



Consolidated Financial Statements,
Supplementary Information and
Report of Independent Certified
Public Accountants

Peninsula Regional Health System, Inc.

June 30, 2020 and 2019



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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
Peninsula Regional Health System, Inc.

We have audited the accompanying consolidated financial statements of Peninsula Regional Health System, Inc. and subsidiaries (the "Health System"), which comprise the consolidated balance sheets as of June 30, 2020 and 2019, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with 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 audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the 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 Health System'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 Health System'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 consolidated financial position of Peninsula Regional Health System, Inc. and subsidiaries as of June 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.

Emphasis of matter

As discussed in Note 2 to the consolidated financial statements, during the year ended June 30, 2020, the Health System adopted Accounting Standard Update 2016-02, *Leases*. Our opinion is not modified with respect to this matter.

Supplementary information

Our audits were performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating information is presented for the purpose of additional analysis, rather than to present the financial position, results of operations and changes in net assets, and cash flows of the individual entities, and is not a required part of the consolidated financial statements. Such supplementary 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 our audits of the consolidated financial statements and certain additional procedures. These additional procedures include comparing and reconciling the information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.



Philadelphia, Pennsylvania
October 28, 2020

Peninsula Regional Health System, Inc.

CONSOLIDATED BALANCE SHEETS

June 30,

(Dollar amounts in thousands)

	<u>2020</u>	<u>2019</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 179,524	\$ 46,639
Short-term investments	7,528	7,919
Assets limited as to use	3,149	3,695
Patient accounts receivable	57,020	41,484
Supplies	14,792	9,450
Prepays and other	<u>13,205</u>	<u>9,407</u>
Total current assets	275,218	118,594
INVESTMENTS	415,488	344,053
ASSETS LIMITED AS TO USE		
Under debt agreement	58,609	-
Self-insurance fund	33,428	24,247
Donor-restricted fund	<u>49,064</u>	<u>42,463</u>
	141,101	66,710
PROPERTY AND EQUIPMENT, net	315,721	220,725
OTHER ASSETS	<u>43,655</u>	<u>21,108</u>
Total assets	<u>\$ 1,191,183</u>	<u>\$ 771,190</u>

The accompanying notes are an integral part of these consolidated financial statements.

Peninsula Regional Health System, Inc.

CONSOLIDATED BALANCE SHEETS - CONTINUED

June 30,

(Dollar amounts in thousands)

	2020	2019
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current portion of long-term debt	\$ 4,671	\$ 2,394
Current portion of lease liability	1,932	-
Current portion of self-insurance liabilities	3,149	3,695
Accounts payable	34,335	19,138
Accrued liabilities	32,896	20,595
Advances from third-party payors	133,059	9,775
Total current liabilities	210,042	55,597
Long-term debt, less current portion	237,429	132,736
Lease liability, less current portion	6,628	-
Self-insurance liabilities, less current portion	29,197	16,614
Accrued retirement benefits	17,599	155
Other liabilities	1,282	559
Total liabilities	502,177	205,661
NET ASSETS		
Net assets without donor restrictions:		
Peninsula Regional Health System, Inc.	634,633	516,916
Non-controlling interest	1,889	1,590
Total net assets without donor restrictions	636,522	518,506
Net assets with donor restrictions	52,484	47,023
Total net assets	689,006	565,529
Total liabilities and net assets	\$ 1,191,183	\$ 771,190

The accompanying notes are an integral part of these consolidated financial statements.

Peninsula Regional Health System, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS

Years ended June 30,
(Dollar amounts in thousands)

	2020	2019
NET ASSETS WITHOUT DONOR RESTRICTIONS		
Revenue		
Patient service revenue	\$ 535,924	\$ 458,468
Other revenue	34,993	6,235
	570,917	464,703
Expenses		
Salaries and wages	235,861	189,698
Supplies and other expenses	254,769	189,762
Employee benefits	56,354	46,269
Depreciation and amortization	35,277	30,256
Interest	6,492	5,210
	588,753	461,195
Total expenses		
	(17,836)	3,508
(Loss) income from operations before other items		
Other items		
Investment return	33,011	33,944
Other pension gains	2,978	2,828
Contribution received in acquisitions	111,283	-
Loss on extinguishment of debt	(4,142)	-
	143,130	36,772
Total other items		
	125,294	40,280
Excess of revenue over expenses		
Non-controlling interest in earnings of controlled subsidiary	(299)	(50)
	124,995	40,230
Excess of revenue over expenses attributable to Peninsula Regional Health System, Inc.		

(continued on next page)

The accompanying notes are an integral part of these consolidated financial statements.

Peninsula Regional Health System, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS - CONTINUED

Years ended June 30,
(Dollar amounts in thousands)

	2020	2019
NET ASSETS WITHOUT DONOR RESTRICTIONS		
Excess of revenue over expenses attributable to Peninsula Regional Health System, Inc. <i>(continued from previous page)</i>	\$ 124,995	\$ 40,230
Net assets released from restrictions, net	1,726	585
Change in non-controlling interest	(143)	50
Other changes in accrued retirement benefits	(8,562)	(4,654)
Increase in net assets without donor restrictions	118,016	36,211
NET ASSETS WITH DONOR RESTRICTIONS		
Contributions	3,118	2,055
Net realized gains on investments	2,679	3,010
Change in unrealized gains and losses on investments	1,574	599
Net assets released from restrictions, net	(1,910)	(1,033)
Increase in net assets with donor restrictions	5,461	4,631
Increase in net assets	123,477	40,842
Net assets at beginning of year	565,529	524,687
Net assets at end of year	\$ 689,006	\$ 565,529

The accompanying notes are an integral part of these consolidated financial statements.

Peninsula Regional Health System, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended June 30,
(Dollar amounts in thousands)

	2020	2019
Operating activities:		
Increase in net assets	\$ 123,477	\$ 40,842
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Contribution received in acquisitions	(111,283)	-
Loss on extinguishment of debt	4,142	-
Depreciation and amortization	35,277	30,256
Other changes in accrued retirement benefits	8,562	4,654
Amortization of original issue premium and financing costs	(832)	(802)
Equity in earnings of unconsolidated joint ventures	(1,547)	(482)
(Gain) losses on sale of property and equipment	(1,232)	67
Net realized and unrealized gains and losses on investments	(27,174)	(30,902)
Proceeds from restricted contributions	(3,118)	(2,055)
Changes in operating assets and liabilities:		
Patient accounts receivable	4,334	(1,055)
Supplies and other assets	(524)	(1,600)
Distributions from unconsolidated joint ventures	1,009	2,944
Accounts payable and accrued liabilities	10,572	3,614
Accrued retirement benefits	6,094	678
Other liabilities	4,044	(1,771)
Lease liability	(1,684)	-
Advances from third-party payors	123,284	(309)
	173,401	44,079
Investing activities:		
Change in investments and assets limited as to use	(63,633)	(7,275)
Cash received in the acquisitions	6,021	-
Investment in unconsolidated joint ventures	(8,139)	(1,134)
Purchases of property and equipment, net	(24,826)	(25,687)
	(90,577)	(34,096)
Financing activities:		
Proceeds from restricted contributions	3,118	2,055
Debt issuance costs paid	(1,617)	-
Proceeds from long-term debt	101,672	-
Repayments of long-term debt	(53,112)	(2,280)
	50,061	(225)
Net cash provided by (used in) financing activities	50,061	(225)
Net increase in cash and cash equivalents	132,885	9,758
Cash and cash equivalents at beginning of year	46,639	36,881
Cash and cash equivalents at end of year	\$ 179,524	\$ 46,639

The accompanying notes are an integral part of these consolidated financial statements.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2020 and 2019

(Dollar amounts in thousands)

NOTE 1 - ORGANIZATION AND MISSION

Peninsula Regional Health System, Inc. (“PRHS”) is a not-for-profit Maryland membership corporation, that serves as the parent company to a group of affiliated non-profit and for-profit entities (collectively the “Health System”). The Health System’s mission is to improve the health of communities of the eastern shore of Maryland, southern Delaware, northern Virginia and portions of the Delaware-Maryland-Virginia Peninsula (the “Delmarva Peninsula”). The Health System’s group of affiliated non-profit and for-profit entities are as follows:

Peninsula Regional Medical Center, Inc. (the “PRMC”) is a not-for-profit, nonstock corporation founded in 1897 to serve the health care needs of its region. Service areas include the Maryland counties of Wicomico, Dorchester, Somerset, and Worcester; southern Delaware; and the northern Eastern Shore of Virginia. PRMC wholly owned Delmarva Peninsula Insurance Company (“DPIC”), a Cayman Island captive insurance company that provides professional and general liability insurance. Effective June 30, 2020, DPIC’s ownership was transferred to PRHS.

Peninsula Regional Medical Center Foundation, Inc. (the “Foundation”) is a not-for-profit, nonstock corporation organized to raise contributions exclusively for the benefit of charitable, educational, medical, and scientific purposes for the Health System.

Peninsula Health Ventures, Inc. (“Health Ventures”) is a for-profit corporation organized for the purpose of owning, developing, operating, and investing in health care enterprises on the Delmarva Peninsula.

Peninsula Women’s Center, LLC d/b/a Peninsula Surgery Center, operates an ambulatory surgery center.

Peninsula Regional Clinically Integrated Network, LLC participates in the Medicare Shared Savings Program as an Accountable Care Organization (“ACO”), providing Medicare beneficiaries on the Delmarva Peninsula with access to coordinated care.

