$ 472,222	484,766

(a) The interest rate on the lease financing obligation was 1.96% at June 30, 2023. For more information on our lease financing obligations, see Note 12, Leases.

The Obligated Group is required to satisfy certain measures of financial performance as long as the bonds are outstanding under the Master Trust Indenture.

In November 2016, Salem entered into a loan agreement with the Hospital Facility Authority of Salem (the Authority), whereby the Authority issued \$197,685 of par amount fixed-rate, tax-exempt revenue refunding bonds (Series 2016A Bonds). The proceeds from Series 2016A were used to refund, redeem and defease various outstanding bond obligations.

In October 2019, Salem entered into a loan agreement with the Authority, whereby the Authority issued \$279,480 of par amount fixed-rate, tax-exempt revenue refunding bonds (Series 2019A Bonds). The proceeds from Series 2019A were used to (i) refund, redeem and defease the 2008B Bonds, (ii) terminate and settle the interest rate swap associated with 2008B Bonds, (iii) finance the construction of a new hospital tower on the Corporation's main campus, and (iv) pay fees and expenses related to the Series 2019A Bonds.

Salem Health may borrow up to \$100,000 under its line of credit agreement until it expires April 12, 2024. There were no outstanding borrowings against the line at June 30, 2023 and 2022, respectively.

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Scheduled principal repayments of long-term bonds are as follows:

	Revenue bonds
2024	\$ 8,870
2025	9,310
2026	9,710
2027	10,170
2028	10,680
Thereafter	386,360
	\$ 435,100

(10) Net Assets with Donor Restrictions

Net assets were restricted for the following purposes at June 30, 2023 and 2022:

	2023	2022
Subject to expenditure for specified purpose:		
Acquisition or construction of property and equipment for the hospitals	\$ 4,702	4,094
Specific programs of the hospitals	2,476	2,472
Scholarships	411	450
Other	337	360
	7,926	7,376
Donor-restricted endowed funds:		
Acquisition or construction of property and equipment for the hospitals	1,091	1,091
Specific programs of the hospitals	538	538
Scholarships	357	357
Other	291	291
	2,277	2,277
Total donor restricted net assets	\$ 10,203	9,653

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(11) Retirement and Postretirement Plans

(a) *Defined-Contribution Retirement Plan*

The Corporation has a contributory, defined-contribution retirement plan (the Retirement Plan) covering substantially all full-time employees. All eligible employees are allowed to contribute to the Retirement Plan on the first day of the month following their date of hire. The Hospitals contribute 5.5% to 8.5% of participating employees' annual compensation to the Retirement Plan. To receive the benefit of the Hospitals' contributions, employees must have one year or more of service at one of the Hospitals and contribute at least 1.0% of their annual compensation to the Retirement Plan. The Retirement Plan's costs were \$25,675 and \$23,941 for the fiscal years ended June 30, 2023 and 2022, respectively, and are included in labor and benefits in the accompanying consolidated statements of operations.

(b) *Postretirement Healthcare Plan*

The Corporation also sponsored a postretirement healthcare plan (the Postretirement Plan) that provided healthcare benefits to certain retirees and their dependents until the retirees reached the age of Medicare eligibility. This plan terminated during the year ending June 30, 2023. Generally, retirees were eligible to participate in the Postretirement Plan if they retired from one of the Hospitals at age 55 years or older with 10 years of service. Retirees could have converted 25% of their unused extended illness bank balance to an equivalent dollar amount, which then could be used to purchase medical, dental, or vision coverage for the retiree and/or dependents. Any unused balance would be forfeited when the retiree reached the age of Medicare eligibility.

The Corporation accounted for the Postretirement Plan in accordance with FASB ASC Topic 715, Compensation – Retirement Benefits, which requires the employer to recognize the overfunded or underfunded status of a plan as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through changes in net assets without donor restrictions. Under ASC Topic 715 the measurement of the funded status is the difference between the fair value of the plan assets and the benefit obligation of the plan. ASC Topic 715 also requires the Corporation to recognize in net assets without donor restrictions any unrecognized net actuarial gains or losses and any unrecognized prior service costs or credits as they arise and disclose in the notes to the consolidated financial statements additional information about the effect on net periodic benefit cost on the next fiscal year that arises from the delayed recognition of these items.

