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OUR PATIENTS

To Whom It May Concern:

Enclosed please find the audited financial report of Covenant HealthCare System and Subsidiaries for the year ended June 30, 2020. Unless otherwise noted, the information speaks only as of June 30, 2020 and relates solely to the year then ended, and no implication is created that there has been no change in the financial position or operations of Covenant HealthCare System and its subsidiaries since that date. Neither Covenant HealthCare System nor any of its subsidiaries assume any responsibility to update any of the information contained in the financial report or any related material.

The financial report has been audited by outside, independent auditors.

The statements and data provided are for informational purposes only, and do not purport to include every item which may be of interest to holders of bonds payable from payments made by the subsidiaries of Covenant HealthCare System. Some of the statements, to the extent that they are not recitations of historical fact, may constitute "forward-looking statements." Words such as "estimate," "project," "anticipate," "expect," "intend," "believe" and similar expressions are indicative of forward-looking statements. A number of factors could cause actual results to differ materially from those stated in forward-looking statements, and as a result, readers are cautioned not to rely on forward-looking statements.

A handwritten signature in black ink that reads "Kevin S. Albosta".

Kevin S. Albosta, VP/CFO

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05/04/04

Covenant HealthCare System and Subsidiaries

**Consolidated Financial Report
with Additional Information
June 30, 2020**

Covenant HealthCare System and Subsidiaries

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Independent Auditor's Report

To the Board of Directors
Covenant HealthCare System and Subsidiaries

We have audited the accompanying consolidated financial statements of Covenant HealthCare System and Subsidiaries (Covenant HealthCare), which comprise the consolidated balance sheet as of June 30, 2020, 2019, and 2018 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 Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Covenant HealthCare System and Subsidiaries as of June 30, 2020, 2019, and 2018 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.

To the Board of Directors
Covenant HealthCare System and Subsidiaries

Emphasis of Matters

As described in Note 2 to the consolidated financial statements, Covenant HealthCare adopted the provisions of Accounting Standards Update (ASU) No. 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, as of July 1, 2019 by means of a cumulative-effect adjustment to the consolidated balance sheet as of the beginning of the fiscal year of adoption. Covenant HealthCare also adopted the provisions of ASU No. 2017-07, *Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, as of July 1, 2019 with retrospective application. Our opinion is not modified with respect to these matters.

Plante & Moran, PLLC

October 26, 2020

Covenant HealthCare System and Subsidiaries

Consolidated Balance Sheet

June 30, 2020, 2019, and 2018

(In Thousands)

	2020	2019	2018
Assets			
Current Assets			
Cash and cash equivalents (Notes 6 and 7)	\$ 113,066	\$ 35,116	\$ 30,880
Patient accounts receivable (Note 3)	67,704	74,647	70,475
Inventory	16,063	16,554	16,463
Estimated third-party payor settlements (Note 4)	1,002	2,864	1,601
Assets limited as to use (Notes 6 and 7)	-	-	3,665
Prepaid expenses and other	17,178	14,736	16,724
Total current assets	215,013	143,917	139,808
Assets Limited as to Use (Notes 6 and 7)			
Funds held under bond agreements	37,630	-	-
Professional liability fund	4,386	4,524	5,730
By donors for specific purpose	16,318	13,074	12,763
Investments (Notes 6 and 7)	450,235	423,710	403,212
Property and Equipment - Net (Note 9)	176,929	179,850	175,671
Other Assets			
Investments in unconsolidated entities (Note 15)	18,745	18,744	18,769
Other	24,939	22,215	22,714
Total other assets	43,684	40,959	41,483
Total assets	\$ 944,195	\$ 806,034	\$ 778,667

Covenant HealthCare System and Subsidiaries

Consolidated Balance Sheet (Continued)

June 30, 2020, 2019, and 2018

(In Thousands)

	2020	2019	2018
Liabilities and Net Assets			
Current Liabilities			
Accounts payable and accrued expenses	\$ 27,645	\$ 13,017	\$ 18,274
Current portion of long-term debt (Note 10)	4,510	6,710	6,505
Estimated third-party payor settlements (Note 4)	11,757	6,134	3,798
Medicare accelerated payments (Note 1)	61,681	-	-
Accrued liabilities and other:			
Accrued compensation and related amounts	46,147	36,795	39,121
Accrued interest payable	1,012	1,434	1,490
Current portion of accrued pension obligation (Note 13)	599	7,439	-
Current portion of accrued postretirement benefit obligation (Note 13)	3,928	3,757	-
Total current liabilities	157,279	75,286	69,188
Long-term Debt - Net of current portion (Note 10)	127,061	93,194	82,805
Other Liabilities			
Accrued pension obligation (Note 13)	49,694	51,193	46,305
Accrued postretirement benefit obligations (Note 13)	27,216	28,362	30,976
Reserve for professional liability claims (Note 12)	29,631	25,391	32,025
Other	20,034	18,661	16,757
Total other liabilities	126,575	123,607	126,063
Total liabilities	410,915	292,087	278,056
Net Assets			
Without donor restrictions	516,962	500,873	487,849
With donor restrictions	16,318	13,074	12,762
Total net assets	533,280	513,947	500,611
Total liabilities and net assets	\$ 944,195	\$ 806,034	\$ 778,667

Covenant HealthCare System and Subsidiaries

Consolidated Statement of Operations and Changes in Net Assets

Years Ended June 30, 2020, 2019, and 2018
(In Thousands)

	2020	2019	2018
Unrestricted Revenue, Gains, and Other Support			
Net patient service revenue before provision for bad debts			\$ 659,406
Provision for bad debts			(28,138)
Net patient service revenue (Note 4)	\$ 611,737	\$ 632,629	631,268
Investment income and realized gains and losses (Note 6)	180	546	614
Other revenue	38,492	30,148	40,812
Grant revenue (Note 1)	22,959	-	-
Total unrestricted revenue, gains, and other support	673,368	663,323	672,694
Expenses			
Salaries and wages	328,378	313,488	299,618
Benefits	69,449	72,921	70,072
Supplies	129,421	135,689	132,208
Professional fees	12,988	11,578	14,524
Purchased services	63,462	60,821	63,452
Insurance	6,800	1,634	6,005
Utilities	6,031	6,200	6,415
Depreciation and amortization	31,016	29,988	29,693
Interest expense	3,530	3,504	3,658
Other	13,244	13,956	12,219
Total expenses (Note 16)	664,319	649,779	637,864
Operating Income	9,049	13,544	34,830
Nonoperating Income (Expense)			
Investment income (Note 6)	8,453	9,160	7,492
Realized and unrealized net gains on investments (Note 6)	9,526	11,990	15,273
Other components of net periodic benefit cost	(8,439)	(1,600)	(7,078)
Other	(3,780)	464	500
Total nonoperating income	5,760	20,014	16,187
Excess of Revenue Over Expenses	\$ 14,809	\$ 33,558	\$ 51,017

Covenant HealthCare System and Subsidiaries

Consolidated Statement of Operations and Changes in Net Assets (Continued)

Years Ended June 30, 2020, 2019, and 2018
(In Thousands)

	2020	2019	2018
Net Assets without Donor Restrictions			
Excess of revenue over expenses	\$ 14,809	\$ 33,558	\$ 51,017
Change in unrealized losses in fair value of investments (Note 6)	-	(707)	(1,291)
Other	(100)	(20)	(20)
Pension and other postretirement benefit obligation adjustment (Note 13)	1,380	(19,807)	29,532
Increase in net assets without donor restrictions	16,089	13,024	79,238
Net Assets with Donor Restrictions			
Contributions	4,088	1,370	1,361
Investment income (Note 6)	379	461	495
Change in unrealized losses in fair value of investments (Note 6)	(95)	(28)	(19)
Other	100	20	(9)
Net assets released from restrictions	(1,228)	(1,511)	(1,004)
Increase in net assets with donor restrictions	3,244	312	824
Increase in Net Assets	19,333	13,336	80,062
Net Assets - Beginning of year	513,947	500,611	420,549
Net Assets - End of year	\$ 533,280	\$ 513,947	\$ 500,611

Covenant HealthCare System and Subsidiaries

Consolidated Statement of Cash Flows

Years Ended June 30, 2020, 2019, and 2018

(In Thousands)

	2020	2019	2018
Cash Flows from Operating Activities			
Increase in net assets	\$ 19,333	\$ 13,336	\$ 80,062
Adjustments to reconcile increase in net assets to net cash and cash equivalents from operating activities:			
Depreciation and amortization	31,016	29,988	29,693
Provision for bad debts	-	-	28,138
Change in realized and unrealized gains in fair value of investments	(9,792)	(11,954)	(14,861)
Pension and other postretirement benefit obligation adjustment	(1,380)	19,807	(29,532)
Restricted contributions, investment income, and other	(4,567)	(1,851)	(1,847)
Gain on investment in unconsolidated entities	(119)	(665)	(1,123)
Loss on extinguishment of debt	491	-	-
Changes in operating assets and liabilities that provided (used) cash and cash equivalents:			
Patient accounts receivable	6,943	(4,172)	(31,085)
Inventory and other current assets	(1,951)	1,897	(3,925)
Estimated third-party payor settlements	7,485	1,073	(9,076)
Accounts payable and accrued liabilities	19,316	(7,023)	7,943
Medicare accelerated payments	61,681	-	-
Accrued pension and postretirement obligations	(7,934)	(6,337)	(3,645)
Other liabilities	5,613	(4,730)	7,883
Net cash and cash equivalents provided by operating activities	126,135	29,369	58,625
Cash Flows from Investing Activities			
Purchase of property and equipment	(23,853)	(34,783)	(33,472)
Purchases of investments	(194,496)	(146,528)	(142,634)
Proceeds from sales and maturities of investments	177,763	137,984	128,001
Contributions to unconsolidated entities	(20)	(271)	(741)
Distributions from unconsolidated entities	138	961	1,328
Change in assets limited as to use - Funds held under bond agreements	(37,630)	3,665	860
Change in professional liability fund	138	1,206	(2,639)
Change in assets limited as to use by donors	(3,244)	(311)	(825)
Change in other assets	(2,724)	499	(3,730)
Net cash and cash equivalents used in investing activities	(83,928)	(37,578)	(53,852)
Cash Flows from Financing Activities			
Payment of debt issuance costs	(1,117)	-	-
Proceeds from issuance of long-term debt	109,329	17,075	-
Repayments of long-term debt	(77,036)	(6,481)	(3,722)
Restricted contributions, investment income, and other	4,567	1,851	1,847
Net cash and cash equivalents provided by (used in) financing activities	35,743	12,445	(1,875)
Increase in Cash and Cash Equivalents	77,950	4,236	2,898
Cash and Cash Equivalents - Beginning of year	35,116	30,880	27,982
Cash and Cash Equivalents - End of year	<u>\$ 113,066</u>	<u>\$ 35,116</u>	<u>\$ 30,880</u>
Supplemental Cash Flow Information - Property and equipment additions in accounts payable and accrued expenses	\$ 4,325	\$ 83	\$ 699

See notes to consolidated financial statements.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 1 - Nature of Business

Covenant HealthCare System (Covenant HealthCare) is the sole corporate member of Covenant Medical Center, Inc. (the "Medical Center" or CMC); Covenant HealthCare Foundation (CHF); Covenant Development Corporation (CDC); Visiting Nurse Association of Saginaw (VNA); and Visiting Nurse Special Services (VNSS). During 2019, VNSS was legally dissolved, and its net assets were transferred to CMC.