On January 1, 2020 (the Nanticoke Acquisition Date), PRHS acquired and became the sole corporate member of Nanticoke Memorial Hospital, Inc. (“NMH”), a not-for-profit 99 licensed bed hospital in Seaford, Delaware, serving the health care needs of Sussex County, Nanticoke Insurance Company Ltd (“NIC”), a captive insurance company domiciled in the Cayman Islands, which was wholly owned by NMH, and provides professional and general liability insurance to related affiliates, Mid-Sussex Medical Center, Inc. d/b/a Nanticoke Physician Network (“NPN”), a not-for-profit physician practice organization that provides outpatient medical care in clinics located in Georgetown, Laurel, Bridgeville, Delmar and Seaford, Delaware as well as Federalsburg, Maryland and the not-for-profit Nanticoke Health Foundation, (collectively “Nanticoke”). Concurrently, the Nanticoke Health Foundation was merged into the Foundation.

Effective June 30, 2020, NIC was merged into DPIC.

On March 1, 2020 (the McCready Acquisition Date), PRHS acquired and became the sole corporate member of McCready Foundation, Inc., a not-for-profit located in Crisfield, Maryland, which consists of the following divisions: Edward W. McCready Memorial Hospital (“McCready Hospital”), a 3 bed hospital, Alice Byrd Tawes Nursing Home (the “Nursing Home”), a 76-licensed bed skilled nursing home, Chesapeake Cove Assisted Living Center (the “Rehab Center”), a rehabilitation center and assisted living facility and the McCready Foundation, Inc. Endowment Fund (“Endowment Fund”). Concurrently, the McCready Hospital division was merged into PRMC and the hospital was converted into a free standing medical center and the Endowment Fund was merged into the McCready Foundation, Inc.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019

(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Health System and all affiliated non-profit and for-profit entities as described in Note 1, with the exception of joint ventures where there is less than 50% control or where the Health System does not have the ability to exercise significant influence. Joint ventures where the ownership is greater than 50% or control are included in the accompanying consolidated financial statements and the non-controlling interest is recorded equal to the remaining ownership interest. All significant intercompany transactions have been eliminated.

Recently Adopted Accounting Pronouncement

In February 2016, the Financial Accounting Standards Board "FASB" issued Accounting Standards Update "ASU" No. 2016 02, *Leases*, as amended, which requires (1) most leases to be recognized on the balance sheet and (2) disclosure about leasing arrangements. The new standard is effective for fiscal years beginning after December 15, 2019, with early application permitted. The new standard establishes a right of use ("ROU") model that requires a lessee to recognize a ROU asset and lease liability on the balance sheet for all leases with a term longer than 12 months. Leases will be classified as finance or operating, with classification affecting the pattern and classification of expense recognition in the statement of operations.

The Health System adopted the new standard on July 1, 2019, and elected the option to apply the transition requirements in the standard. Consequently, financial information will not be updated and the disclosures required under the standard will not be provided for dates and periods before July 1, 2019.

The new standard provides a number of optional practical expedients in transition. The Health System has elected the "package of practical expedients," which permits entities to not reassess conclusions prior to the implementation of the new standard about lease identification, lease classification and initial direct costs.

The most significant effects on the Health System's consolidated financial statements relate to: (1) the recognition of new ROU assets and lease liabilities on the consolidated balance sheets for existing real estate and equipment operating leases; and (2) providing significant new disclosures about leasing activities.

The impact on the July 1, 2019 consolidated balance sheet is the recognition of the ROU assets, included in other assets in the consolidated balance sheet and corresponding operating lease liabilities of \$6,916 based on the present value of the remaining minimum rental payments for existing operating leases.

The new standard also provides practical expedients for an entity's ongoing accounting. The Health System has elected the short-term lease recognition exemption for all leases that qualify. This means, for those leases that qualify, the Health System will not recognize ROU assets or lease liabilities, and this includes not recognizing ROU assets or lease liabilities for existing short-term leases of those assets in transition.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES - Continued

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") 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 revenues and expenses during the reporting period. The most significant management estimates and assumptions are used in recording patient accounts receivable and patient service revenue, estimated settlements with third-party payors, useful lives of property and equipment, goodwill and other intangibles, actuarial estimates for the accrued retirement benefits, professional, general liabilities and workers' compensation costs, the reported fair value of certain assets and liabilities, including the fair value of assets and liabilities as part of the acquisitions, and the allocation of functional expenses. Actual amounts could differ from those estimates.

Fair Value of Financial Instruments

Financial instruments consist of cash equivalents, patient accounts receivable, investments and assets limited as to use, accounts payable, accrued liabilities, estimated settlements with third-party payors, advances from third-party payors and long-term debt. The carrying amounts reported in the consolidated balance sheets for cash equivalents, patient accounts receivable, investments and assets limited as to use, accounts payable, accrued liabilities, estimated settlements with third-party payors, advances from third-party payors, approximate fair value. Management's estimate of the fair value of other financial instruments is described elsewhere in the notes to the consolidated financial statements.

Cash and Cash Equivalents

Cash and cash equivalents include surplus operating funds invested in money market funds and highly-liquid corporate, U.S. government, and agency obligations, all with maturities of less than three months when purchased.

Investments and Assets Limited As To Use

Investments are carried at fair value. Fair values of all investments, including short-term investments, investments, and assets limited as to use are based on quoted market prices and/or prices obtained from a third party using other market data for the same or comparable instruments and transactions in establishing the prices. Short term investments represent investments with contractual maturities within one year and current investments in money market funds that have been designated for investment purposes.

Assets limited as to use includes externally held assets held by trustees under a debt agreement and consists of those assets designated for the payments of construction projects, principal and interest due on indebtedness and cost of issuance, externally held assets held by trustees self-insurance programs and assets internally held to meet donor's intentions. Assets limited as to use required to meet current liabilities have been classified as current assets on the consolidated balance sheets.

Investment income, including interest and dividend, realized gains and losses (the value of securities sold) is based on the specific identification method. Investment income on investments of restricted assets are added to or deducted from the appropriate restricted net assets when restricted as to use by the donor.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES - Continued

Patient Accounts Receivable

A receivable is recognized when there is an unconditional right to payment, subject only to the passage of time. Patient accounts receivable, including billed accounts and unbilled accounts, which have the unconditional right to payment, and estimated amounts due from third-party payers for retroactive adjustments, are recorded as receivables since the right to consideration is unconditional and only the passage of time is required before payment of that consideration is due. The estimated uncollectible amounts are generally considered implicit price concessions that are recorded as a direct reduction to patient accounts receivable.

Discounts ranging from 2.0% to 7.7% of charges are given to Medicare, Medicaid, and certain approved commercial health insurance and health maintenance organization programs for regulated services. Discounts in varying percentages are given for certain unregulated services.

Supplies

Supplies are carried at the lower of cost or market, using the first-in, first-out method.

Property and Equipment

Property and equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Equipment acquired under finance leases is amortized based on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Construction in progress represents amounts expended or incurred toward property and equipment projects that have not been completed. No depreciation or amortization has been recorded for these items. Interest cost incurred, net of investment income earned on borrowed funds, during the period of construction is capitalized as a component of the cost of acquiring those assets.

Software development costs that are incurred in the preliminary project stage for internal use software are expensed as incurred. During the development stage, direct consulting costs and payroll and payroll-related costs for employees that are directly associated with each project are capitalized and amortized over the estimated useful life of the software once the software is ready for its intended use. Capitalized software is amortized using the straight-line method over its estimated useful life, which is generally seven years. Replacements and upgrades and enhancements to existing systems that result in added functionality are capitalized, while maintenance and repairs are charged to expense as incurred.

Gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted donations. Absent explicit donor stipulations about how long those assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Leases

The Health System determines if an arrangement is a lease at inception of the contract. Right of use assets represent the Health System's right to use the underlying assets for the lease term and lease liabilities represent the Health System's obligation to make lease payments arising from the leases. Right of use assets and lease liabilities are recognized at commencement date based on the present value of lease payments over the lease term. The Health System uses an estimated incremental borrowing rate, which is derived from information available at the lease commencement date, in determining the present value of lease payments. The Health System determines this rate based on information obtained from its bankers, its secured debt fair value and publicly available data for instruments with similar characteristics.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES - Continued

The Health System's operating leases are primarily for real estate, including off-campus outpatient facilities, medical office buildings, and corporate and other administrative offices, as well as medical and office equipment. Finance leases are for medical equipment. The real estate lease agreements typically have initial terms of five to ten years, and equipment lease agreements typically have initial terms of three to five years. The Health System does not record leases with an initial term of 12 months or less ("short-term leases") in its consolidated balance sheets.

The Health System's real estate leases may include one or more options to renew, with renewals that typically can extend the lease term from five to ten years. The exercise of lease renewal options is at the Health System's sole discretion. In general, the Health System does not consider renewal options to be reasonably likely to be exercised, therefore, renewal options are generally not recognized as part of right of use assets and lease liabilities. The useful life of assets and leasehold improvements are limited by the expected lease term, unless there is a transfer of title or purchase option reasonably certain of exercise. The majority of the medical equipment leases have terms of three years with no renewal options or bargain purchase options, so these assets are depreciated over their lease term.

Certain of the Health System's lease agreements for real estate include payments based on actual common area maintenance expenses. These variable lease payments are recognized in other operating expenses, net, but are not included in the right-of-use asset or liability balances. The Health System's lease agreements do not contain any material residual value guarantees, restrictions or covenants.