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(In thousands)

The accrued liability for postretirement benefits at June 30, 2023 and 2022 was as follows:

	<u>2023</u>	<u>2022</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 2,282	3,594
Interest cost	40	44
Participants' contributions	179	442
Amendments	(1,964)	—
Actuarial gain	(217)	(978)
Benefits paid	<u>(320)</u>	<u>(820)</u>
Benefit obligation at end of year	\$ <u>—</u>	<u>2,282</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ —	—
The Corporation's contributions	141	378
Participants' contributions	179	442
Benefits paid	<u>(320)</u>	<u>(820)</u>
Fair value of plan assets at end of year	\$ <u>—</u>	<u>—</u>

A reconciliation of the Postretirement Plan's funded status at June 30, 2023 and 2022 and to the Hospitals' accrued postretirement healthcare benefits at June 30, 2023 and 2022 was as follows:

	<u>2023</u>	<u>2022</u>
Funded status	\$ —	2,282
Current portion of accrued postretirement healthcare benefits	<u>—</u>	<u>(281)</u>
Long-term portion of accrued postretirement healthcare benefits	\$ <u>—</u>	<u>2,001</u>

The current portion of accrued postretirement healthcare benefits is included in accrued liabilities in the accompanying consolidated balance sheets.

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The service cost component of the Corporation's net periodic postretirement benefit cost included in labor and benefits and the other components of the Hospitals' net periodic postretirement benefit cost are included in other, net in the accompanying consolidated statements of operations for the fiscal years ended June 30, 2023 and 2022 were as follows:

	12 months ended June 30	
	2023	2022
Interest cost	\$ 40	44
Expected return on plan assets	(2,430)	—
Amortization of prior service cost	(1,964)	—
Net actuarial (gain) / loss recognized	(447)	—
Net periodic postretirement benefit (gain) cost	\$ (4,801)	44

Losses (gains) accumulated in net assets without donor restrictions in the accompanying consolidated statements of changes in net assets through the fiscal years ended June 30, 2023 and 2022 were \$0 and (\$2,458), respectively. The components of the Corporation's other changes in plan assets and benefit obligations recognized in net assets without donor restrictions in the accompanying consolidated statements of changes in net assets for the fiscal years ended June 30, 2023 and 2022 were as follows:

	12 months ended June 30	
	2023	2022
Net (gain) loss	\$ (218)	(978)
Prior service cost (credit)	(1,964)	—
Amortization of net loss	2,877	—
Amortization of prior service cost	1,964	777
Total recognized in net assets without donor restrictions	\$ 2,659	(201)

Weighted average assumptions used to determine benefit obligations for June 30, 2023 and 2022 were as follows:

	2023	2022
Discount rate	— %	3.73 %
Rate of compensation increase	—	—

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For actuarial measurement purposes, annual rate increases in the per capita cost of covered healthcare benefits of 7.3% (pre-65) and 4.8% (post-65) were assumed for 2022 through 2023. Thereafter, the rate was assumed to decrease by approximately 1.4% percentage points on an annual basis to 4.97% in 2031 and then decrease gradually to 3.94%. For the fiscal year ended June 30, 2022, the Corporation utilized the PRI-2012 total dataset Mortality Table with the MP-2021 Mortality Improvement Scale for estimating the actuarial values

(12) Leases

The Corporation leases medical and administrative office buildings and equipment to support operations. The operating and finance leases are reflected within the consolidated balance sheets as follows at June 30, 2023 and 2022:

	June 30, 2023		
	Operating leases	Finance leases	Total
Assets:			
Rental and other property, net	\$ 12,918	—	12,918
Property and equipment, net	—	11,216	11,216
Total leased assets	\$ 12,918	11,216	24,134
Liabilities:			
Lease liabilities due within one year:			
Accrued liabilities other	\$ 3,537	—	3,537
Current portion of long-term debt	—	921	921
Long-term lease liabilities:			
Other long-term liabilities	9,541	—	9,541
Long-term debt, net of current portion	—	5,600	5,600
Total lease liabilities	\$ 13,078	6,521	19,599

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	<u>June 30, 2022</u>		
	<u>Operating leases</u>	<u>Finance leases</u>	<u>Total</u>
Assets:			
Rental and other property, net	\$ 8,795	—	8,795
Property and equipment, net	<u>—</u>	<u>13,035</u>	<u>13,035</u>
Total leased assets	<u>\$ 8,795</u>	<u>13,035</u>	<u>21,830</u>
Liabilities:			
Lease liabilities due within one year:			
Accrued liabilities other	\$ 2,713	—	2,713
Current portion of long-term debt	<u>—</u>	<u>903</u>	<u>903</u>
Long-term lease liabilities:			
Other long-term liabilities	6,282	—	6,282
Long-term debt, net of current portion	<u>—</u>	<u>6,521</u>	<u>6,521</u>
Total lease liabilities	<u>\$ 8,995</u>	<u>7,424</u>	<u>16,419</u>

The weighted average remaining terms of operating and financing leases were 4 and 6 years, respectively. The weighted average discount rates on operating and financing leases were 2.19% and 1.96%, respectively.