Covenant HealthCare is organized exclusively for charitable, scientific, and educational purposes. CDC is a for-profit corporation organized to further the health care services and needs of Covenant HealthCare. Covenant HealthCare provides health care services to Saginaw County, Michigan and surrounding areas, and its mission is to provide extraordinary care for every generation. To achieve this mission, Covenant HealthCare meets the needs of individuals and the communities in its service area through a complement of general and specialized health care services, including inpatient acute care, outpatient services, home health care, and other health care services.

COVID-19 Pandemic

On March 11, 2020, the World Health Organization declared the outbreak of a respiratory disease caused by a new coronavirus a pandemic. First identified in late 2019 and now known as COVID-19, the outbreak has impacted millions of individuals in the United States and worldwide. In response, the United States federal government and individual state and local governments have implemented measures to combat the outbreak that have impacted health care business operations. During the last quarter of fiscal year 2020, Covenant HealthCare's operations were significantly impacted as shelter-in-place orders and government mandates to suspend elective procedures reduced volumes significantly during the period. Covenant HealthCare has moved to mitigate the impact by reducing workforce, eliminating and delaying capital expenditures, and actively managing cash balances.

Enacted on March 27, 2020 by the federal government, the Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") was established, which authorizes \$100 billion to be administered through grants and other mechanisms to hospitals, public entities, not-for-profit entities, and Medicare and Medicaid-enrolled suppliers and institutional providers. The purpose of these funds is to reimburse providers for lost revenue attributable to the coronavirus pandemic, such as forgone revenue from canceled procedures, and to provide support for related health care expenses, such as constructing temporary structures or emergency operation centers; retrofitting facilities; purchasing medical supplies and equipment, including personal protective equipment and testing supplies; and increasing workforce. Further, these relief funds ensure uninsured patients are receiving testing and treatment for COVID-19.

On April 10, 2020, the U.S. Department of Health and Human Services (HHS) began making payments to health care providers from the \$100 billion appropriation. These are payments to health care providers that will not need to be repaid as long as Covenant HealthCare complies with certain terms and conditions outlined by HHS. Covenant HealthCare received approximately \$24 million of payments as part of general and targeted distributions of the CARES Act Provider Relief Fund. Covenant HealthCare initially relied upon the guidance in the HHS frequently asked questions (FAQs) published as of June 19, 2020 to determine the amount of grant revenue eligible for recognition as of June 30, 2020. Such FAQs stated general and targeted distributions of the CARES Act Provider Relief Fund could be used to offset lost revenue that is attributable to the coronavirus and that any reasonable method of estimating the revenue lost could be utilized. The FAQs also stated that general distributions could be shared within a health system. Covenant HealthCare estimated the lost revenue in March through June 2020, the months most severely impacted by the coronavirus, by comparing the revenue in those months to the expected revenue had the coronavirus not caused disruption in Covenant HealthCare facilities, to derive the total amount earned on targeted and general distributions.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 1 - Nature of Business (Continued)

Subsequent to June 30, 2020, HHS issued new reporting requirements for the CARES Act Provider Relief Fund. The new requirements first require the recipient to identify health care-related expenses attributable to the coronavirus pandemic that another source has not reimbursed. If those expenses do not exceed the funding received, the recipient will need to demonstrate the remaining funding was applied toward lost revenue, defined as the difference between calendar years 2019 and 2020 actual patient care revenue, with an additional six months to use through June 2021. HHS is entitled to recoup amounts in excess of the negative change in patient care revenue reported net of health care-related expenses attributable to the coronavirus pandemic. Management adjusted the calculation determining the targeted and general distributions earned by Covenant HealthCare using the guidance published by HHS subsequent to June 30.

There is at least a reasonable possibility that amounts recorded under the CARES Act by Covenant HealthCare may change in future periods. As of June 30, 2020, Covenant HealthCare has asserted that it has met the conditions and restrictions outlined with the HHS published terms and conditions and has recognized approximately \$22.5 million within grant revenue on the consolidated statement of operations and changes in net assets. Covenant HealthCare also has approximately \$1.5 million recorded as a liability within accounts payable and accrued expenses on the consolidated balance sheet, as Covenant HealthCare has not met the conditions and restrictions of the CARES Act as of June 30, 2020. Subsequent to June 30, Covenant HealthCare received additional targeted distributions of approximately \$14.5 million, which are not recorded in the accompanying consolidated balance sheet or consolidated statement of operations and changes in net assets.

During 2020, Covenant HealthCare requested accelerated Medicare payments, as provided for in the CARES Act, which allows for eligible health care facilities to request up to six months of accelerated Medicare payments for acute-care hospitals. The initial repayment terms for this funding stated that repayment was to begin 120 days past receipt of the accelerated payment; claims for services provided to Medicare beneficiaries will be applied against the accelerated payment balance. Any unapplied accelerated payment amounts must be paid in full within one year from receipt of the accelerated payments. As of June 30, 2020, Covenant HealthCare received approximately \$62 million from these accelerated Medicare payment requests, which is recorded as a contract liability on the consolidated balance sheet.

Subsequent to year end, the U.S. Congress and Centers for Medicare & Medicaid Services (CMS) extended the repayment terms of the accelerated Medicare payments to begin one year after the first payment was issued, at which point these amounts will be repaid at 25 percent of the Medicare payments to Covenant HealthCare for 11 months. After 11 months, the recoupment will increase to 50 percent of the Medicare payments for 6 additional months (or until all amounts are repaid). Any unapplied accelerated payment amounts that are unpaid after this 17-month period are due to CMS, plus interest at a rate of 4 percent on the outstanding balance. With the change in repayment terms issued subsequent to year end, repayment of the accelerated payments for Covenant HealthCare will begin during the year ending June 30, 2021 and will continue into the year ending June 30, 2023.

Note 2 - Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of Covenant HealthCare and all of its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 2 - Significant Accounting Policies (Continued)

Cash and Cash Equivalents

Cash and cash equivalents include cash and investments in highly liquid investments purchased with an original maturity of three months or less, excluding those amounts included in assets limited as to use. Cash balances held in the bank exceed the federal depository insurance limit. Covenant HealthCare's cash is only insured up to the federal depository insurance limit.

Investments

Investments in equity securities with readily determinable fair values, investments in common trust funds that invest in marketable equity securities, and all investments in debt securities are measured at fair value using quoted market prices. The realized gains and losses on investments are the difference between the proceeds received and the cost determined using the average method of investment valuation.

Covenant HealthCare has investments in certain limited partnerships, including private equity investments, real estate investments, common trust funds, and hedge funds, which are reported using the equity method of accounting.

Investments in unconsolidated entities where Covenant HealthCare does not have operating control are recorded using the equity method of accounting.

Accounts Receivable

Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges, reduced by explicit price concessions provided to third-party payors, discounts provided to qualifying individuals as part of a financial assistance policy, and implicit price concessions provided primarily to self-pay patients. Estimates for explicit price concessions are based on provider contracts, payment terms for relevant prospective payment systems, and historical experience adjusted for economic conditions and other trends affecting Covenant HealthCare's ability to collect outstanding amounts.

For receivables associated with self-pay patients (which include both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), Covenant HealthCare records significant implicit price concessions in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

Third-party Settlements

Contractual adjustments under third-party reimbursement programs represent the difference between Covenant HealthCare's established rates for services and amounts reimbursed by third-party payors. Cost report settlements result from the adjustment of interim payments to final reimbursement under these programs.

Inventory

Inventory, which consists of medical and office supplies and pharmaceutical products, is stated at cost, determined on a first-in, first-out basis or net realizable value.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 2 - Significant Accounting Policies (Continued)

Property and Equipment

Property and equipment, including internal-use software, are recorded at cost. The straight-line method is used for computing depreciation and amortization. Assets are depreciated over their estimated useful lives. Estimated useful lives by asset category are as follows: land improvements - 2 to 25 years; buildings - 20 to 40 years; and equipment - 3 to 20 years. Costs of maintenance and repairs are charged to expense when incurred.

Donated property and equipment are reported as unrestricted support and are excluded from excess of revenue over expenses unless explicit donor stipulations specify how the donated asset must be used. Donated property and equipment are recorded at estimated fair value at the time of donation.

Classification of Net Assets

Net assets of Covenant HealthCare are classified based on the presence or absence of donor-imposed restrictions.

Net assets without donor restrictions: Net assets that are not subject to donor-imposed restrictions or for which the donor-imposed restrictions have expired or been fulfilled. Net assets in this category may be expended for any purpose in performing the primary objectives of Covenant HealthCare.

Net assets with donor restrictions: Net assets subject to stipulations imposed by donors and grantors. Net assets with donor restrictions at Covenant HealthCare Foundation are used primarily for capital equipment and programs to support the care that CMC provides. In addition, certain funds support scholarships and educational opportunities for current and future staff alike. Some donor restrictions are temporary in nature; those restrictions will be met by actions of Covenant HealthCare or by the passage of time. When a donor restriction expires, that is, when a stipulated time restriction ends or the purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statement 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 without donor restrictions in the accompanying consolidated financial statements. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity. Restricted net assets which may be used subsequent to the passage of time or other stipulated activities total \$15,595, \$12,351, and \$12,040 as of June 30, 2020, 2019, and 2018, respectively. Net assets restricted in perpetuity total \$723 as of June 30, 2020, 2019, and 2018.