Other Intangibles

For the year ended June 30, 2020, the Health System added intangibles of \$2,600 related to a trade name. At June 30, 2020, the amount of this intangible is \$2,295 net of accumulated amortization of \$305 and is included in other assets in the consolidated balance sheet.

Other Assets

Other assets are comprised of:

	June 30,	
	2020	2019
Investments in unconsolidated joint ventures (Note 10)	\$ 18,093	\$ 9,416
Right to use assets (Note 13)	8,477	-
Reinsurance receivable (Note 15)	10,408	5,957
Contributions receivable, net (Note 16)	1,875	1,431
Other	4,802	4,304
Total	\$ 43,655	\$ 21,108

Estimated Self-Insurance Liabilities

The provision for estimated professional liability claims, general liability claims, and workers' compensation claims includes estimates of the ultimate costs for both reported claims and claims incurred but not reported.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES - Continued

Net Assets with Donor Restrictions

Certain net assets are temporarily restricted and whose use has been limited by donors to a specific time period or purpose.

Certain net assets have been permanently restricted by donors to be maintained by the Health System in perpetuity.

Performance Indicator

The performance indicator for the Health System is excess of revenue over expenses, which excludes net assets released from restrictions for property acquisitions net of transfers to restricted net assets, changes in non-controlling interest, and other changes in accrued retirement benefits.

Donor-Restricted Gifts

Unconditional promises to give cash and other assets 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 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 the purpose of the restriction is accomplished, net assets with donor restrictions are reclassified as net assets without donor restrictions and reported on the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as contributions in net assets without donor restrictions in the accompanying consolidated financial statements.

Patient Service Revenue

The Health System has the following agreements for patient services: for those provided at the PRMC hospital campus, all payors are required to pay the Maryland Health Services Cost Review Commission ("HSCRC") approved rates; and for all other locations, patient services are based on negotiated agreements with third-party payors, including health insurance companies and rates set by government regulations (for payors such as Medicare and Medicaid) that provide for reimbursement at amounts different from established charges. Reimbursement methodologies include prospectively determined rates per discharge, per diem rates, reimbursed costs, and discounted charges.

Patient service revenues are recorded at the amounts that reflect the consideration to which the Health System expects to be entitled to in exchange for providing patient care for both the hospital and any employed physicians. These amounts are due from patients, third-party payors (including managed care organizations and government programs, i.e., Medicare and Medicaid), and others and they include variable consideration for retroactive adjustments due to settlement of future audits, reviews, and investigations. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations. Generally, patients and third-party payors are billed several days after the services are performed or shortly after discharge. Patient service revenue is recognized in the period in which the performance obligations are satisfied under contracts by transferring services to patients.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES - Continued

Performance obligations are determined based on the nature of the services provided. The Health System recognizes revenues for performance obligations satisfied over time based on actual charges incurred in relation to total expected charges. The Health System believes that this method provides an appropriate depiction of the transfer of services over the term of performance obligations based on the inputs needed to satisfy the obligations. Generally, performance obligations are satisfied over time related to patients receiving inpatient acute care services. The Health System measures performance obligations from admission to the point when there are no further services required for the patient, which is generally the time of discharge. The Health System recognizes revenues for performance obligations satisfied at a point in time, which generally relate to patients receiving outpatient services, when: (1) services are provided; and (2) when it is believed the patient does not require additional services.

The Health System determines estimates of contractual adjustments and discounts based on government regulations, contractual agreements, discount policies and historical experience, as applicable. The Health System determines its estimate of implicit price concessions based on historical collection experience within each class of patients using a portfolio approach as a practical expedient to account for patient contracts as collective groups rather than individually. The consolidated financial statement effects of using this practical expedient are not materially different from an individual contract approach.

Advertising Costs

The Health System expenses advertising costs as incurred. For the years ended June 30, 2020 and 2019, the Health System incurred advertising costs of \$1,731 and \$945, respectively, which are included in supplies and other expenses in the accompanying consolidated statements of operations and changes in net assets.

Income Taxes

PRHS, the Foundation, the McCready Foundation, Inc., the Nursing Home, and the Rehab Center have been recognized as supporting organizations exempt from federal income tax under Section 501(c)(3) as described in Sections 509(a)(3) of the Internal Revenue Code (the "Code"). PRMC, NMH, and NPN have been recognized as organizations exempt from federal income tax under Section 501(c)(3) as described in Section 509(a)(1) and Section 170(b)(1)(A)(iii) of the Code. The Health System is subject to tax on income unrelated to its exempt purpose, unless that income is otherwise excluded by the Code. Each organization has processes presently in place to ensure the maintenance of its tax-exempt status; to identify and report unrelated income; to determine its filing and tax obligations in jurisdictions for which it has nexus; and to identify and evaluate other matters that may be considered tax positions.

Peninsula Women's Center, LLC and Peninsula Regional Clinically Integrated Network, LLC, are limited liability companies with the Health System as sole member and are disregarded for income tax purposes. Health Ventures is a for-profit corporation, wholly owned by the Health System. DPIC is a Cayman Island captive insurance company. Under Cayman Islands tax regulations, no tax is imposed on DPIC for premium and investment income.

The Health System follows guidance that clarifies the accounting for uncertainty in tax positions taken or expected to be taken in a tax return, including issues relating to financial statement recognition and measurement. This guidance provides that the tax effects from an uncertain tax position can only be recognized in the financial statements if the position is "more-likely-than-not" to be sustained if the position were to be challenged by a taxing authority. The assessment of the tax position is based solely on the technical merits of the position, without regard to the likelihood that the tax position may be challenged.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES - Continued

The tax years ending June 30, 2020, 2019 and 2018 are still open to audit for both federal and state purposes. The Health System has determined that there are no material uncertain tax positions that require recognition or disclosure in the consolidated financial statements for the years ended June 30, 2020 and 2019.

Pending Accounting Pronouncement

Goodwill Impairment

In January 2017, FASB issued ASU 2017-04, *Intangibles - Goodwill and Other - Simplifying the Test of Goodwill Impairment*. This guidance eliminates Step 2 from the goodwill impairment test. The guidance also eliminates the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The guidance is effective for fiscal years beginning after December 15, 2020. Early adoption is permitted for impairment tests after January 1, 2017. ASU 2017-04 will be adopted on a prospective basis. The Health System is evaluating the impact of ASU 2017-04 at this time.

Reclassifications

Certain amounts in the prior-year consolidated financial statements have been reclassified to be consistent with the current-year presentation.

NOTE 3 - IMPACT OF THE COVID-19 PANDEMIC

In March 2020, the World Health Organization declared COVID-19, the disease caused by the novel coronavirus, a pandemic, which started to and continues to spread throughout the United States of America. As a result of the COVID-19 pandemic, the Health System experienced a decline in patient visits, admissions, and medical procedures performed. Elective medical procedures were suspended by state and local governments at varying time periods beginning in mid-March through late May 2020, contributing to a significant decline in patient service revenue due to COVID-19 when compared to historic and forecasted results for that period. Additionally, in response to the pandemic, the Health System incurred additional costs for testing, personal protective equipment, third-party contract services and other operating costs associated with ensuring employee and patient safety while operating during a pandemic. Since late May, the Health System has begun to see increases in its patient visits, admissions, and medical procedures, however volumes have not returned to pre-pandemic levels. Management is actively monitoring operating revenues, and expenses and based on the continuing uncertainties of COVID-19, it is unable to determine if it will have a material impact on its operations for the year ending June 30, 2021.

The Health System received grant payments, which are considered nonexchange transactions, from the federal government distributed under the Coronavirus Aid, Recovery and Economic Security ("CARES") Act. For the year ended June 30, 2020, payments received of \$24,075 are included in other revenue in the statement of operations and changes in net assets. These payments are subject to audit and compliance with federal regulations. While the federal regulations have not been finalized as of October 28, 2020, the Health System believes it has met the conditions to retain these funds, and no amounts are reserved for repayment at June 30, 2020 in the accompanying consolidated balance sheet. During July 2020, the Health System received additional grant payments under the CARES Act in the amount of \$24,449. Future grant payments are uncertain at this time.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 3 - IMPACT OF THE COVID-19 PANDEMIC - Continued

The CARES Act also provided for an expansion of the Medicare Accelerated and Advance Payment Program for patient services. Under the program, the Health System received \$123,055 in April 2020, and recorded these payments in estimated settlements due to third-party payors in the consolidated balance sheet. Prior to the beginning of the recoupment period (which begins 29 months from the date of the first advance payment was issued), the Health System continued to bill for services provided to Medicare patients and was paid by Medicare, as usual. Once the recoupment period begins, amounts billed to Medicare for services provided will be offset against the advance payments received until the advance is fully recouped by the Medicare program. During the first 11 months when such payment offsets are made, a total of 25% of the amount will be due; during the succeeding 6 months, 50% of the amount will be due; and the Health System will have 29 months before the outstanding balance will be required to be paid in full. If the advance has not been entirely offset by claims at the end of this period, the Health System will be required to repay the remaining amount.