The Corporation incurred lease expenses for the year ended June 30, 2023 and 2022 as follows:

	<u>2023</u>	<u>2022</u>
Finance lease expense included in depreciation and amortization:		
Amortization of ROU assets	\$ 1,819	1,819
Finance lease expense included in interest:		
Interest on lease liabilities	<u>136</u>	<u>153</u>
Total finance lease expense	<u>\$ 1,955</u>	<u>1,972</u>
Operating lease expense included in purchased services and other		
	\$ 3,059	3,228
Operating lease expense included in other, net	765	593
Short-term lease expense included in purchased services and other	758	1,234
Short-term lease expense included in other, net	<u>190</u>	<u>227</u>
Total operating lease expense	<u>\$ 4,772</u>	<u>5,282</u>

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The finance and operating leases liabilities will mature as follows:

	Finance leases	Operating leases	Total leases
2024	\$ 1,038	3,874	4,912
2025	1,125	2,785	3,910
2026	1,142	2,629	3,771
2027	1,142	2,029	3,171
2028	1,142	1,003	2,145
Thereafter	1,333	1,746	3,079
Interest	<u>(401)</u>	<u>(988)</u>	<u>(1,389)</u>
	<u>\$ 6,521</u>	<u>13,078</u>	<u>19,599</u>

(13) Functional Classification of Expenses

The Corporation allocates expenses by function on a department basis based on their functional role. Departments supporting the entire corporation in a support services function are classified as management and general; departments providing hospital based services and clinics providing ambulatory services are categorized accordingly. Foundation expenses consist of both the hospital foundations and the support services associated with operating those foundations incurred by other Salem entities. Expenses on a functional basis for the fiscal years ended June 30, 2023 and 2022 were as follows:

	2023				Total
	Hospital	Clinics	Foundation	General and administrative	
Labor and benefits	\$ 443,781	132,542	262	119,151	695,736
Medical and other supplies	132,967	4,275	66	8,092	145,400
Purchased services and other	83,654	4,622	3,292	53,444	145,012
Depreciation	29,686	2,361	101	21,301	53,449
Professional fees	13,942	21,620	7	9,612	45,181
Interest and amortization	<u>17,383</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>17,383</u>
Total	<u>\$ 721,413</u>	<u>165,420</u>	<u>3,728</u>	<u>211,600</u>	<u>1,102,161</u>

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

	2022				
	Hospital	Clinics	Foundation	General and administrative	Total
Labor and benefits	\$ 418,089	111,459	265	133,427	663,240
Medical and other supplies	123,039	4,476	55	10,829	138,399
Purchased services and other	78,924	4,735	1,585	47,146	132,390
Depreciation	28,849	1,852	106	16,488	47,295
Professional fees	16,924	3,651	2	7,159	27,736
Interest and amortization	11,178	—	—	—	11,178
Total	\$ 677,003	126,173	2,013	215,049	1,020,238

(14) Commitments and Contingencies

(a) General and Professional Liability Insurance

On a claims-made basis, WVIC provides primary insurance coverage up to a \$1,000 self-insured retention limit per occurrence and \$6,000 annual aggregate limits for healthcare professional and general liability (\$1,000/\$6,000 limits) for Salem and West Valley for the years ending June 30, 2023 and 2022. Excess insurance coverage is in place. In excess of the \$1,000/\$6,000 limits, the Hospitals annually purchase reinsurance coverage for claims up to \$34,000 in aggregate on a claims-made basis. Reinsurance contracts do not relieve the Corporation from its obligations to claimants. Failure of reinsurers to honor their obligations could result in losses to the Corporation. The Corporation evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurer to manage its exposure to significant losses from reinsurer insolvencies.

General and professional liability costs are accrued based upon an actuarial determination with estimated incurred-but-not-reported professional liability losses recorded at the expected, undiscounted level. The Corporation has recorded estimated liabilities for incurred-but-not-reported professional liability claims and for deductibles on reported claims aggregating \$13,357 and \$10,098 as of June 30, 2023 and 2022, respectively. The estimated liabilities for incurred-but-not-reported medical claims are recorded on the Hospitals' books. WVIC carries the estimated liabilities for deductibles on reported claims. Management believes that these estimated liabilities are adequate; however, the establishment of estimated liabilities for incurred-but-not-reported medical malpractice claims and for deductibles on reported claims is an inherently uncertain process, and there can be no assurance that currently established reserves will prove adequate to cover actual ultimate expenses. Subsequent actual experience could result in reserves being too high or too low, which could positively or negatively impact operations in future periods.