Earnings, gains, and losses on donor-restricted net assets are classified as net assets without donor restrictions unless specifically restricted by the donor or by applicable state law.

Revenue Recognition - Net Patient Service Revenue

Patient care service revenue is reported at the amount that reflects the consideration to which Covenant HealthCare expects to be entitled in exchange for providing patient care. These amounts are due from patients, third-party payors (including health insurers and government programs), and others and include variable consideration for retroactive revenue adjustments due to settlement of audits, reviews, and investigations. Generally, Covenant HealthCare bills the patients and third-party payors several days after the services are performed or the patient is discharged from the facility. Revenue is recognized as performance obligations are satisfied.

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 2 - Significant Accounting Policies (Continued)

Performance obligations are determined based on the nature of the services provided by Covenant HealthCare. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. Covenant HealthCare believes that this method provides a faithful depiction of the transfer of services over the term of the performance obligation based on the inputs needed to satisfy the obligation. Generally, performance obligations satisfied over time relate to patients in our hospital receiving inpatient acute-care services or patients receiving services in our outpatient centers or other clinical settings. Covenant HealthCare measures the performance obligation from admission into the hospital, or the commencement of an outpatient service or other visit, to the point when it is no longer required to provide services to that patient, which is generally at the time of discharge or completion of the outpatient services or other visit. Revenue for performance obligations satisfied at a point in time is generally recognized when goods are provided to our patients and customers in a retail setting (for example, pharmaceuticals and medical equipment), and Covenant HealthCare does not believe it is required to provide additional goods or services related to that sale.

Because all of its performance obligations relate to contracts with a duration of less than one year, Covenant HealthCare has elected to apply the optional exemption provided in FASB ASC 606-10-50-14(a) and, therefore, is not required to disclose the aggregate amount of the transaction price allocated to performance obligations that are unsatisfied or partially unsatisfied at the end of the reporting period. The unsatisfied or partially unsatisfied performance obligations referred to above are primarily related to inpatient acute-care services at the end of the reporting period. The performance obligations for these contracts are generally completed when the patients are discharged, which generally occurs within days or weeks of the end of the reporting period.

As of June 30, 2020, Covenant HealthCare recorded \$61,681 as a contract liability within current liabilities in the consolidated balance sheet as a result of Medicare payments received in advance of services being rendered (see Note 1). There were no significant contract liabilities recorded in the consolidated balance sheet as of June 30, 2019.

Covenant HealthCare determines the transaction price based on standard charges for goods and services provided, reduced by contractual adjustments provided to third-party payors, discounts provided to uninsured patients in accordance with Covenant HealthCare's policy, and implicit price concessions provided to uninsured patients. Covenant HealthCare determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies, and historical experience. Covenant HealthCare determines its estimate of implicit price concessions based on its historical collection experience with this class of patients.

Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. Covenant HealthCare also provides services to uninsured patients and offers those uninsured patients a discount, either by policy or law, from standard charges. Covenant HealthCare estimates the transaction price for patients with deductibles and coinsurance and from those who are uninsured based on historical experience and current market conditions. The initial estimate of the transaction price is determined by reducing the standard charge by any contractual adjustments, discounts, and implicit price concessions. Subsequent changes to the estimate of the transaction price are generally recorded as adjustments to net patient service revenue in the period of the change. For the years ended June 30, 2020, 2019, and 2018, changes in estimates of implicit price concessions, discounts, and contractual adjustments for performance obligations satisfied in prior years were not significant. Subsequent changes that are determined to be the result of an adverse change in the patient's ability to pay are recorded as bad debt expense.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 2 - Significant Accounting Policies (Continued)

Consistent with Covenant HealthCare's mission, care is provided to patients regardless of their ability to pay. Therefore, Covenant HealthCare has determined it has provided implicit price concessions to uninsured patients and patients with other uninsured balances (for example, copays and deductibles). The implicit price concessions included in estimating the transaction price represent the difference between amounts billed to patients and the amounts Covenant HealthCare expects to collect based on its collection history and those patients.

Patients who meet Covenant HealthCare's criteria for charity care are provided care without charge or at amounts less than established rates. Such amounts determined to qualify as charity care are not reported as revenue.

Covenant HealthCare has elected the practical expedient allowed under FASB ASC 606-10-32-18 and does not adjust the promised amount of consideration from patients and third-party payors for the effects of a significant financing component due to the Covenant HealthCare's expectation that the period between the time the service is provided to a patient and the time that the patient or a third-party payor pays for that service will be one year or less. However, Covenant HealthCare does, in certain instances, enter into payment agreements with patients that allow payments in excess of one year. For those cases, the financing component is not deemed to be significant to the contract.

Excess of Revenue Over Expenses

The consolidated statement of operations and changes in net assets includes excess of revenue over expenses, which is Covenant HealthCare's performance indicator. Changes in net assets without donor restrictions, which are excluded from excess of revenue over expenses, consistent with industry practice, include unrealized gains and losses on investments classified as available-for-sale securities (prior to the adoption of ASU No. 2016-01 in 2020), pension and other postretirement-related changes other than net periodic benefit cost, and contributions of long-lived assets (including assets acquired using contributions, which, by donor restriction, were to be used for the purpose of acquiring such assets).

Use of Estimates

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

Income Taxes

Covenant HealthCare and its subsidiaries, except for CDC, are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. No provision for income taxes has been included in the consolidated financial statements for the exempt entities. CDC is a Michigan for-profit corporation; income tax provisions for CDC are not material to the consolidated financial statements.

Change in Accounting Principles

In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. Covenant HealthCare adopted the standard as of July 1, 2019 and implemented the standard through a cumulative-effect adjustment to the consolidated balance sheet as of July 1, 2019. The adoption of this standard resulted in unrealized gains and losses on equity securities, other than those that are restricted by donors, to be presented within nonoperating income during 2020, rather than as a component of changes in net assets as previously reported.

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 2 - Significant Accounting Policies (Continued)

In March 2017, the FASB issued ASU No. 2017-07, *Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This standard requires service cost to be included within operating expenses, the other components of net benefit cost to be presented separately outside of income from operations, and capitalization of only the service cost component, when applicable. Covenant HealthCare adopted this guidance as of July 1, 2019, with retrospective application for the years ended June 30, 2019 and 2018. The effect of this change within the consolidated statement of operations and changes in net assets was to increase operating income by \$1,600 and \$7,078, with corresponding decreases in nonoperating income, for the years ended June 30, 2019 and 2018, respectively.

Upcoming Accounting Pronouncement

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations and changes in net assets. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and changes in net assets and cash flows will be generally consistent with the current guidance. The new lease guidance was scheduled to be effective for Covenant HealthCare's year ended June 30, 2020. However, as a result of the COVID-19 pandemic, the FASB allowed for an optional one-year deferral of the implementation, of which Covenant HealthCare has elected to take advantage. As a result, the ASU will be implemented in the year ending June 30, 2021. The new lease standard is expected to have a significant effect on Covenant HealthCare's consolidated financial statements as a result of the leases for real estate and equipment currently classified as operating leases. The effect of applying the new lease guidance on the consolidated financial statements will be to increase long-term assets and lease liabilities. The effects on the results of operations are not expected to be significant, as recognition and measurement of expenses and cash flows for leases will be substantially the same under the new standard.

Subsequent Events

The consolidated financial statements and related disclosures include evaluation of events up through and including October 26, 2020, which is the date the consolidated financial statements were available to be issued.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 3 - Patient Accounts Receivable

Patient accounts receivable are based on the estimated transaction price for completed contracts, which total \$67,704 and \$74,647 at June 30, 2020 and 2019, respectively. Prior to the adoption of ASU No. 2014-09, patient accounts receivable at June 30, 2018 were composed of accounts receivable of \$277,941, less allowances for uncollectible accounts of \$19,997 and allowances for contractual adjustments of \$187,469.

Covenant HealthCare grants credit without collateral to patients, most of whom are local residents and are insured under third-party payor agreements. The composition of receivables from these major payor sources was as follows as of June 30:

	2020	2019	2018
Medicare	33 %	30 %	33 %
Medicaid	13	14	16
Blue Cross/Blue Shield of Michigan	13	10	11
Self-pay and other	41	46	40
Total	100 %	100 %	100 %

Note 4 - Net Patient Service Revenue

Covenant HealthCare has agreements with third-party payors that provide payments at amounts less than established charges. A summary of the basis of the payment arrangements with major third-party payors is as follows:

- **Medicare** - Inpatient, acute-care, and rehabilitation services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. Inpatient psychiatric and substance abuse services are reimbursed at cost subject to a per case limit. Outpatient and homecare services related to Medicare beneficiaries are reimbursed based on a prospectively determined amount per episode of care.
- **Medicaid** - Inpatient, acute-care services rendered to Medicaid program beneficiaries are also paid at prospectively determined rates per discharge. Capital costs relating to Medicaid patients are paid on a cost-reimbursement method. Outpatient and physician services are reimbursed on an established fee-for-service methodology.
- **Blue Cross/Blue Shield of Michigan** - Inpatient, acute-care services are reimbursed at prospectively determined rates per discharge. Outpatient services are reimbursed on a fee-for-service and percentage of charge basis.

Cost report settlements result from the adjustment of interim payments to final reimbursement under the Medicare, Medicaid, and Blue Cross/Blue Shield of Michigan programs that are subject to audit by fiscal intermediaries.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 4 - Net Patient Service Revenue (Continued)

Laws and regulations concerning government programs, including Medicare and Medicaid, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care entities have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in entities entering into significant settlement agreements. Compliance with such laws and regulations may also be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties, and potential exclusion from the related programs. There can be no assurance that regulatory authorities will not challenge Covenant HealthCare's compliance with these laws and regulations, and it is not possible to determine the impact (if any) such claims or penalties would have upon Covenant HealthCare. In addition, the contracts Covenant HealthCare has with commercial payors also provide for retroactive audit and review of claims.