NOTE 4 - ACQUISITIONS

In 2020, PRHS made acquisitions as describe in Note 1 by means of inherent contributions where no consideration was transferred by PRHS. The Health System accounted for these business combinations by applying the acquisition method and, accordingly, the inherent contributions received were valued as the excess of assets acquired over liabilities assumed. In determining each acquisitions inherent contribution received, all assets acquired and liabilities assumed were measured at fair value as of the respective acquisition dates. The results of the operations of each acquisition have been included in the accompanying consolidated financial statements since the respective acquisition dates.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 4 - ACQUISITIONS - Continued

The estimated fair values of the assets acquired and liabilities assumed at the acquisition date are as follows:

	Nanticoke	McCready
	At January 1, 2020	At March 1, 2020
Assets		
Cash and cash equivalents	\$ 5,385	\$ 636
Patient accounts receivable	16,648	3,222
Supplies	4,198	127
Prepaid and other	4,412	271
Investments and assets limited as to use	54,082	-
Property and equipment	91,489	12,726
Other assets	6,364	198
Total assets acquired	<u>182,578</u>	<u>17,180</u>
Liabilities		
Accounts payable	7,580	448
Accrued liabilities	7,840	1,058
Self-insurance liabilities	8,290	426
Long-term debt	47,629	9,088
Lease liability	3,328	-
Accrued retirement benefits	2,788	-
Total liabilities assumed	<u>77,455</u>	<u>11,020</u>
Net assets acquired		
Net assets without donor restrictions	<u>105,123</u>	<u>6,160</u>
Excess of assets acquired over liabilities assumed	<u>\$ 105,123</u>	<u>\$ 6,160</u>

The following are the results of the acquisitions from the date of acquisition that have been included in the consolidated statement of operations and changes in net assets for the year ended June 30, 2020:

	Nanticoke	McCready
	At January 1, 2020	At March 1, 2020
Total revenues	\$ 78,806	\$ 2,621
Excess of revenues over expenses	\$ 85,191	\$ 6,448
Increase (decrease) in net assets without donor restrictions	\$ 93,166	\$ (14)
Increase (decrease) in net assets	\$ 93,166	\$ (14)

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 4 - ACQUISITION - Continued

The following are the combined, unaudited pro-forma results for the years ended June 30, 2020 and 2019, respectively, as if the acquisition had occurred on July 1, 2018. The combined unaudited pro-forma financial information excludes the contribution received in the acquisitions and is not necessarily indicative of the results of operations as they would have been, had the transaction been effected on July 1, 2018:

	Combined Unaudited Pro-forma	
	Year ended June 30	
	2020	2019
Total revenues	\$ 661,827	\$ 652,532
Excess of revenues over expenses	\$ 106,085	\$ 119,624
Change in net assets:		
Without donor restrictions	\$ 106,085	\$ (7,021)

NOTE 5 - LIQUIDITY AND AVAILABILITY OF RESOURCES

As of June 30, 2020 and 2019, the adjusted working capital was \$477,856 and \$403,355, respectively, and the adjusted average days of cash on hand was 392 and 331 days, respectively, both of which include long-term investments.

In addition to cash flows provided by operating activities, the financial assets available for general expenditure within one year of the consolidated balance sheet date consist of the following:

	June 30	
	2020	2019
Cash	\$ 179,524	\$ 46,639
Short-term investments	7,528	7,919
Patient accounts receivable	57,020	41,484
Investments	415,488	344,053
	\$ 659,560	\$ 440,095

NOTE 6 - CHARITY CARE

The Health System provides care to patients who meet certain criteria under its charity care policy, without charge or at amounts less than its approved rates. Because the Health System does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

The Health System maintains records to identify and monitor the level of charity care and community service it provides. These records include the amount of charges foregone based on established rates for services and supplies furnished under its charity care and community service policies and the number of patients receiving services under these policies. The Health System provided \$12,150 and \$6,722 for the years ended June 30, 2020 and 2019, respectively, of charity care at full cost including direct and indirect costs, based on the actual charity population using its cost to charge ratio. The HSCRC includes components within the rates to partially compensate eligible providers for uncompensated care.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 6 - CHARITY CARE - Continued

Additionally, the Health System provides a wide range of community services to the general public. These include but are not limited to the following: free health screenings for breast cancer, prostate cancer, skin cancer, diabetes, high blood pressure, high blood cholesterol, hearing loss and glaucoma; free educational programs on a variety of health care topics; health fairs and demonstrations; and networking and coordination of services for the needy, elderly, and disabled. These community services are offered at the Health System and at schools, businesses, and other locations throughout the Health System's service area.

NOTE 7 - PATIENT SERVICE REVENUE

Patient service revenue recognized from major payer sources based on primary insurance designation, is as follows:

	June 30,	
	2020	2019
Medicare	52%	53%
Medicaid	18%	17%
Managed care	4%	6%
CareFirst Blue Cross Blue Shield	12%	12%
Other, including self-pay	14%	12%
	100%	100%

For services provided at the PRMC hospital campus, all payors are required to pay the Maryland Health Services Cost Review Commission ("HSCRC") approved rates. Management believes that this program will remain in effect at least through June 30, 2021. The major third-party payors, as recognized by the HSCRC, are allowed discounts of up to 7.7% on approved rates. These charges are subject to review and approval by the HSCRC. The total rate of reimbursement for services to patients under the Medicare and Medicaid programs is based on a waiver arrangement between the Centers for Medicare and Medicaid Service and the HSCRC. This waiver arrangement will be in place as long as Maryland hospitals achieve certain savings and improvements, as defined. PRMC has an agreement with the HSCRC to participate in its Global Budgeted Revenue ("GBR") program. GBR methodology encourages hospitals to focus on population health strategies by establishing a fixed annual revenue cap for each GBR hospital. The agreement is evergreen in nature and covers both regulated inpatient and outpatient revenues.

Under GBR, hospital revenue is known at the beginning of each fiscal year, and for the year ending June 30, 2021, is expected to be approximately \$511,752. Annual revenue is calculated from a base year and is adjusted annually for inflation, infrastructure requirements, population changes, performance in quality-based programs, and changes in levels of uncompensated care. Revenue may also be adjusted annually for market levels and shifts of services to unregulated services. The HSCRC's rate-setting methodology for hospital service centers that provide both inpatient and outpatient services and only outpatient services, consists of establishing an acceptable unit rate for defined inpatient and outpatient service centers within a hospital. The actual average unit charge for each service center is compared to the approved rate monthly and annually. Overcharges and undercharges due to either patient volume or price variances, adjusted for penalties where applicable, are applied to decrease (in the case of overcharges) or increase (in the case of undercharges) in future approved rates on an annual basis. PRMC undercharged for the years ended June 30, 2020 and 2019, within the allowable corridor as specified in the GBR Agreement.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 7 - PATIENT SERVICE REVENUE - Continued

The timing of the HSCRC's rate adjustments for PRMC could result in an increase or reduction in rates due to the variances and penalties described above in a year subsequent to the year in which such items occurred, and there is at least a possibility that the amounts may be material. For both the years ended June 30, 2020 and 2019, approximately 58% and 77% of patient service revenue was subject to the HSCRC's regulations.

Inpatient acute care and outpatient services not located on the PRMC hospital campus, including NMH and certain other services not regulated by the HSCRC provided to Medicare and Medicaid program beneficiaries are paid at prospectively determined rates per discharge or outpatient service. These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. Additionally, there are certain defined Medicare program pass-through items, and certain other costs provisionally reimbursed by Medicare, are paid based on a cost reimbursement methodology or tentative rate. These are ultimately subjected to certain cost limitations or contingent on actual data for the year, with final settlement determined after submission of annual cost reports by NMH and audits thereof, by the programs' fiscal intermediaries.

The NMH Medicare cost reports have been audited and finalized through June 30, 2019. Differences between the estimated settlements and the amounts settled are recorded in the year of settlement. Estimated favorable results of appeal items are recorded when realization is reasonably assured. These estimates are included in estimated settlements due to third-party payers in the consolidated balance sheets. Management uses the expected-value method when determining these amounts. In the opinion of management, adequate provision has been made for any adjustment, which may result from the final settlement of these cost reports, and any appeal issues. For the years ended June 30, 2020 and 2019, patient service revenue includes net favorable settlements and adjustments for cost reports, audit and appeal items from prior years of \$277 and \$310, respectively.

Laws and regulations governing the HSCRC, Medicare and Medicaid programs, which represent a substantial portion of the patient service revenues, are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. The Health System believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While there are no currently known regulatory inquiries, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action.

The following table sets forth the detail of patient service revenue:

	Year ended June 30,	
	2020	2019
Gross patient service revenue	\$ 792,934	\$ 593,753
Less: revenue deductions:		
Charity care	(16,356)	(8,455)
Contractual and other allowances	(225,913)	(118,854)
Implicit price concessions	(14,741)	(7,976)
Patient service revenue	\$ 535,924	\$ 458,468

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 8 - INVESTMENTS AND ASSETS LIMITED AS TO USE

Fair value of investments and assets limited as to use is summarized as follows:

	June 30,	
	2020	2019
Cash and cash equivalents	\$ 21,348	\$ 18,924
U.S. Treasury securities	152,154	46,799
Corporate bonds	115,971	89,398
Mortgage-backed securities	-	42,388
Equity securities	277,793	224,868
	<u>567,266</u>	<u>422,377</u>
Less amounts required for current liabilities	(3,149)	(3,695)
	<u>564,117</u>	<u>418,682</u>
Total	\$ 564,117	\$ 418,682
	Year ended June 30,	
	2020	2019
Investment return		
Interest and dividend income	\$ 11,545	\$ 7,132
Realized gains, net	14,484	28,524
Changes in unrealized gains and losses	8,437	(1,231)
Other	(1,455)	(481)
	<u>33,011</u>	<u>33,944</u>
Total	\$ 33,011	\$ 33,944

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 9 - FAIR VALUE MEASUREMENTS

U.S. GAAP establishes a 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 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below.