The Corporation records claim liabilities without consideration of insurance recoveries and receivables for insurance recoveries to be reported separately subject to a valuation allowance as appropriate. The Corporation recorded an asset for insurance recoveries receivable and estimated liabilities in the amount of \$2,810 and \$2,292 as of June 30, 2023 and 2022, respectively. The insurance recovery receivable and insured claims liability are included in other noncurrent assets and estimated medical

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

malpractice claims liability in the accompanying consolidated balance sheets. No valuation allowance was recorded related to reinsurance receivables as of June 30, 2023 and 2022.

(b) Self-Insured Employee Benefits

The Corporation is self-insured for employee's medical and dental claims. Claims are accrued as incurred. The Corporation has recorded an accrual for the estimated claims, including estimates of the ultimate costs for both reported claims and claims incurred but not reported of \$6,980 and \$7,109 as of June 30, 2023 and 2022, respectively. Management believes that these amounts, which have been included within other accrued liabilities in the accompanying consolidated balance sheets, are adequate to cover estimated employee's medical and dental claims.

(c) Risk Management

In the ordinary course of business, the Corporation is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; and natural disasters. Management believes that adequate commercial insurance coverage has been purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage for the fiscal year ended June 30, 2023 or 2022. The Corporation is self-insured for workers' compensation claims. The Corporation has recorded estimated liabilities for claims in the amount of \$3,563 and \$4,187 as of June 30, 2023 and 2022, respectively, which have been included in other accrued liabilities in the accompanying balance sheet.

(d) Regulation and Litigation

The healthcare industry is governed by various laws and regulations of federal, state, and local governments. These laws and regulations are subject to ongoing government review and interpretation and include matters such as licensure, accreditation, reimbursement for patient services, and referrals for Medicare and Medicaid beneficiaries. Compliance with these laws and regulations is required for participation in government healthcare programs and have become more complicated in recent years due to changes resulting from the health reform law and the introduction of health benefit exchanges and coordinated care organizations into the local marketplace. Certain governmental agencies routinely investigate and pursue allegations concerning possible overpayments resulting from violation of fraud and abuse statutes by healthcare providers. These types of investigations may result in settlements involving fines and penalties, as well as repayment of improper reimbursement. The Corporation has implemented procedures for monitoring and enforcing compliance with laws and regulations and is not aware of significant instances of noncompliance.

SALEM HEALTH HOSPITALS AND CLINICS

Notes to Consolidated Financial Statements

June 30, 2023 and 2022

(In thousands)

(15) Lean Initiatives (Unaudited)

The lean management system (Lean) was initially introduced to the Corporation in 2010 to improve the quality of care and transform their culture. The purpose of Lean is to create value for the patient through its three main components: continuous improvement, elimination of waste and variation, and respect for people. Using Lean, the Corporation aligns its strategies to their daily work: engaging its providers and employees to become problem solvers and continually ask the question “why,” ensuring all employees work together toward the same outcomes and keeping the Corporation strong and effective.

In fiscal years 2023 and 2022, the Corporation had a strategic goal to engage frontline staff in leading and completing a Lean activity to remove waste from the system, creating improved value for their patients.

	12 months ended June 30	
	2023	2022
	(Not in thousands)	
% of front line staff leading and completing a lean activity	98 %	97 %
Total lean activities completed	6,452	6,813

The Corporation continues to invest increasing efforts in Lean to create value for their patients by increasing access to care, improving patient experience, and delivering quality care at a lower cost.

(16) Subsequent Events

The Corporation evaluated subsequent events after the consolidated balance sheet date of June 30, 2023 through October 6, 2023 which was the date the consolidated financial statements were issued.