Settlements with third-party payors for retroactive adjustments due to audits, reviews, or investigations are considered variable consideration and are included in the determination of the estimated transaction price for providing patient care. These settlements are estimated based on the terms of the payment agreement with the payor, correspondence from the payor, and Covenant HealthCare's historical settlement activity, including an assessment to ensure that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the retroactive adjustment is subsequently resolved. Estimated settlements are adjusted in future periods as adjustments become known (that is, new information becomes available) or as years are settled or are no longer subject to such audits, reviews, and investigations. Adjustments arising from a change in the transaction price were not significant in 2020, 2019, or 2018.

Covenant HealthCare has determined that the nature, amount, timing, and uncertainty of revenue and cash flows are affected primarily by payor. The composition of net patient service revenue by primary payor for the years ended June 30 is as follows:

	2020	2019	2018
Medicare	\$ 265,433	\$ 263,975	\$ 271,445
Medicaid	102,891	106,699	101,003
Blue Cross/Blue Shield of Michigan	113,119	112,431	107,316
Self-pay and other	130,294	149,524	151,504
Total	<u>\$ 611,737</u>	<u>\$ 632,629</u>	<u>\$ 631,268</u>

Revenue from patients' deductibles and coinsurance is included in the categories presented above based on the primary payor.

Covenant HealthCare recognizes its net patient service revenue over time, as patients simultaneously receive and consume benefits provided as care is administered.

Covenant HealthCare recognizes revenue related to retail pharmacy at a point in time. Retail pharmacy sales are recognized within other operating revenue in the accompanying consolidated statement of operations and changes in net assets and totaled \$7,381, \$8,509, and \$8,152 during the years ended June 30, 2020, 2019, and 2018, respectively.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 4 - Net Patient Service Revenue (Continued)

Net patient service revenue consists of the following for the years ended June 30:

	2020	2019	2018
Gross patient service charges	\$ 2,272,871	\$ 2,286,482	\$ 2,256,853
Explicit price concessions to commercial and governmental payors	(1,637,530)	(1,628,318)	(1,597,447)
Implicit price concessions to self-pay patients (in 2018, this amount represents the provision for bad debts)	(23,604)	(25,535)	(28,138)
Net patient service revenue	<u>\$ 611,737</u>	<u>\$ 632,629</u>	<u>\$ 631,268</u>

Note 5 - Charity Care

Covenant HealthCare provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because Covenant HealthCare does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Charity care is determined based on established policies, using patient income and assets to determine payment ability. The estimated cost of providing charity services is based on a calculation that applies a ratio of cost to charges to the gross uncompensated charges associated with providing care to charity patients. Covenant HealthCare estimates that it provided, at cost, \$1,693, \$1,522, and \$1,207 of services to indigent patients during 2020, 2019, and 2018, respectively. Net patient service revenue excludes charity care adjustments of \$5,408, \$4,886, and \$3,828 during 2020, 2019, and 2018, respectively.

Note 6 - Investments

The details of Covenant HealthCare's investments, including cash and cash equivalents and assets limited as to use, at June 30 are as follows:

	2020	2019	2018
Cash and cash equivalents	\$ 155,111	\$ 38,538	\$ 34,597
Marketable equity security mutual funds	1,194	13,610	25,245
Fixed-income mutual funds	140,906	100,158	96,846
Publicly traded mutual funds	237,629	222,505	209,122
Common trust funds	28,808	39,575	27,601
Limited partnerships	1,540	10,010	10,473
Hedge funds	56,447	52,028	52,366
Total	<u>\$ 621,635</u>	<u>\$ 476,424</u>	<u>\$ 456,250</u>

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 6 - Investments (Continued)

A reconciliation of investments, assets limited as to use, and cash and cash equivalents from the above table to the consolidated balance sheet is presented below as of June 30:

	2020	2019	2018
Cash and cash equivalents	\$ 113,066	\$ 35,116	\$ 30,880
Assets limited as to use:			
Funds held under bond agreements	37,630	-	3,665
Professional liability fund	4,386	4,524	5,730
By donors for specific purposes	16,318	13,074	12,763
Total assets limited as to use	58,334	17,598	22,158
Investments	450,235	423,710	403,212
Total	<u>\$ 621,635</u>	<u>\$ 476,424</u>	<u>\$ 456,250</u>

Investment income and realized and unrealized gains and losses on investments are reported as follows for the years ended June 30:

	2020	2019	2018
Interest and dividends	\$ 8,651	\$ 9,468	\$ 7,703
Realized gains on sale of investments	10,976	8,886	13,952
Change in unrealized (losses) gains	(1,184)	3,068	909
Total	<u>\$ 18,443</u>	<u>\$ 21,422</u>	<u>\$ 22,564</u>

Investment income and realized and unrealized gains and losses on investments are included in the accompanying consolidated statement of operations and changes in net assets for the years ended June 30 as follows:

	2020	2019	2018
Operating revenue	\$ 180	\$ 546	\$ 614
Nonoperating income	17,979	21,150	22,765
Change in net assets without donor restrictions	-	(707)	(1,291)
Restricted investment income	379	461	495
Change in net assets with donor restrictions	(95)	(28)	(19)
Total	<u>\$ 18,443</u>	<u>\$ 21,422</u>	<u>\$ 22,564</u>

Covenant HealthCare invests in various financial instruments that are publicly and privately traded. Financial instruments are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the consolidated statement of operations and changes in net assets.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 6 - Investments (Continued)

Prior to the adoption of ASU No. 2016-01 as of July 1, 2019, Covenant HealthCare classified its equity investments as available-for-sale securities. The gross unrealized gains (losses) since acquisition on marketable equity securities were \$38,184 and \$(5,856), respectively, at June 30, 2019, and \$40,961 and \$(7,521), respectively, at June 30, 2018.

Information pertaining to available-for-sale investment securities with gross unrealized losses at June 30, 2019 and 2018, aggregated by investment category and length of time that individual securities have been in a continuous loss position, is as follows:

	2019					
	Less Than 12 Months		12 Months or Greater		Total	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
Investments with unrealized losses:						
Fixed-income mutual funds	\$ -	\$ -	\$ (1,622)	\$ 12,858	\$ (1,622)	\$ 12,858
Publicly traded mutual funds	(718)	12,409	(3,516)	47,993	(4,234)	60,402
Total investments with unrealized losses	<u>\$ (718)</u>	<u>\$ 12,409</u>	<u>\$ (5,138)</u>	<u>\$ 60,851</u>	<u>\$ (5,856)</u>	<u>\$ 73,260</u>
	2018					
	Less Than 12 Months		12 Months or Greater		Total	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
Investments with unrealized losses:						
Fixed-income mutual funds	\$ -	\$ -	\$ (3,977)	\$ 93,181	\$ (3,977)	\$ 93,181
Publicly traded mutual funds	(836)	20,164	(2,708)	44,341	(3,544)	64,505
Total investments with unrealized losses	<u>\$ (836)</u>	<u>\$ 20,164</u>	<u>\$ (6,685)</u>	<u>\$ 137,522</u>	<u>\$ (7,521)</u>	<u>\$ 157,686</u>

Note 7 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the consolidated financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following tables present information about Covenant HealthCare's assets measured at fair value on a recurring basis at June 30, 2020, 2019, and 2018 and the valuation techniques used by Covenant HealthCare to determine those fair values.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that Covenant HealthCare has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs, such as interest rates and yield curves, that are observable at commonly quoted intervals.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 7 - Fair Value Measurements (Continued)

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. Covenant HealthCare's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

Covenant HealthCare's policy is to recognize transfers into and transfers out of Level 1, 2, and 3 fair value classifications as of the end of the reporting period. During the years ended June 30, 2020, 2019, and 2018, there were no transfers between levels of the fair value hierarchy.

Assets Measured at Fair Value on a Recurring Basis at
June 30, 2020

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at June 30, 2020
Assets				
Cash and cash equivalents	\$ 117,481	\$ -	\$ -	\$ 117,481
Assets limited as to use and investments:				
Cash and cash equivalents	37,630	-	-	37,630
Mutual funds:				
U.S. large cap	129,026	-	-	129,026
Fixed income	140,906	-	-	140,906
International fixed income	14,010	-	-	14,010
International companies	74,702	-	-	74,702
Real estate	21,085	-	-	21,085
Total assets limited as to use and investments	417,359	-	-	417,359
Other assets - Benefit plan assets	17,342	-	-	17,342
Total assets	\$ 552,182	\$ -	\$ -	\$ 552,182

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 7 - Fair Value Measurements (Continued)

Assets Measured at Fair Value on a Recurring Basis at June 30, 2019				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at June 30, 2019
Assets				
Cash and cash equivalents	\$ 38,538	\$ -	\$ -	\$ 38,538
Assets limited as to use and investments -				
Mutual funds:				
U.S. large cap	119,259	-	-	119,259
Fixed income	100,158	-	-	100,158
International fixed income	12,858	-	-	12,858
International companies	77,928	-	-	77,928
Real estate	26,070	-	-	26,070
Total assets limited as to use and investments	336,273	-	-	336,273
Other assets - Benefit plan assets	15,910	-	-	15,910
Total assets	\$ 390,721	\$ -	\$ -	\$ 390,721
Assets Measured at Fair Value on a Recurring Basis at June 30, 2018				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at June 30, 2018
Assets				
Cash and cash equivalents	\$ 34,597	\$ -	\$ -	\$ 34,597
Assets limited as to use and investments -				
Mutual funds:				
U.S. large cap	122,413	-	-	122,413
Fixed income	96,846	-	-	96,846
International fixed income	12,166	-	-	12,166
International companies	71,879	-	-	71,879
Real estate	27,909	-	-	27,909
Total assets limited as to use and investments	331,213	-	-	331,213
Other assets - Benefit plan assets	13,408	-	-	13,408
Total assets	\$ 379,218	\$ -	\$ -	\$ 379,218

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 7 - Fair Value Measurements (Continued)

Included within investments on the consolidated balance sheet are investments in common trust funds, limited partnerships, and hedge funds totaling \$86,795, \$101,613, and \$90,440 at June 30, 2020, 2019, and 2018, respectively. These investments are accounted for under the equity method. Equity method investments are not measured at fair value on a recurring basis and, therefore, are not included in the tables above.