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

Level 2 Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets
- Quoted prices for identical or similar assets or liabilities in inactive markets
- Inputs other than quoted prices that are observable for the asset or liability
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means

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

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

The asset's 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.

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

The following tables present the Health System's assets measured at fair value, aggregated by level in the fair value hierarchy within which those measurements fall:

	June 30, 2020			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 21,348	\$ -	\$ -	\$ 21,348
U.S. government securities	119,462	32,692	-	152,154
Corporate bonds	-	115,971	-	115,971
Equity securities	277,688	105	-	277,793
Total assets	\$ 418,498	\$ 148,768	\$ -	\$ 567,266

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
 (Dollar amounts in thousands)

NOTE 9 - FAIR VALUE MEASUREMENTS - CONTINUED

	June 30, 2019			
	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents	\$ 18,924	\$ -	\$ -	\$ 18,924
U.S. government securities	46,799	-	-	46,799
Corporate bonds	-	89,398	-	89,398
Government-sponsored mortgage-backed securities	-	42,388	-	42,388
Equity securities	224,868	-	-	224,868
Total assets	\$ 290,591	\$ 131,786	\$ -	\$ 422,377

The fair values of securities are determined by third-party service providers utilizing various methods depending on the specific type of investment. Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Where significant inputs, including benchmark yields, broker-dealer quotes, issuer spreads, bids, offers, the London Interbank Offered Rate curve, and measures of volatility, are used by these third-party dealers or independent pricing services to determine fair values, the securities are classified within Level 2.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 10 - INVESTMENT IN UNCONSOLIDATED JOINT VENTURES

The Health System and physicians located throughout Maryland and Delaware have joined together, along with other non-related for-profit investors, to expand surgical and certain other services within the local communities through jointly owned ventures, as follows:

	Membership percentage	Investment in unconsolidated joint ventures		Equity earnings (losses) in unconsolidated joint ventures	
		June 30,		Year ended June 30,	
		2020	2019	2020	2019
Health System:					
Health Visions Delmarva, LLC	50%	\$ -	\$ -	\$ -	\$ (2)
Advanced Health Collaborative I, LLC	25%	-	16	(78)	(88)
Advanced Health Collaborative II, LLC	25%	67	10	(120)	(1,674)
		<u>67</u>	<u>26</u>	<u>(198)</u>	<u>(1,764)</u>
Health Ventures:					
Peninsula Imaging, LLC	50%	4,195	3,822	874	1,028
AHP Delmarva, LLP	50%	1,106	1,056	179	268
Genesis Healthcare - Salisbury, LLC	50%	4,023	3,493	531	538
Peninsula Home Care, LLC	50%	372	293	406	584
PHC at Nanticoke, LLC	33%	398	39	85	1
YDI, Inc.	50%	112	-	112	-
Corelife, Inc.	50%	652	127	(240)	(173)
Delmarva Endoscopy Center, LLC	80%	308	560	(553)	-
Deerpointe	26.3%	6,860	-	351	-
		<u>18,026</u>	<u>9,390</u>	<u>1,745</u>	<u>2,246</u>
		<u>\$ 18,093</u>	<u>\$ 9,416</u>	<u>\$ 1,547</u>	<u>\$ 482</u>

Regardless of the proportionate ownership of capital investment in these ventures, all decisions are made by the respective venture's operating board. In each case, the operating board is composed equally of members appointed by the Health System/Health Ventures and the other investors as a group. Accordingly, these are accounted for on the equity method of accounting.

Equity earnings (losses) in unconsolidated joint ventures for the Health System are included in investment return and Health Ventures are included in other revenue on the consolidated statements of operations and changes in net assets, due to the type of operations of the joint venture.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
 (Dollar amounts in thousands)

NOTE 11 - PROPERTY AND EQUIPMENT

A summary of property and equipment follows:

	Estimated useful lives (in years)	June 30,	
		2020	2019
Land	-	\$ 18,872	\$ 12,772
Land improvements	20	13,814	11,944
Buildings and improvements	15 - 40	346,184	265,973
Fixed equipment	20	41,965	37,115
Movable equipment	5 - 7	283,697	261,292
		704,532	589,096
Less accumulated depreciation and amortization		(401,044)	(371,482)
		303,488	217,614
Construction in progress		12,233	3,111
Property and equipment, net		<u>\$ 315,721</u>	<u>\$ 220,725</u>

As of June 30, 2020, the Health System was committed to building and equipment purchases totaling approximately \$14,276.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 12 - LONG-TERM DEBT

Long-term debt consists of the following:

	June 30,	
	2020	2019
Maryland Health and Higher Educational Facilities Authority ("MHHEFA") Revenue Bonds:		
Series 2020A 3.00% to 5.00% serial and term bonds and effective rates ranging from 1.90% to 4.136% due in annual amounts ranging from \$1,030 to \$13,130 on July 1 of each year through 2048	\$ 95,995	\$ -
Series 2015 5.00% serial and term bonds and effective rates ranging from 2.57% to 4.13% due in annual amounts ranging from \$2,195 to \$7,795 on July 1 of each year through 2045	115,380	117,685
Delaware Economic Development Authority Strategic Fund Loan, maturing in varying annual amounts through 2023, no stated interest rate	1,433	-
United States Department of Agriculture ("USDA") - Second mortgage - \$6,000 dated June 4, 2009 bearing interest at 4.25%, amortized over 40 years with the final installment due June 4, 2049. The purpose of the loan is to construct the new nursing home. The collateral includes all assets of the McCready Foundation, Inc.	5,259	-
The Bank of Delmarva - Third mortgage - \$4,000 dated June 4, 2009 bearing interest at the rate of prime minus one-half percent (-.50%) as defined and will change every 60 months beginning June 2016; it is understood and agreed, by and between the parties hereto, that the interest rate set forth herein shall, in no event, be less than 6.50%, nor greater than 9.75%, for the life of the loan. The interest rate is 6.50% at June 30, 2020. Principal and interest are due monthly through the due date of June 4, 2041. This loan is guaranteed by the USDA. The collateral includes all assets of the McCready Foundation, Inc.	3,205	-
Building and equipment collateral loans, with interest rates ranging from 3.67% to 4.40% fixed rate due monthly through 2022	182	1,527
Financing leases, with various interest rates, secured by related equipment	1,236	-
	222,690	119,212
Less: current portion of long-term debt	(4,671)	(2,394)
	218,019	116,818
Plus: original issue premiums, net	22,147	17,109
Less: unamortized debt issue costs, net	(2,737)	(1,191)
Long-term debt, less current portion	\$ 237,429	\$ 132,736

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 12 - LONG-TERM DEBT - Continued

Series 2020A Revenue Bonds

In May 2015, MHHEFA authorized the issuance of \$95,995 aggregate principal amount of Revenue Bonds (Series 2020A Revenue Bonds) at a premium of \$5,944. The proceeds of the issue, after payment of financing costs, were used primarily; (i) to advance refund NMH debt obligations with the USDA and the 2013 Delaware Health and Facilities Authority Bonds; and (ii) to finance \$58,500 of capital purchases. The advance refunding generated a loss on extinguishment of debt of \$4,142, consisting of the call premium and the write off of the original issue premium and costs of issuance.

Series 2015 Revenue Bonds

In February 2015, MHHEFA authorized the issuance of \$126,665 aggregate principal amount of Revenue Bonds (Series 2015 Revenue Bonds) at a premium of \$20,770. The proceeds of the issue, after payment of financing costs, were used primarily; (i) to advance the 2006 bonds and; (ii) to finance \$25,000 of capital purchases.

Covenants

The Obligated Group for the 2020A and 2015 Bonds (collectively the Bonds), consists of PRHS, PRMC, NMH and NPN, is required to make semiannual payments to the trustee sufficient to meet the annual debt service requirements. The premiums and related financing costs on the Bonds are being amortized over the life of the bonds.

As security for the debt service requirements of the Bonds, MHHEFA has a first lien and claim on all receipts of the Obligated Group. The terms of the indenture agreement restrict the Obligated Group's ability to create additional indebtedness and its use of the facilities and require the Obligated Group to maintain stipulated insurance coverage and a rate structure in each year sufficient to meet certain rate covenant requirements. The Obligated Group has complied with these financial covenants for the years ended June 30, 2020 and 2019.