SALEM HEALTH HOSPITALS AND CLINICS

Supplemental Schedule – Consolidating Balance Sheet Information

June 30, 2023

(In thousands)

	<u>Obligated group</u>	<u>Non-obligated group</u>	<u>Consolidated FY23</u>	<u>Consolidated FY22</u>
Current assets:				
Cash and cash equivalents	\$ 43,156	936	44,092	18,568
Patient accounts receivable, net	132,812	—	132,812	128,264
Other receivables	30,257	3,182	33,439	17,641
Supplies inventory	10,552	—	10,552	11,513
Prepaid expense and other	15,586	16	15,602	16,948
Total current assets	<u>232,363</u>	<u>4,134</u>	<u>236,497</u>	<u>192,934</u>
Investments	848,551	30,311	878,862	917,583
Property and equipment, net	717,705	—	717,705	671,915
Rental and other property held for future development, net	38,184	692	38,876	54,685
Investments in health related entities	40,549	(11,555)	28,994	27,696
Other noncurrent assets	34,119	(10,794)	23,325	26,734
Total assets	<u>\$ 1,911,471</u>	<u>12,788</u>	<u>1,924,259</u>	<u>1,891,547</u>

SALEM HEALTH HOSPITALS AND CLINICS

Supplemental Schedule – Consolidating Balance Sheet Information

June 30, 2023

(In thousands)

	<u>Obligated group</u>	<u>Non-obligated group</u>	<u>Consolidated FY23</u>	<u>Consolidated FY22</u>
Current liabilities:				
Accounts payable	\$ 67,054	(1)	67,053	72,932
Accrued liabilities:				
Payroll, payroll taxes, and withholdings	21,245	—	21,245	15,981
Paid time off	29,526	—	29,526	28,760
Other	19,067	—	19,067	18,847
Estimated third-party payor settlements, net	11,798	—	11,798	7,423
Current portion of long-term debt	12,599	—	12,599	12,215
Current portion of estimated professional liability	2,399	—	2,399	2,245
Total current liabilities	<u>163,688</u>	<u>(1)</u>	<u>163,687</u>	<u>158,403</u>
Long-term debt, net of current portion	472,222	—	472,222	484,766
Accrued postretirement healthcare benefits	—	—	—	2,001
Other long-term liabilities	9,670	—	9,670	6,348
Estimated medical malpractice claims liability	2,810	8,148	10,958	7,853
Total liabilities	<u>648,390</u>	<u>8,147</u>	<u>656,537</u>	<u>659,371</u>
Net assets:				
Without donor restrictions	1,255,943	1,576	1,257,519	1,222,523
With donor restrictions	7,138	3,065	10,203	9,653
Total net assets	<u>1,263,081</u>	<u>4,641</u>	<u>1,267,722</u>	<u>1,232,176</u>
Total liabilities and net assets	<u>\$ 1,911,471</u>	<u>12,788</u>	<u>1,924,259</u>	<u>1,891,547</u>

See accompanying independent auditors' report.

SALEM HEALTH HOSPITALS AND CLINICS

Supplemental Schedule – Consolidating Operations Information

Fiscal year ending June 30, 2023

(In thousands)

	<u>Obligated group</u>	<u>Non-obligated group</u>	<u>Consolidated FY23</u>	<u>Consolidated FY22</u>
Operating revenue:				
Patient service revenue	\$ 1,027,399	—	1,027,399	965,254
Other revenue	47,297	1,630	48,927	51,502
Net assets released from restriction used for operations	—	317	317	299
Total operating revenue	<u>1,074,696</u>	<u>1,947</u>	<u>1,076,643</u>	<u>1,017,055</u>
Operating expenses:				
Labor and benefits	695,736	—	695,736	663,240
Medical and other supplies	145,397	3	145,400	138,399
Purchased services and other	140,263	4,749	145,012	132,390
Depreciation	53,449	—	53,449	47,295
Professional fees	45,098	83	45,181	27,736
Interest and amortization	17,383	—	17,383	11,178
Total operating expenses	<u>1,097,326</u>	<u>4,835</u>	<u>1,102,161</u>	<u>1,020,238</u>
(Deficit) excess of revenue over expenses from operations	<u>(22,630)</u>	<u>(2,888)</u>	<u>(25,518)</u>	<u>(3,183)</u>
Other income (loss):				
Investment (loss) income, net	68,315	1,671	69,986	(118,418)
Gain on disposal of property and equipment	(171)	—	(171)	4
Other, net	(9,736)	3,255	(6,481)	(4,810)
Total other income (expense)	<u>58,408</u>	<u>4,926</u>	<u>63,334</u>	<u>(123,224)</u>
(Deficit) excess of revenue over expenses	35,778	2,038	37,816	(126,407)
Change in net unrealized gain or loss on fixed income investments	—	(161)	(161)	(1,307)
Change in postretirement benefit obligation	(2,659)	—	(2,659)	201
Change in net assets	<u>\$ 33,119</u>	<u>1,877</u>	<u>34,996</u>	<u>(127,513)</u>

See accompanying independent auditors' report.