Note 8 - Liquidity and Availability of Resources

The following reflects Covenant HealthCare's financial assets as of June 30, 2020 and 2019, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of June 30:

	2020	2019
Cash and cash equivalents	\$ 113,066	\$ 35,116
Patient accounts receivable	67,704	74,647
Estimated third-party payor settlements	1,002	2,864
Investments and assets limited as to use	508,569	441,308
Other financial assets	30,299	26,606
	<u>720,640</u>	<u>580,541</u>
Financial assets - At year end		
Less those unavailable for general expenditures within one year due to contractual or donor-imposed restrictions:		
Funds held under bond agreements	37,630	-
Deferred compensation assets	17,342	15,910
Professional liability fund	4,386	4,524
By donors for specific purposes	16,318	13,074
	<u>644,964</u>	<u>547,033</u>
Financial assets available to meet cash needs for general expenditures within one year		

Covenant HealthCare has certain contractual and donor-restricted assets limited as to use, which are more fully described in Notes 6 and 13. These amounts are not available for general expenditure within the next year.

Covenant HealthCare has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, Covenant HealthCare invests cash in excess of daily requirements in various short-term investments, including certificates of deposit and short-term treasury instruments.

Covenant HealthCare also realizes there could be unanticipated liquidity needs. A revolving credit agreement (line of credit) is available to Covenant HealthCare, which is more fully described in Note 10.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 9 - Property and Equipment

Property and equipment are summarized at June 30 as follows:

	2020	2019	2018
Land and land improvements	\$ 17,581	\$ 17,351	\$ 16,583
Buildings	224,759	223,567	221,532
Equipment	452,707	432,418	397,833
Construction in progress	7,832	1,954	8,909
Total cost	702,879	675,290	644,857
Accumulated depreciation	525,950	495,440	469,186
Net property and equipment	<u>\$ 176,929</u>	<u>\$ 179,850</u>	<u>\$ 175,671</u>

During 2020, Covenant HealthCare entered into construction contracts totaling \$31,954 with a company affiliated with a member of the board of directors of Covenant HealthCare. As of June 30, 2020, \$30,134 was remaining on the construction contracts.

Note 10 - Long-term Debt

Long-term debt at June 30 is as follows:

	2020	2019	2018
City of Saginaw Hospital Finance Authority Hospital Revenue Refunding Bonds, Series 2010H	\$ -	\$ 56,780	\$ 58,975
City of Saginaw Hospital Finance Authority Hospital Revenue and Refunding Bonds, Series 2014I	16,375	19,970	23,490
City of Saginaw Hospital Finance Authority Hospital Revenue Refunding Bonds, Series 2020J	55,325	-	-
City of Saginaw Hospital Finance Authority Hospital Revenue Bonds, Series 2020K	40,110	-	-
2015 term loan agreement	5,390	6,205	6,995
2019 term loan agreement	1,675	17,075	-
Unamortized premium	13,894	729	759
Unamortized debt issuance costs	(1,198)	(855)	(909)
Total debt	131,571	99,904	89,310
Less current portion	4,510	6,710	6,505
Long-term portion	<u>\$ 127,061</u>	<u>\$ 93,194</u>	<u>\$ 82,805</u>

Covenant HealthCare entered into long-term debt agreements with the City of Saginaw Hospital Finance Authority. The debt agreements require payments sufficient to pay principal and interest on the bonds. Among other things, the debt agreements contain covenants that place restrictions on the amount of new debt that Covenant HealthCare can incur and the maintenance of a minimum debt service coverage ratio. The debt is secured by the accounts receivable and general intangibles of the obligated group members pursuant to the master indenture. The obligated group is responsible for making all principal and interest payments on the bonds as they become due. The obligated group consists of CMC and CHF.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 10 - Long-term Debt (Continued)

On April 2, 2020, Covenant HealthCare issued the Series 2020J bonds, which were purchased by a bank. At June 30, 2020, the Series 2020J bonds consist of \$55,325 of fixed-rate serial bonds, which bear annual interest at rates ranging from 4.00 to 5.00 percent. Beginning in 2022, the bonds mature annually through 2041 in amounts ranging from \$385 to \$6,820. The bonds are secured by a pledge of gross revenue of the members of the obligated group. The proceeds from the Series 2020J bonds were used to refund the Series 2010H bonds, partially refund the 2019 term loan, and pay for the expenses incurred in connection with the issuance of the 2020J bonds.

On March 31, 2020, Covenant HealthCare issued the Series 2020K bonds, which were purchased by a bank. At June 30, 2020, the Series 2020K bonds consist of \$40,110 of fixed-rate term bonds, which bear annual interest at rates ranging from 3.26 to 3.39 percent. Beginning in 2032, the bonds mature annually through 2051 in amounts ranging from \$1,440 to \$2,710. The bonds are secured by a pledge of gross revenue of the members of the obligated group. The proceeds from the Series 2020K bonds were used to pay for certain capital projects and to pay for the expenses incurred in connection with the issuance of the 2020K bonds. At June 30, 2020, \$37,630 of the proceeds was unused and recorded as assets limited as to use within the consolidated balance sheet (see Note 6).

On June 25, 2019, a \$17,075 10-year term loan agreement was entered into with PNC Bank. This loan bears a variable rate of interest based on the one-month London Interbank Offered Rate (LIBOR) plus 29 basis points, which, at June 30, 2020 and 2019, was 1.8 and 2.7 percent, respectively. The loan was partially refunded on April 2, 2020 with the proceeds of the 2020J bonds. The loan matures in 2022. The proceeds of this loan were used to fund various capital projects on Covenant HealthCare's campus.

On May 27, 2015, an \$8,500 10-year term loan agreement was entered into with JPMorgan Chase Bank. This loan bears a variable rate of interest based on the one-month (LIBOR) plus 135 basis points, which, at June 30, 2020 and 2019 was 1.5 and 3.8 percent, respectively. Annual principal payments of amounts ranging from \$835 in 2021 to \$965 in 2025 are required. The proceeds of this loan were used to fund the purchase of the remaining two-thirds interest in Saginaw Radiation Oncology Center, as well as certain real property.

On April 25, 2014, Covenant HealthCare issued the Series 2014I bonds, which were purchased by JPMorgan Chase Bank, National Association. At June 30, 2020, the Series 2014I bonds consist of \$16,375 of fixed-rate bonds, which bear an annual interest rate of 2.09 percent. The bonds mature annually through 2024 in amounts ranging from \$3,675 to \$5,130. The bonds are secured by a pledge of gross revenue of the members of the obligated group. The proceeds from the Series 2014I bonds were used to pay for certain capital projects, refund the Series 2004G bonds, and pay for the expenses incurred in connection with the issuance of the 2014I bonds.

On October 28, 2010, Covenant HealthCare issued the Series 2010H bonds, consisting of both serial and term bonds, which bore annual interest at rates ranging from 4.25 to 5.00 percent. The Series 2010H bonds were refunded in the full on April 2, 2020 with the proceeds of the Series 2020J bonds. The bonds were secured by a pledge of gross revenue of the members of the obligated group. The proceeds from the Series 2010H bonds were used to refund the Series 1999E and Series 2000F bonds and to pay the expenses incurred in connection with the issuance of the Series 2010H bonds.

On June 24, 2020, Covenant HealthCare entered into a revolving credit agreement with JPMorgan Chase Bank that permits borrowings of up to \$50,000 and matures on June 23, 2021. The credit agreement bears interest at the prime rate, provided that the prime rate is not less than the adjusted one-month LIBOR, as defined in the agreement. The effective interest rate as of June 30, 2020 was 3.25 percent. There were no outstanding borrowings under the credit facility as of June 30, 2020.

Covenant HealthCare has several letters of credit available at June 30, 2020 to provide funding for certain self-insured benefits. There were no outstanding draws on the letters of credit at June 30, 2020.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 10 - Long-term Debt (Continued)

Cash paid for interest during 2020, 2019, and 2018 amounted to \$4,266, \$3,537, and \$3,705, respectively. Of the amount paid during 2020, \$337 was capitalized.

The balance of the above debt matures as follows:

<u>Years Ending</u>	<u>Amount</u>
2021	\$ 4,510
2022	8,050
2023	6,530
2024	6,745
2025	6,230
Thereafter	<u>86,810</u>
Total	<u>\$ 118,875</u>

Note 11 - Operating Leases

Covenant HealthCare has various operating leases for buildings and equipment. Rental expense under these leases during the years ended June 30, 2020, 2019, and 2018 amounted to \$4,860, \$6,176, and \$5,662, respectively.

Future minimum annual commitments under these operating leases are as follows:

<u>Years Ending June 30</u>	<u>Amount</u>
2021	\$ 3,991
2022	3,203
2023	2,569
2024	1,769
2025	921
Thereafter	<u>974</u>
Total	<u>\$ 13,427</u>

Note 12 - Professional and Other Liability Insurance

Covenant HealthCare maintains a self-insured irrevocable trust fund for medical malpractice claims. Under terms of the trust agreements, trust assets may be used for payment of professional liability losses, related expenses, and the cost of administering the trusts, subject to certain retention limits. Excess professional liability insurance coverage has been obtained in amounts deemed adequate by Covenant HealthCare to cover claims in excess of self-insured retention limits.

Covenant HealthCare records its estimated liabilities for damages and costs that may be awarded on claims and unreported liabilities. Covenant HealthCare's estimates are based on historical experience, the evaluations of all known claims and certain incidents, and the evaluation of claims of substance. Estimated liabilities for known incidents that may result in the assertion of additional claims and other claims that may be asserted arising from services provided to patients during the period are based upon projections by a consulting actuary. The recorded loss reserves as of June 30, 2020, 2019, and 2018 are \$29,631, \$25,391, and \$32,025, respectively. The loss reserves are discounted using an annual discount rate of 4.0 percent at June 30, 2020, 2019, and 2018.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 12 - Professional and Other Liability Insurance (Continued)

Covenant HealthCare has recognized a receivable of \$4,184, \$2,892, and \$5,892 at June 30, 2020, 2019, and 2018, respectively, for amounts to be recovered from various insurance carriers and captive insurance companies within other long-term assets in the consolidated balance sheet. While it is possible that settlement of asserted claims and claims that may be asserted in the future could result in liabilities in excess of amounts for which Covenant HealthCare has provided, management believes that the additional liabilities, if any, would not materially affect the consolidated financial position at June 30, 2020.

Note 13 - Pension and Other Postretirement Benefit Plans

Covenant HealthCare has funded noncontributory defined benefit pension plans. The plans provide defined benefits based on years of service and the employee's compensation during the last five years of employment. In February 2011, Covenant HealthCare elected to freeze the pension benefits at the levels in place as of that date.