Scheduled principal repayments on long-term debt for the years ending June 30, are as follows:

2021	\$	4,671
2022		4,676
2023		4,594
2024		4,674
2025		4,800
Thereafter		<u>199,275</u>
	\$	<u>222,690</u>

Fair Value

The Health System uses quoted market prices in estimating the fair value of its long-term debt, excluding financing leases. The fair value of the long-term debt, excluding financing leases outstanding as of June 30, 2020 and 2019, was approximately \$240,229 and \$132,148, respectively.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 13 - LEASES

The following table presents the components of the Health System's right of use assets and liabilities related to leases and their classification as of June 30, 2020:

<u>Component of lease balances</u>	<u>Classification in consolidated balance sheet</u>	<u>2020</u>
Assets		
Operating lease assets	Other assets	\$ 8,477
Finance lease assets	Property and equipment, net	<u>777</u>
Total leased assets		<u>\$ 9,253</u>
Liabilities		
Operating lease liabilities		
Current	Current portion of lease liability	\$ 1,932
Long-term	Lease liability, less current portion	<u>6,628</u>
Total operating lease liabilities		<u>8,560</u>
Finance lease liabilities		
Current	Current portion of long-term debt	566
Long-term	Long-term debt, less current portion	<u>670</u>
Total finance lease liabilities		<u>1,236</u>
Total lease liabilities		<u>\$ 9,796</u>

The following table presents the components of lease expense and their classification in the consolidated statement of operations and changes in net assets for the year ended June 30, 2020:

<u>Component of lease balances</u>	<u>Classification in consolidated statement of operations and changes in net assets</u>	<u>2020</u>
Operating lease expense	Supplies and other	\$ 2,957
Finance lease expense:		
Amortization of leased assets	Depreciation and amortization	202
Interest on lease liabilities	Interest	<u>26</u>
Total finance lease expense		228
Variable and short-term lease expense	Supplies and other	<u>2,659</u>
Total lease expense		<u>\$ 5,844</u>

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 13 - LEASES - Continued

The weighted-average lease terms and discount rates for operating and finance leases at June 30, 2020 is as follows:

	2020
Weighted-average remaining lease term (years)	
Operating leases	6.81 years
Finance leases	2.70 years
Weighted-average discount rate	
Operating leases	2.59%
Finance leases	3.71%

Cash flow related to leases for the year ended June 30, 2020 is as follows:

	2020
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash outflows from operating leases	\$ 2,957
Operating cash outflows from finance leases	\$ 26
Financing cash outflows from finance leases	\$ 995

The future minimum rental commitments for all noncancelable operating and finance leases as of June 30, 2020 are as follows:

	Operating leases	Finance leases	Total
Years ending June 30,			
2021	\$ 2,100	\$ 612	\$ 2,712
2022	1,868	408	2,276
2023	1,427	225	1,652
2024	1,215	131	1,346
2025	744	-	744
Thereafter	2,419	-	2,419
Total lease payments	9,773	1,376	11,149
Less: Imputed interest	(1,213)	(140)	(1,353)
Lease liability	\$ 8,560	\$ 1,236	\$ 9,796

Prior to the adoption of ASU 2016-02, *Leases*, rent expense for operating lease agreements for the year ended June 30, 2019 totaled \$2,635.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019

(Dollar amounts in thousands)

NOTE 14 - RETIREMENT BENEFIT PLANS

Defined Benefit Plans

The Health System has a cash balance-type defined benefit pension plan, The Peninsula Regional Medical Center Pension Plus Plan (the "Plan"), covering substantially all of its employees. The Plan was remeasured on January 1, 2020, due to the significant amount of new participants entering the Plan as a result of the acquisition of Nanticoke. Plan benefits are based on years of service and the employees' compensation during the last five years of covered employment. The Health System's funding policy is to make sufficient contributions to the Plan to comply with the minimum funding provisions of the Employee Retirement Income Security Act of 1974. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

The Plan provides annual allocations to a participant's hypothetical account. When a participant retires, the participant has the choice to receive a lump-sum distribution equal to the value of the hypothetical account or to receive an annuity based on the value of the hypothetical account.

The Plan provided three different allocations: (i) a service-related allocation; (ii) an age-related allocation, and (iii) a matching allocation for certain employees. Both the service-related allocation and the age-related allocation were determined by multiplying a participant's annual compensation by a certain percentage. The matching allocation operated to provide an annual allocation in the Plan based on the participant's contribution to the Health System's 403(b) plan.

NHM has a qualified noncontributory defined benefit pension plan (the "NMH Plan") that was frozen effective January 1, 2009. The funding policy is to make sufficient contributions to comply with the minimum funding requirements of the Employee Retirement Income Security Act (ERISA).

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 14 - RETIREMENT BENEFIT PLANS - Continued

The following provides a reconciliation of the changes in the projected benefit obligations and the fair value of plans assets, and plans funded status:

	June 30		
	2020 The Plan	2020 NMH Plan	2019 The Plan
Accumulated benefit obligation	\$ 153,558	\$ 22,200	\$ 123,227
Projected benefit obligation, beginning of year	\$ 148,914	\$ 20,472	\$ 131,111
Service cost	9,854	-	6,506
Interest cost	4,530	599	5,086
Actuarial gain	13,647	3,191	10,746
Benefits paid	(7,160)	(2,062)	(4,534)
Projected benefit obligation, end of year	169,785	22,200	148,915
Fair value of plan assets, beginning of year	148,760	20,306	136,288
Actual gain on plan assets	15,085	227	14,006
Employer contributions	-	-	3,000
Benefits paid	(7,160)	(2,062)	(4,534)
Fair value of plan assets, end of year	156,685	18,471	148,760
Funded status	\$ (13,100)	\$ (3,729)	\$ (155)
Amounts recognized in the consolidated balance sheets:			
Accrued retirement benefits	\$ (13,100)	\$ (3,729)	\$ (155)
Net amounts recognized in net assets without donor restrictions:			
Net actuarial loss	\$ 27,161	\$ 2,861	\$ 21,078

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 14 - RETIREMENT BENEFIT PLANS - Continued

Components of net periodic benefit cost and changes in net asset without donor restrictions are as follows:

	Year ended June 30,		
	2020 The Plan	2020 NMH Plan	2019 The Plan
Components of net periodic benefit cost recognized in employee benefits:			
Service cost	\$ 9,854	\$ -	\$ 6,506
Components of net periodic benefit cost recognized in other items:			
Interest cost	4,530	240	5,086
Expected return on plan assets	(9,083)	(626)	(8,915)
Recognized net actuarial loss	1,562	-	1,001
	<u>(2,991)</u>	<u>(386)</u>	<u>(2,828)</u>
Net periodic benefit cost (gain)	6,863	(386)	3,678
Recognized in net assets without donor restrictions as other changes in other changes in accrued retirement benefits:			
Net actuarial loss	<u>(6,082)</u>	<u>(2,861)</u>	<u>(4,654)</u>
Total recognized in net periodic benefit cost and change in net assets without donor restrictions	<u>\$ (12,945)</u>	<u>\$ (2,475)</u>	<u>\$ (8,332)</u>

The estimated net actuarial loss for the Plan and NMH Plan that will be amortized from net assets without donor restrictions into net periodic benefit cost over the next fiscal year is \$1,662 and \$53, respectively.

Weighted average assumptions used to determine projected benefit obligations and net periodic benefit costs were as follows:

	June 30,		
	2020 The Plan	2020 NMH Plan	2019 The Plan
Projected benefit obligation			
Discount rate	2.35%	1.50%	3.25%
Rates of increase in compensation levels:			
Service:			
<11	8.00	N/A	8.00
11<21	5.00	N/A	5.00
21=<	3.00	N/A	3.00

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 14 - RETIREMENT BENEFIT PLANS - Continued

	June 30,		
	2020	2020	2019
	The Plan	NMH Plan	The Plan
Net periodic benefit cost			
Discount rate (July 1 st)	3.25%	N/A	4.00%
Discount rate (January 1 st)	3.00%	3.75%	N/A
Expected long-term return on plan assets	6.75	6.50	7.00
Rate of increase in compensation levels:			
Service:			
<11	8.00	N/A	8.00
11<21	5.00	N/A	5.00
21=<	3.00	N/A	3.00

The defined benefit pension plan asset allocation as of the measurement date and the target asset allocation, presented as a percentage of total plan assets, were as follows:

	2020	2020	2019	Target allocations
	The Plan	NMH Plan	The Plan	
Debt securities	40%	48%	40%	25% - 50%
Equity securities	57	52	57	45% - 75%
Cash and cash equivalents	3	-	3	1% - 10%
Total	100%	100%	100%	

The Health System's defined benefit plan invests in a diversified mix of traditional asset classes. Investments in U.S. equity securities and fixed income securities are made to maximize long-term results while recognizing the need for adequate liquidity to meet ongoing benefit and administrative obligations. Risk tolerance of unexpected investment and actuarial outcomes is continually evaluated by understanding the pension plan's liability characteristics. This is performed through forecasting and assessing ranges of investment outcomes over short-term and long-term horizons, and by assessing the Health System's financial condition and its future potential obligations from both the pension and general operational requirements. Complementary investment styles, such as growth and value equity investing techniques, are utilized by the Health System's investment advisors to further improve portfolio and operational risk characteristics. Equity investments, both actively and passively managed, are used primarily to increase overall plan returns. Fixed income investments provide diversification benefits and liability hedging attributes that are desirable, especially in falling interest rate environments.

Asset allocations and investment performance are formally reviewed at regularly scheduled meetings of the Health System's Financial Resources Committee.