Covenant HealthCare also has other postretirement benefit plans for retirees who meet eligibility requirements. This plan is frozen and has had no new participants since January 2000. The plan participants also stopped accumulating years of service as of December 31, 2007.

The following tables set forth the funded status and amounts recognized in the consolidated balance sheet for the defined benefit pension and other postretirement benefit plans as of June 30, 2020, 2019, and 2018:

Obligations and Funded Status

	Pension Benefits			Other Postretirement Benefits		
	2020	2019	2018	2020	2019	2018
Change in benefit obligation:						
Benefit obligation at beginning of year	\$ 375,380	\$ 346,491	\$ 373,690	\$ 32,119	\$ 30,976	\$ 35,041
Service cost	231	261	453	-	-	-
Interest cost	12,969	14,665	14,336	1,555	1,238	1,267
Actuarial loss (gain)	32,258	31,062	(22,238)	375	2,261	(3,487)
Benefits paid	(25,722)	(17,099)	(19,750)	(2,905)	(2,356)	(1,845)
Benefit obligation at end of year	395,116	375,380	346,491	31,144	32,119	30,976
Change in plan assets:						
Fair value of plan assets at beginning of year	316,748	300,186	298,273	-	-	-
Actual return on plan assets	39,706	27,362	11,734	-	-	-
Employer contributions	14,091	6,299	9,929	2,905	2,356	1,845
Benefits paid	(25,722)	(17,099)	(19,750)	(2,905)	(2,356)	(1,845)
Fair value of plan assets at end of year	344,823	316,748	300,186	-	-	-
Funded status at end of year	\$ (50,293)	\$ (58,632)	\$ (46,305)	\$ (31,144)	\$ (32,119)	\$ (30,976)

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 13 - Pension and Other Postretirement Benefit Plans (Continued)

Amounts recognized in changes in net assets consist of the following:

	Pension Benefits			Other Postretirement Benefits		
	2020	2019	2018	2020	2019	2018
Net loss (gain)	\$ 127,984	\$ 129,739	\$ 112,161	\$ (2,075)	\$ (2,450)	\$ (4,640)
Prior service credit	-	-	(39)	-	-	-
Total	\$ 127,984	\$ 129,739	\$ 112,122	\$ (2,075)	\$ (2,450)	\$ (4,640)

The accumulated benefit obligation for all defined benefit pension plans was \$390,183, \$372,197, and \$343,798 at June 30, 2020, 2019, and 2018, respectively. The accumulated benefit obligation for all other postretirement benefit plans was \$30,396, \$31,256, and \$30,377 at June 30, 2020, 2019, and 2018, respectively.

Components of net periodic benefit cost are as follows:

	Pension Benefits			Other Postretirement Benefits		
	2020	2019	2018	2020	2019	2018
Net Periodic Benefit Cost						
Service cost	\$ 231	\$ 261	\$ 453	\$ -	\$ -	\$ -
Interest cost	13,066	14,665	14,336	1,065	1,238	1,267
Expected return on plan assets	(20,945)	(21,327)	(20,732)	-	-	-
Amortization of prior service cost	-	(38)	(94)	-	(193)	-
Amortization of actuarial loss Settlement	10,697	7,255	10,093	-	-	-
	4,556	-	2,208	-	-	-
Total recognized in net periodic benefit cost	\$ 7,605	\$ 816	\$ 6,264	\$ 1,065	\$ 1,045	\$ 1,267

For measurement purposes in the other postretirement plan, a 6.40 percent initial annual rate of increase in the per capita cost of covered health care benefits was assumed for 2020. The rate was assumed to decrease gradually annually to 4.50 percent in 2029 and remain at that level thereafter.

The health care cost trend rate assumptions have a significant effect on the amounts reported for the health care plans. To illustrate, a 1 percentage point change in assumed health care cost trend rates would have the following effects:

	1 Percentage Point Increase	1 Percentage Point Decrease
Effect on total of service and interest cost components	\$ 27	\$ (25)

Weighted-average assumptions used to determine benefit obligations at June 30 are as follows:

	Pension Benefits			Other Postretirement Benefits		
	2020	2019	2018	2020	2019	2018
Discount rate	2.82%	3.63%	4.35%	2.82%	3.63%	4.35%

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 13 - Pension and Other Postretirement Benefit Plans (Continued)

Weighted-average assumptions used to determine net periodic benefit cost for the years ended June 30 are as follows:

	Pension Benefits			Other Postretirement Benefits		
	2020	2019	2018	2020	2019	2018
Discount rate	3.63%	4.35%	3.95%	3.63%	4.35%	3.95%
Expected long-term return on plan assets	6.75%	7.00%	7.00%	-	-	-
Rate of compensation increase	5.00%	5.00%	3.25%	-	-	-

Pension Plan Assets

The investments of the plans are held by a trustee and managed in accordance with guidelines established by Covenant HealthCare. The plan assets are invested in a well-diversified portfolio designed to maximize returns without assuming undue risk. The plans use investment managers specializing in each asset class. Plan assets largely consist of domestic and international equity holdings, domestic and international fixed-income holdings, common trust funds, limited partnerships, and hedge funds. The performance of all managers and the aggregate asset allocation are formally reviewed quarterly.

The expected long-term rate of return of plan assets is based on historical and projected rates of return for current and planned asset categories in the plans' investment portfolio. Assumed projected rates of return for each asset category were selected after analyzing historical experience and future expectations of the returns and volatility for assets of that category using benchmark rates. Based on the target asset allocation among the asset categories, the overall expected rate of return for the portfolio was developed and adjusted for historical and expected experience of active portfolio management results compared to benchmark returns and for the effect of expenses paid from plan assets.

The weighted-average asset allocation and the target allocation, by asset category, are as follows:

Asset category:	Percentage of Plan Assets at June 30			Target Allocation
	2020	2019	2018	2020
Cash and cash equivalents	3.00 %	0.60 %	1.40 %	0.50 %
Marketable equity securities	2.70	2.80	5.10	5.10
Fixed income	48.60	51.20	50.00	49.50
Publicly traded mutual funds	40.80	40.00	37.20	38.00
Common trust funds	4.30	4.60	4.80	4.80
Limited partnerships	0.60	0.80	1.10	1.60
Hedge funds	-	-	0.40	0.50

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 13 - Pension and Other Postretirement Benefit Plans (Continued)

Fair Value Measurements at June 30, 2020				
Asset Classes	Quoted Prices in			Total
	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Cash and cash equivalents	\$ 11,589	\$ -	\$ -	\$ 11,589
Mutual funds:				
U.S. large cap	86,426	-	-	86,426
International	87,618	-	-	87,618
Fixed income	85,822	-	-	85,822
Real estate	13,178	-	-	13,178
Fixed-income contracts	-	830	-	830
Total	\$ 284,633	\$ 830	\$ -	\$ 285,463

Fair Value Measurements at June 30, 2019				
Asset Classes	Quoted Prices in			Total
	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Cash and cash equivalents	\$ 3,482	\$ -	\$ -	\$ 3,482
Mutual funds:				
U.S. large cap	123,957	-	-	123,957
International	47,441	-	-	47,441
Fixed income	72,433	-	-	72,433
Real estate	14,666	-	-	14,666
Fixed-income contracts	-	822	-	822
Total	\$ 261,979	\$ 822	\$ -	\$ 262,801

Fair Value Measurements at June 30, 2018				
Asset Classes	Quoted Prices in			Total
	Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Cash and cash equivalents	\$ 5,808	\$ -	\$ -	\$ 5,808
Mutual funds:				
U.S. large cap	117,829	-	-	117,829
International	37,255	-	-	37,255
Fixed income	72,963	-	-	72,963
Real estate	14,612	-	-	14,612
Fixed-income contracts	-	722	-	722
Total	\$ 248,467	\$ 722	\$ -	\$ 249,189

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 13 - Pension and Other Postretirement Benefit Plans (Continued)

The tables above present information about the pension plan assets measured at fair value at June 30, 2020, 2019, and 2018 and the valuation techniques used by Covenant HealthCare to determine those fair values.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the Plan has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs, such as interest rates and yield curves, that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. Covenant HealthCare's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each plan asset.

Investments in Entities that Calculate Net Asset Value per Share

The pension plan holds shares or interests in investment companies whereby the fair value of the investment held is estimated based on net asset value per share (or its equivalent) of the investment company.

At June 30, the fair values of those investments are as follows:

	2020	2019	2018
Fixed-income common trust funds	\$ 43,610	\$ 37,972	\$ 33,411
International common trust funds	13,903	13,509	13,153
Real asset limited partnerships	590	749	991
Private equity limited partnerships	1,257	1,717	2,432
Hedge funds	-	-	1,010
Total	<u>\$ 59,360</u>	<u>\$ 53,947</u>	<u>\$ 50,997</u>

Cash Flow

Contributions

Covenant HealthCare expects to contribute \$6,612 to its pension plan and \$3,983 to its other postretirement benefit plan in 2021. The contribution amount for the pension plan includes the amount paid to the pension trust, and the contribution amount for the other postretirement plan includes amounts expected to be paid by Covenant HealthCare.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 13 - Pension and Other Postretirement Benefit Plans (Continued)

Estimated Future Benefit Payments

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

Years Ending	Pension Benefits	Other Postretirement Benefits
2021	\$ 20,449	\$ 3,983
2022	21,861	3,845
2023	21,394	3,688
2024	23,124	3,267
2025	24,301	2,910
Thereafter	114,443	10,317

The pension plan benefit payment amounts above also reflect the total benefits expected to be paid from the pension trust. The other postretirement plan benefit payment amounts above also reflect the total benefits expected to be paid from Covenant HealthCare's assets. As part of Covenant HealthCare's retiree health plan, \$1,500 per year is provided to eligible participants, based on years of service, to be used for health-related expenses after retirement.

In addition, Covenant HealthCare sponsors a deferred compensation plan for certain employees. Covenant HealthCare has recorded an asset and corresponding liability of \$17,342, \$15,910, and \$13,408 at June 30, 2020, 2019, and 2018, respectively, in the consolidated financial statements as other noncurrent assets and liabilities.

Note 14 - Defined Contribution Retirement Plan

Covenant HealthCare sponsors a defined contribution plan in which approximately 63 percent of its eligible employees participate. Employees who meet eligibility requirements specified by the plan may contribute to the plan. The plan provides for Covenant HealthCare to make a required matching contribution. Covenant HealthCare also may make additional contributions to the plan at its discretion. Expense under the defined contribution plan was \$9,568, \$9,224, and \$8,539 during 2020, 2019, and 2018, respectively.

Note 15 - Investments in Unconsolidated Entities

The following table summarizes Covenant HealthCare's investments in unconsolidated entities at June 30:

	2020	2019	2018
CMU Medical Education Partners	\$ 1,772	\$ 1,732	\$ 1,777
Covenant HealthCare Partners, Inc.	1,403	1,227	1,188
MMR - Mobile Medical Response	14,173	13,290	12,954
Mackinaw Surgery Center	497	1,571	1,650
Other	900	924	1,200
Total	\$ 18,745	\$ 18,744	\$ 18,769

CMU Medical Education Partners, formerly known as Synergy Medical Education, is a joint venture owned 5 percent by Covenant HealthCare that provides medical education to medical residents in the area.

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 15 - Investments in Unconsolidated Entities (Continued)

Covenant HealthCare Partners, Inc. is a joint venture owned 50 percent by Covenant HealthCare that provides health care services to the area.

Mobile Medical Response (MMR) is a joint venture owned 50 percent by Covenant HealthCare that provides emergency medical services to the area.

Mackinaw Surgery Center is a joint venture owned 46.2 percent by Covenant HealthCare that provides surgical facility services to the area.

The following is a summary of the financial position and results of operations for MMR, which is Covenant HealthCare's only significant investment accounted for under the equity method, as of and for the years ended June 30:

	2020	2019	2018
Assets	\$ 39,368	\$ 31,670	\$ 32,150
Liabilities	(11,022)	(5,090)	(6,242)
Equity	<u>\$ 28,346</u>	<u>\$ 26,580</u>	<u>\$ 25,908</u>
	2020	2019	2018
Revenue	\$ 45,604	\$ 46,446	\$ 45,353
Expenses	(44,047)	(45,510)	(42,889)
Net income	<u>\$ 1,557</u>	<u>\$ 936</u>	<u>\$ 2,464</u>

Note 16 - Functional Expenses

Covenant HealthCare fulfills the health requirements of residents within the communities it serves by providing, as its principal function, a complete array of health services. The consolidated financial statements report certain categories of expenses that are attributable to more than one program or supporting function; these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including benefits and depreciation and amortization, are allocated based on information, such as the percentage of salaries and wages, which are classified as health care or general and administrative services or total expenses by category for the remaining operating expenses.

Expenses related to providing these services, including \$8,439 of other components of net periodic benefit cost recorded in nonoperating income in the accompanying consolidated statement of operations and changes in net assets, are as follows for the year ended June 30, 2020:

	Health Care Services	General and Administrative	Total
Salaries and wages	\$ 293,662	\$ 34,716	\$ 328,378
Benefits	69,654	8,234	77,888
Supplies	128,993	428	129,421
Professional fees	10,263	2,725	12,988
Purchased services	45,546	17,916	63,462
Insurance	31	6,769	6,800
Utilities	5,610	421	6,031
Depreciation and amortization	27,294	3,722	31,016
Interest expense	3,530	-	3,530
Other	6,330	6,914	13,244
Total	<u>\$ 590,913</u>	<u>\$ 81,845</u>	<u>\$ 672,758</u>

Covenant HealthCare System and Subsidiaries

Notes to Consolidated Financial Statements

June 30, 2020, 2019, and 2018

(In Thousands)

Note 16 - Functional Expenses (Continued)

Expenses related to providing these services, including \$1,600 of other components of net periodic benefit cost recorded in nonoperating income in the accompanying consolidated statement of operations and changes in net assets, are as follows for the year ended June 30, 2019:

	Health Care Services	General and Administrative	Total
Salaries and wages	\$ 282,332	\$ 31,156	\$ 313,488
Benefits	67,115	7,406	74,521
Supplies	135,200	489	135,689
Professional fees	9,691	1,887	11,578
Purchased services	42,892	17,929	60,821
Insurance	387	1,247	1,634
Utilities	5,596	604	6,200
Depreciation and amortization	27,296	2,692	29,988
Interest expense	3,504	-	3,504
Other	5,015	8,941	13,956
Total	<u>\$ 579,028</u>	<u>\$ 72,351</u>	<u>\$ 651,379</u>

Expenses related to providing these services, including \$7,078 of other components of net periodic benefit cost recorded in nonoperating income in the accompanying consolidated statement of operations and changes in net assets, are as follows for the year ended June 30, 2018:

	Health Care Services	General and Administrative	Total
Salaries and wages	\$ 267,017	\$ 32,601	\$ 299,618
Benefits	68,754	8,396	77,150
Supplies	131,606	602	132,208
Professional fees	9,474	5,050	14,524
Purchased services	45,633	17,819	63,452
Insurance	264	5,741	6,005
Utilities	5,719	696	6,415
Depreciation and amortization	26,447	3,246	29,693
Interest expense	3,658	-	3,658
Other	4,667	7,552	12,219
Total	<u>\$ 563,239</u>	<u>\$ 81,703</u>	<u>\$ 644,942</u>

Note 17 - Contingencies

In addition to managing its professional liability claims, Covenant HealthCare is involved in litigation and regulatory investigations arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, these matters are expected to be resolved without material adverse effect on Covenant HealthCare's consolidated balance sheet.

Additional Information

Independent Auditor's Report on Additional Information

To the Board of Directors
Covenant HealthCare System and Subsidiaries

We have audited the consolidated financial statements of Covenant HealthCare System and Subsidiaries as of and for the year ended June 30, 2020 and have issued our report thereon dated October 26, 2020, which contained an unmodified opinion on those consolidated financial statements. Our audit was performed for the purpose of forming an opinion on the 2020 consolidated financial statements as a whole. The consolidating information in the accompanying schedules, as listed in the table of contents, is presented for the purpose of additional analysis rather than to present the financial position, results of operations, and cash flows of the individual companies and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the 2020 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the 2020 consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the 2020 consolidated financial statements as a whole.

Plante & Moran, PLLC

October 26, 2020

Covenant HealthCare System and Subsidiaries

Consolidating Balance Sheet

June 30, 2020
(In Thousands)

	Nonobligated Group	Obligated Group	Eliminating Entries	Total
Assets				
Current Assets				
Cash and cash equivalents	\$ 1,874	\$ 111,192	\$ -	\$ 113,066
Patient accounts receivable	2,581	65,123	-	67,704
Inventory	379	15,684	-	16,063
Due from affiliates	-	105	(105)	-
Estimated third-party payor settlements	-	1,002	-	1,002
Prepaid expenses and other	12	17,166	-	17,178
Total current assets	4,846	210,272	(105)	215,013
Assets Limited as to Use				
Funds held under bond agreements	-	37,630	-	37,630
Professional liability fund	-	4,386	-	4,386
By donors for specific purpose	-	16,318	-	16,318
Investments	15,446	434,789	-	450,235
Property and Equipment - Net	312	176,617	-	176,929
Other Assets				
Investments in unconsolidated entities	509	18,236	-	18,745
Other	-	24,939	-	24,939
Total other assets	509	43,175	-	43,684
Total assets	\$ 21,113	\$ 923,187	\$ (105)	\$ 944,195

Covenant HealthCare System and Subsidiaries

Consolidating Balance Sheet (Continued)

June 30, 2020
(In Thousands)

	Nonobligated Group	Obligated Group	Eliminating Entries	Total
Liabilities and Net Assets				
Current Liabilities				
Accounts payable and accrued expenses	\$ 359	\$ 27,286	\$ -	\$ 27,645
Current portion of long-term debt	-	4,510	-	4,510
Estimated third-party payor settlements	-	11,757	-	11,757
Medicare accelerated payments	-	61,681	-	61,681
Accrued liabilities and other:				
Accrued compensation and related amounts	511	45,636	-	46,147
Accrued interest payable	-	1,012	-	1,012
Due to affiliates	105	-	(105)	-
Current portion of accrued pension obligation	-	599	-	599
Current portion of accrued postretirement benefit obligation	-	3,928	-	3,928
Total current liabilities	975	156,409	(105)	157,279
Long-term Debt - Net of current portion	-	127,061	-	127,061
Other Liabilities				
Accrued pension obligation	-	49,694	-	49,694
Accrued postretirement benefit obligations	-	27,216	-	27,216
Reserve for professional liability claims	-	29,631	-	29,631
Other	-	20,034	-	20,034
Total other liabilities	-	126,575	-	126,575
Total liabilities	975	410,045	(105)	410,915
Net Assets				
Without donor restrictions	20,138	496,824	-	516,962
With donor restrictions	-	16,318	-	16,318
Total net assets	20,138	513,142	-	533,280
Total liabilities and net assets	\$ 21,113	\$ 923,187	\$ (105)	\$ 944,195

Covenant HealthCare System and Subsidiaries

Consolidating Statement of Operations

Year Ended June 30, 2020

(In Thousands)

	Nonobligated Group	Obligated Group	Eliminating Entries	Total
Unrestricted Revenue, Gains, and Other Support				
Net patient service revenue	\$ 10,857	\$ 600,880	\$ -	\$ 611,737
Investment income and realized gains and losses	-	180	-	180
Other revenue	1,742	36,750	-	38,492
Grant revenue	-	22,959	-	22,959
Total unrestricted revenue, gains, and other support	12,599	660,769	-	673,368
Expenses				
Salaries and wages	6,955	321,423	-	328,378
Benefits	1,465	67,984	-	69,449
Supplies	2,945	126,476	-	129,421
Professional fees	160	12,828	-	12,988
Purchased services	785	62,677	-	63,462
Insurance	1	6,799	-	6,800
Utilities	82	5,949	-	6,031
Depreciation and amortization	83	30,933	-	31,016
Interest expense	-	3,530	-	3,530
Other	439	12,805	-	13,244
Total expenses	12,915	651,404	-	664,319
Operating (Loss) Income	(316)	9,365	-	9,049
Nonoperating Income (Expense)				
Investment income	273	8,180	-	8,453
Realized and unrealized net gains on investments	174	9,352	-	9,526
Other components of net periodic benefit cost	-	(8,439)	-	(8,439)
Other	-	(3,780)	-	(3,780)
Total nonoperating income	447	5,313	-	5,760
Excess of Revenue Over Expenses	131	14,678	-	14,809
Other	-	(100)	-	(100)
Pension and Other Postretirement Benefit Obligation Adjustment	-	1,380	-	1,380
Increase in Net Assets without Donor Restrictions	\$ 131	\$ 15,958	\$ -	\$ 16,089