The overall rate of expected return on assets assumption was based on historical returns, with adjustments made to reflect expectations of future returns. The extent to which the future expectations were recognized included the target rates of return for the future, which have not historically changed.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 14 - RETIREMENT BENEFIT PLANS - Continued

The fair values of assets as of June 30, by asset category (see Note 10 for a description of the asset categories), are as follows:

	June 30, 2020			
	Level 1	Level 2	Level 3	Total
Assets - The Plan				
Investments at fair value:				
Cash and cash equivalents	\$ 2,067	\$ -	\$ -	\$ 2,067
U.S. Treasuries	23,415	-	-	23,415
Government-sponsored mortgage-backed securities	-	5,321	-	5,321
Corporate debt securities	-	28,998	-	28,998
Publicly traded equity securities	96,490	-	-	96,490
Other	394	-	-	394
Total	<u>\$ 122,366</u>	<u>\$ 34,319</u>	<u>\$ -</u>	<u>\$ 156,685</u>
	June 30, 2020			
	Level 1	Level 2	Level 3	Total
Assets - NMH Plan				
Investments at fair value:				
Publicly traded equity securities	\$ 18,471	-	-	\$ 18,471
Total	<u>\$ 18,471</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 18,471</u>
	June 30, 2019			
	Level 1	Level 2	Level 3	Total
Assets - The Plan				
Investments at fair value:				
Cash and cash equivalents	\$ 3,033	\$ -	\$ -	\$ 3,033
U.S. Treasuries	17,071	-	-	17,071
Government-sponsored mortgage-backed securities	-	10,347	-	10,347
Corporate debt securities	-	32,654	-	32,654
Publicly traded equity securities	85,186	-	-	85,186
Other	469	-	-	469
Total	<u>\$ 105,759</u>	<u>\$ 43,001</u>	<u>\$ -</u>	<u>\$ 148,760</u>

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 14 - RETIREMENT BENEFIT PLANS - Continued

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

U.S. Treasuries: The fair value is determined by an active price for an identical security in an observable market.

Corporate debt securities and government-sponsored mortgage-backed securities: The fair value is estimated using quoted prices for similar assets in active markets or quoted prices for identical or similar assets in non-active markets (few transactions, limited information, noncurrent prices, and high variability over time).

Money market funds: The carrying value of these money market funds approximates fair value as the maturities are less than three months.

Publicly traded equity securities: The fair value is determined by market quotes for an identical security in an observable market.

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

Cash Flows

The Health System intends to make voluntary contributions of \$3,000 and none to the Plan and NMH Plan, respectively, for the year ending June 30, 2021. This funding level exceeds any regulatory requirements for 2021.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows for the years ending June 30:

	The Plan	NMH Plan
2021	\$ 9,910	\$ 2,548
2022	10,447	1,432
2023	10,928	1,597
2024	11,580	1,045
2025	12,304	1,486
2026 - 2030	65,175	7,776

Defined Contribution Plans

The Health System has a 403(b) defined contribution savings plan that includes all full-time and part-time employees of the Health System. The Health System matches participant contributions for active participants as of December 31 who have completed at least 975 hours of service during the calendar year. The match is 25% of the first 1% of compensation for participants with 1 - 15 years of service and 50% of the first 2% for participants with more than 15 years of service. The Health System's contribution expense for the years ended June 30, 2020 and 2019 was \$1,717 and \$1,333, respectively.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 15 - COMMITMENTS AND CONTINGENCIES

Self-Insurance Liabilities and litigation

DPIC provides Primary Medical Professional Liability (“MPL”) and Primary General Liability (“GL”) coverage to the Health System and its employed physicians on a mature claims-made basis. The primary MPL policy provides limits of liability of \$2,000 per occurrence with an \$8,000 annual aggregate. The primary GL policy provides limits of liability of \$1,000 per occurrence with a \$3,000 annual aggregate. The employed physicians are covered with retro dates consistent with their date of hire. This policy is retrospectively rated.

DPIC provides excess umbrella liability coverage on a mature claims-made basis with a retroactive date of March 1, 2005. The excess MPL coverage follows the form of the underlying MPL coverage providing a total of \$30,000 limits of liability. The umbrella liability coverage provides \$30,000 limits of liability in excess of scheduled underlying coverages. The excess umbrella liability coverage is 100% reinsured with an unrelated commercial insurance company for the first \$10,000 limit and another unrelated commercial insurance company for the second \$20,000 limit.

DPIC assumed the MPL and GL coverage previously included under the Health System’s self-insurance plan (the “LPT”), for incidents occurring between March 1, 1986 and June 30, 2013 for MPL and for occurrences between March 1, 2004 and June 30, 2013 for GL, that were reported to the Hospital prior to June 30, 2013. The policy provides MPL coverage limits varying from \$1,000 to \$2,000 per occurrence, with policy aggregates varying from \$3,000 to \$8,000. The policy provides GL coverage limits of \$1,000 per occurrence and \$3,000 annual aggregates.

DPIC also provides employee benefit plan stop loss coverage to the Health System on a claims-made basis. DPIC covers liability in excess of \$350 per covered person with a \$100 deductible. DPIC’s liability above \$250 is fully reinsured with an unrelated commercial reinsurance company.

The reserves for reported professional liability claims and claims incurred but not reported (“IBNR”) are reported gross of expected insurance recoveries. The reserves for reported claims and claims IBNR are reported within the self-insured liabilities in the consolidated balance sheets. In addition, the expected insurance recoveries are reported as reinsurance receivable in other assets in the consolidated balance sheets.

The loss reserves are management’s best estimate based on actuarial estimates of the ultimate net cost of settling losses on incurred claims. The estimates are reviewed and adjusted, as necessary, as experience develops or new information becomes known. Management believes that the loss reserves are adequate; however, the ultimate settlement of losses may vary significantly from the amounts recorded in the accompanying consolidated financial statements.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 15 - COMMITMENTS AND CONTINGENCIES - Continued

Accrued claims activity related to MPL, GL and employee benefit plan, is as follows:

	Year ended June 30,	
	2020	2019
Accrued claims and IBNR - beginning of the year	\$ 16,375	\$ 17,274
Less: reinsurance receivable	(5,957)	(5,942)
Accrued claims and IBNR, net - beginning of the year	10,418	11,332
Liabilities assumed from NIC acquisition, net of reinsurance recoverable of \$1,773 at January 1, 2020	3,712	-
Incurred related to:		
Current year	3,420	2,500
Prior year	(846)	(1,723)
Total incurred	2,574	777
Paid related to:		
Current year	(62)	6
Prior year	(1,116)	(1,697)
Total paid	(1,177)	(1,691)
Accrued claims and IBNR, net - end of the year	15,528	10,418
Deduct: write-off of loss recoverable related to prior years	(606)	-
Add: reinsurance receivable	10,408	5,957
Accrued claims and IBNR - end of the year	\$ 25,329	\$ 16,375

The Health System is also self-insured for workers' compensation up to an annual limit of \$500 per occurrence. The Health System carries an excess liability insurance policy for workers' compensation claims above this limit. As of June 30, 2020 and 2019, \$3,891 and \$3,788, respectively, have been reserved for workers' compensation loss contingencies.

The Health System has been named as a defendant in various lawsuits arising from the performance of its normal activities. In the opinion of the Health System's management, after discussion with legal counsel, the amount, if any, of the Health System's ultimate liability under these lawsuits will not have a material adverse effect on the consolidated financial statements.

A portion of the Health System's revenues is received from health maintenance organizations and other managed care payors. Managed care payors generally use case management activities to control utilization. These payors also have the ability to select providers offering the most cost-effective care. Management does not believe that the Health System has undue exposure to any one managed care payor.

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 16 - NET ASSETS WITH DONOR RESTRICTIONS

Restricted net assets are available for the following purposes:

	June 30	
	2020	2019
Subject to expenditure for specific purpose or time:		
Capital purposes	\$ 23,448	\$ 20,608
Patient services	15,804	13,869
Educational purposes	4,699	4,301
	43,951	38,778
Investments to be held in perpetuity, the income from which is expendable to support health care services	8,533	8,245
	\$ 52,484	\$ 47,023
Total	\$ 52,484	\$ 47,023

The Foundation has ongoing fundraising campaigns, which include pledges and contributions receivable included in other assets on the consolidated balance sheets. Scheduled payments on pledges receivable are as follows:

	2020	2019
Due:		
Within one year	\$ 432	\$ 219
2 to 5 years	1,619	1,204
Greater than 5 years	101	205
	2,152	1,628
Less:		
Impact of discounting of pledges receivable to net present value	(62)	(60)
Allowance for uncollectible pledges	(215)	(137)
	\$ 1,875	\$ 1,431
Net pledges receivable, for capital purposes	\$ 1,875	\$ 1,431

NOTE 17 - CONCENTRATIONS OF CREDIT RISK

The Health System grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payer agreements. The mix of accounts receivable from patients and third-party payers is as follows:

	June 30	
	2020	2019
Medicare	52%	53%
Medicaid	19	17
Managed care	14	16
CareFirst Blue Cross Blue Shield	12	12
Other, including self-pay	3	2
	100%	100%
	100%	100%

Peninsula Regional Health System, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

June 30, 2020 and 2019
(Dollar amounts in thousands)

NOTE 18 - FUNCTIONAL EXPENSES

The Health System considers health care services and general and administrative to be its primary functional categories for purposes of expense classification. The operating expenses by functional classification:

	Year ended June 30, 2020		
	Health care services	General and administrative	Total
Salaries and wages	\$ 213,745	\$ 22,116	\$ 235,861
Supplies and other expenses	230,795	23,974	254,769
Employee benefits	50,839	5,515	56,354
Depreciation and amortization	32,000	3,277	35,277
Interest	5,889	603	6,492
	\$ 533,268	\$ 55,485	\$ 588,753
	Year ended June 30, 2019		
	Health care services	General and administrative	Total
Salaries and wages	\$ 165,117	\$ 24,581	\$ 189,698
Supplies and other expenses	165,172	24,590	189,762
Employee benefits	40,273	5,996	46,269
Depreciation and amortization	26,335	3,921	30,256
Interest	4,535	675	5,210
	\$ 401,432	\$ 59,763	\$ 461,195

NOTE 19 - SUBSEQUENT EVENTS

The Health System has evaluated its June 30, 2020 consolidated financial statements for subsequent events through October 28, 2020, the date the consolidated financial statements were issued. Management is not aware of any subsequent events which require recognition or disclosure in the consolidated financial statements, except as noted elsewhere in the footnotes to the consolidated financial statements and as follows:

Effective September 1, 2020, Peninsula Regional Health System, Inc., changed its name to TidalHealth, Inc. The organization has experienced a lot of change and growth over the past few years with several acquisitions and is excited to unite its employees under one health system in celebration of a shared mission: to improve the health of the communities it serves.

SUPPLEMENTARY INFORMATION

Peninsula Regional Health System, Inc.

CONSOLIDATING BALANCE SHEET

June 30, 2020

(Dollar amounts in thousands)

	Peninsula Regional Medical Center	Peninsula Regional Medical Center Foundation	Peninsula Health Ventures	Peninsula Regional Clinically Integrated Network	Peninsula Surgery Center	Nanticoke Memorial Hospital	Nanticoke Physician Network	McCready Foundation	Delmarva Peninsula Insurance Company	Peninsula Regional Health System	Eliminations	Consolidated
ASSETS												
CURRENT ASSETS												
Cash and cash equivalents	\$ 131,074	\$ 1,594	\$ 3,853	\$ 1,261	\$ 9	\$ 30,960	\$ 211	\$ 4,525	\$ 6,034	\$ 3	\$ -	\$ 179,524
Short-term investments	7,528	-	-	-	-	-	-	-	-	-	-	7,528
Assets limited as to use	-	-	-	-	-	-	-	-	3,149	-	-	3,149
Intercompany receivables	8,970	-	-	-	-	-	161	-	-	39,541	(48,672)	-
Patient accounts receivable	42,591	-	222	-	48	12,004	1,510	645	-	-	-	57,020
Supplies	10,183	-	-	-	-	4,584	-	25	-	-	-	14,792
Prepays and other	10,668	-	135	-	276	2,050	14	62	-	-	-	13,205
Total current assets	211,014	1,594	4,210	1,261	333	49,598	1,896	5,257	9,183	39,544	(48,672)	275,218
INVESTMENTS	377,205	-	-	-	-	37,783	-	-	-	500	-	415,488
INVESTMENTS IN SUBSIDIARIES	-	-	-	-	-	-	-	-	-	681,519	(681,519)	-
ASSETS LIMITED AS TO USE												
Under debt agreement	-	-	-	-	-	-	-	-	-	58,609	-	58,609
Self-insurance fund	5,354	-	-	-	-	-	-	-	28,074	-	-	33,428
Donor-restricted fund	49,064	7,611	-	-	-	-	-	-	-	-	(7,611)	49,064
	54,418	7,611	-	-	-	-	-	-	28,074	58,609	(7,611)	141,101
PROPERTY AND EQUIPMENT, net	208,314	-	3,800	-	1,447	89,350	369	12,441	-	-	-	315,721
OTHER ASSETS	9,381	-	18,559	-	-	2,741	2,077	207	10,623	67	-	43,655
Total assets	\$ 860,332	\$ 9,205	\$ 26,569	\$ 1,261	\$ 1,780	\$ 179,472	\$ 4,342	\$ 17,905	\$ 47,880	\$ 780,239	\$ (737,802)	\$ 1,191,183

Peninsula Regional Health System, Inc.
CONSOLIDATING BALANCE SHEET - CONTINUED

June 30, 2020
(Dollar amounts in thousands)

	Peninsula Regional Medical Center	Peninsula Regional Medical Center Foundation	Peninsula Health Ventures	Peninsula Regional Clinically Integrated Network	Peninsula Surgery Center	Nanticoke Memorial Hospital	Nanticoke Physician Network	McCready Foundation	Delmarva Peninsula Insurance Company	Peninsula Regional Health System	Eliminations	Consolidated
LIABILITIES AND NET ASSETS												
CURRENT LIABILITIES												
Current portion of long-term debt	\$ 2,486	\$ -	\$ -	\$ -	\$ -	\$ 985	\$ -	\$ 170	\$ -	\$ 1,030	\$ -	\$ 4,671
Current portion of lease liability	1,201	-	-	-	-	331	400	-	-	-	-	1,932
Current portion self-insurance liabilities	904	-	-	-	-	1,249	-	-	996	-	-	3,149
Intercompany payables	-	5	291	2,236	1,534	37,724	-	2,575	-	-	(44,365)	-
Accounts payable	20,971	-	491	-	-	12,183	294	206	92	99	(1)	34,335
Accrued liabilities	27,605	-	-	-	-	3,579	1,696	16	-	-	-	32,896
Advances from third-party payors	110,121	-	-	-	-	22,551	238	149	-	-	-	133,059
Total current liabilities	163,288	5	782	2,236	1,534	78,602	2,628	3,116	1,088	1,129	(44,366)	210,042
Long-term debt, less current portion	128,202	-	-	-	-	1,683	-	8,294	-	99,250	-	237,429
Lease liability, less current portion	4,488	-	-	-	-	461	1,679	-	-	-	-	6,628
Self insured liabilities, less current portion	3,042	-	-	-	-	826	-	-	25,329	-	-	29,197
Accrued retirement benefits	12,865	-	-	-	-	4,734	-	-	-	-	-	17,599
Other liabilities	947	44	-	-	-	-	49	242	18,904	-	(18,904)	1,282
Total liabilities	312,832	49	782	2,236	1,534	86,306	4,356	11,652	45,321	100,379	(63,270)	502,177
NET ASSETS												
Net assets without donor restrictions:												
Peninsula Regional Health System, Inc.	494,771	1,545	23,898	(975)	246	93,166	(14)	6,499	2,559	619,766	(606,828)	634,633
Non-controlling interest	-	-	1,889	-	-	-	-	-	-	-	-	1,889
Total net assets without donor restrictions	494,771	1,545	25,787	(975)	246	93,166	(14)	6,499	2,559	619,766	(606,828)	636,522
Net assets with donor restrictions	52,729	7,611	-	-	-	-	-	(246)	-	60,094	(67,704)	52,484
Total net assets	547,500	9,156	25,787	(975)	246	93,166	(14)	6,253	2,559	679,860	(674,532)	689,006
Total liabilities and net assets	\$ 860,332	\$ 9,205	\$ 26,569	\$ 1,261	\$ 1,780	\$ 179,472	\$ 4,342	\$ 17,905	\$ 47,880	\$ 780,239	\$ (737,802)	\$ 1,191,183

Peninsula Regional Health System, Inc
CONSOLIDATING STATEMENT OF OPERATIONS
Year ended June 30, 2020
(Dollar amounts in thousands)

	Peninsula Regional Medical Center	Peninsula Regional Medical Center Foundation	Peninsula Health Ventures	Peninsula Regional Clinically Integrated Network	Peninsula Surgery Center	Nanticoke Memorial Hospital	Nanticoke Physician Network	McCready Foundation	Delmarva Peninsula Insurance Company	Peninsula Regional Health System	Eliminations	Consolidated
Net assets without donor restrictions												
Revenue												
Patient service revenue	\$ 463,921	\$ -	\$ 3,053	\$ -	\$ 361	\$ 58,860	\$ 7,750	\$ 1,979	\$ -	\$ -	\$ -	\$ 535,924
Other revenue	19,992	-	3,312	911	23	11,135	1,061	642	(1,011)	-	(1,072)	34,993
Net assets released from restrictions	-	1,673	-	-	-	-	-	-	-	-	(1,673)	-
Total revenue	483,913	1,673	6,365	911	384	69,995	8,811	2,621	(1,011)	-	(2,745)	570,917
Expenses												
Salaries and wages	204,341	-	-	1,126	130	24,629	4,451	1,184	-	-	-	235,861
Supplies and other expenses	205,067	6	4,834	315	729	34,357	8,602	533	326	-	-	254,769
Employee benefits	48,831	-	-	103	10	7,712	1,930	151	-	-	(2,383)	56,354
Depreciation and amortization	29,793	-	201	-	305	4,633	42	303	-	-	-	35,277
Interest	5,258	-	71	-	-	1,019	-	144	-	-	-	6,492
Contributions to Hospital	-	1,673	-	-	-	-	-	-	-	-	(1,673)	-
Total expenses	493,290	1,679	5,106	1,544	1,174	72,350	15,025	2,315	326	-	(4,056)	588,753
(Loss) income from operations before other items	(9,377)	(6)	1,259	(633)	(790)	(2,355)	(6,214)	306	(1,337)	-	1,311	(17,836)
Other items												
Investment return	32,799	30	274	-	-	(1,217)	(2)	(18)	1,337	(192)	-	33,011
Other pension gains	2,978	-	-	-	-	-	-	-	-	-	-	2,978
Contributions received in acquisitions	-	-	-	-	-	105,030	93	6,160	-	-	-	111,283
Loss on extinguishment of debt	-	-	-	-	-	(4,142)	-	-	-	-	-	(4,142)
Total other items	35,777	30	274	-	-	99,671	91	6,142	1,337	(192)	-	143,130
Excess of revenue over expenses	26,400	24	1,533	(633)	(790)	97,316	(6,123)	6,448	-	(192)	1,311	125,294
Non-controlling interest elimination	-	-	(299)	-	-	-	-	-	-	-	-	(299)
Excess (deficit) of revenue over expenses attributable to Peninsula Regional Health System	\$ 26,400	\$ 24	\$ 1,234	\$ (633)	\$ (790)	\$ 97,316	\$ (6,123)	\$ 6,448	\$ -	\$ (192)	\$ 1,311	\$ 124,995