Covenant HealthCare System and Subsidiaries

Consolidating Balance Sheet - Obligated Group

June 30, 2020
(In Thousands)

	Covenant HealthCare Foundation	Covenant Medical Center, Inc.	Eliminating Entries	Total
Assets				
Current Assets				
Cash and cash equivalents	\$ 541	\$ 110,651	\$ -	\$ 111,192
Patient accounts receivable	-	65,123	-	65,123
Inventory	-	15,684	-	15,684
Due from affiliates	-	486	(381)	105
Estimated third-party payor settlements	-	1,002	-	1,002
Prepaid expenses and other	183	16,983	-	17,166
Total current assets	724	209,929	(381)	210,272
Assets Limited as to Use				
Funds held under bond agreements	-	37,630	-	37,630
Professional liability fund	-	4,386	-	4,386
By donors for specific purpose	16,318	-	-	16,318
Investments	8,939	425,850	-	434,789
Property and Equipment - Net	1	176,616	-	176,617
Other Assets				
Investments in unconsolidated entities	-	18,236	-	18,236
Other	-	24,939	-	24,939
Total other assets	-	43,175	-	43,175
Total assets	<u>\$ 25,982</u>	<u>\$ 897,586</u>	<u>\$ (381)</u>	<u>\$ 923,187</u>

Covenant HealthCare System and Subsidiaries

Consolidating Balance Sheet - Obligated Group (Continued)

June 30, 2020
(In Thousands)

	Covenant HealthCare Foundation	Covenant Medical Center, Inc.	Eliminating Entries	Total
Liabilities and Net Assets				
Current Liabilities				
Accounts payable and accrued expenses	\$ 265	\$ 27,021	\$ -	\$ 27,286
Current portion of long-term debt	-	4,510	-	4,510
Estimated third-party payor settlements	-	11,757	-	11,757
Medicare accelerated payments	-	61,681	-	61,681
Accrued liabilities and other:				
Accrued compensation and related amounts	57	45,579	-	45,636
Accrued interest payable	-	1,012	-	1,012
Due to affiliates	381	-	(381)	-
Current portion of accrued pension obligation	-	599	-	599
Current portion of accrued postretirement benefit obligation	-	3,928	-	3,928
Total current liabilities	703	156,087	(381)	156,409
Long-term Debt - Net of current portion	-	127,061	-	127,061
Other Liabilities				
Accrued pension obligation	-	49,694	-	49,694
Accrued postretirement benefit obligations	-	27,216	-	27,216
Reserve for professional liability claims	-	29,631	-	29,631
Other	-	20,034	-	20,034
Total other liabilities	-	126,575	-	126,575
Total liabilities	703	409,723	(381)	410,045
Net Assets				
Without donor restrictions	8,961	487,863	-	496,824
With donor restrictions	16,318	-	-	16,318
Total net assets	25,279	487,863	-	513,142
Total liabilities and net assets	\$ 25,982	\$ 897,586	\$ (381)	\$ 923,187

Covenant HealthCare System and Subsidiaries

Consolidating Statement of Operations - Obligated Group

Year Ended June 30, 2020

(In Thousands)

	Covenant HealthCare Foundation	Covenant Medical Center, Inc.	Eliminating Entries	Total
Unrestricted Revenue, Gains, and Other Support				
Net patient service revenue	\$ -	\$ 600,880	\$ -	\$ 600,880
Investment income and realized gains and losses	-	180	-	180
Other revenue	2,118	34,632	-	36,750
Grant revenue	-	22,959	-	22,959
Total unrestricted revenue, gains, and other support	2,118	658,651	-	660,769
Expenses				
Salaries and wages	695	320,728	-	321,423
Benefits	128	67,856	-	67,984
Supplies	807	125,669	-	126,476
Professional fees	-	12,828	-	12,828
Purchased services	51	62,626	-	62,677
Insurance	-	6,799	-	6,799
Utilities	3	5,946	-	5,949
Depreciation and amortization	-	30,933	-	30,933
Interest expense	-	3,530	-	3,530
Other	1,567	11,238	-	12,805
Total expenses	3,251	648,153	-	651,404
Operating (Loss) Income	(1,133)	10,498	-	9,365
Nonoperating Income (Expense)				
Investment income	327	7,853	-	8,180
Realized and unrealized net gains on investments	172	9,180	-	9,352
Other components of net periodic benefit cost	-	(8,439)	-	(8,439)
Other	-	(3,780)	-	(3,780)
Total nonoperating income	499	4,814	-	5,313
Excess of Revenue (Under) Over Expenses	(634)	15,312	-	14,678
Other	(100)	-	-	(100)
Pension and Other Postretirement Benefit Obligation Adjustment	-	1,380	-	1,380
(Decrease) Increase in Net Assets without Donor Restrictions	\$ (734)	\$ 16,692	\$ -	\$ 15,958

Covenant HealthCare System and Subsidiaries

Consolidating Balance Sheet - Nonobligated Group

June 30, 2020
(In Thousands)

	Covenant Development Corporation	Covenant HealthCare System	Visiting Nurse Association of Saginaw	Eliminating Entries	Total
Assets					
Current Assets					
Cash and cash equivalents	\$ 1,195	\$ 33	\$ 646	\$ -	\$ 1,874
Patient accounts receivable	-	-	2,581	-	2,581
Inventory	-	-	379	-	379
Prepaid expenses and other	12	-	-	-	12
Total current assets	1,207	33	3,606	-	4,846
Investments	5,861	8,298	1,287	-	15,446
Property and Equipment - Net	49	-	263	-	312
Other Assets					
Investments in unconsolidated entities	509	-	-	-	509
Long-term investments	-	7,605	-	(7,605)	-
Total other assets	509	7,605	-	(7,605)	509
Total assets	\$ 7,626	\$ 15,936	\$ 5,156	\$ (7,605)	\$ 21,113
Liabilities and Net Assets					
Current Liabilities					
Accounts payable and accrued expenses	\$ 24	\$ -	\$ 335	\$ -	\$ 359
Accrued liabilities and other:					
Accrued compensation and related amounts	-	-	511	-	511
Due to affiliates	-	-	105	-	105
Total current liabilities	24	-	951	-	975
Net Assets - Without donor restrictions	7,602	15,936	4,205	(7,605)	20,138
Total liabilities and net assets	\$ 7,626	\$ 15,936	\$ 5,156	\$ (7,605)	\$ 21,113

Covenant HealthCare System and Subsidiaries

Consolidating Statement of Operations - Nonobligated Group

Year Ended June 30, 2020

(In Thousands)

	Covenant Development Corporation	Covenant HealthCare System	Visiting Nurse Association of Saginaw	Eliminating Entries	Total
Unrestricted Revenue, Gains, and Other Support					
Patient service revenue	\$ -	\$ -	\$ 11,062	\$ (205)	\$ 10,857
Other revenue	999	1,059	743	(1,059)	1,742
Total unrestricted revenue, gains, and other support	999	1,059	11,805	(1,264)	12,599
Expenses					
Salaries and wages	-	-	6,955	-	6,955
Benefits	-	-	1,465	-	1,465
Supplies	-	-	2,945	-	2,945
Professional fees	-	-	160	-	160
Purchased services	36	-	954	(205)	785
Insurance	-	-	1	-	1
Utilities	-	-	82	-	82
Depreciation and amortization	-	-	83	-	83
Other	31	-	408	-	439
Total expenses	67	-	13,053	(205)	12,915
Operating Income (Loss)	932	1,059	(1,248)	(1,059)	(316)
Nonoperating Income					
Investment income	97	152	24	-	273
Realized and unrealized net gains on investments	29	126	19	-	174
Total nonoperating income	126	278	43	-	447
Increase (Decrease) in Net Assets without Donor Restrictions	\$ 1,058	\$ 1,337	\$ (1,205)	\$ (1,059)	\$ 131

Independent Auditor's Report

To the Board of Directors and Management
Covenant HealthCare System and Subsidiaries

We have audited, in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheet of Covenant HealthCare System and Subsidiaries (including Covenant Medical Center, Inc. and Covenant HealthCare Foundation, which comprise Covenant Medical Center Obligated Group) as of June 30, 2020 and the related consolidated statements of operations and changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements and have issued our report thereon, with an unmodified opinion, dated October 26, 2020.

In connection with our audit of the consolidated financial statements referred to above, nothing came to our attention that caused us to believe that Covenant Medical Center Obligated Group failed to comply with the terms, covenants, provisions, or conditions of Sections 6.27 through 6.33 of the Continuing Covenant Agreement dated April 1, 2014 between JPMorgan Chase Bank, National Association and Covenant Medical Center, Inc., as Obligated Group Agent, insofar as they relate to accounting matters. However, our audit of the consolidated financial statements was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Covenant Medical Center Obligated Group's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the Continuing Covenant Agreement dated April 1, 2014, insofar as they relate to accounting matters.

This report is intended solely for the information and use of management and the board of directors of Covenant HealthCare System and Subsidiaries and JPMorgan Chase Bank, National Association and is not intended to be and should not be used by anyone other than these specified parties.

Plante & Moran, PLLC

October 26, 2020

Independent Auditor's Report

To the Board of Directors and Management
Covenant HealthCare System and Subsidiaries

We have audited, in accordance with auditing standards generally accepted in the United States of America, the consolidated balance sheet of Covenant HealthCare System and Subsidiaries (including Covenant Medical Center, Inc. and the Covenant HealthCare Foundation, which comprise the Covenant Medical Center Obligated Group) as of June 30, 2020 and the related consolidated statements of operations and changes in net assets and cash flows for the year then ended and the related notes to the consolidated financial statements and have issued our report thereon, with an unmodified opinion, dated October 26, 2020.

In connection with our audit of the consolidated financial statements referred to above, nothing came to our attention that caused us to believe that Covenant Medical Center Obligated Group failed to comply with the terms, covenants, provisions, or conditions of Sections 506 through 510 of the master indenture dated July 15, 1991 between U.S. Bank National Association (successor to Comerica Bank) and Covenant Medical Center, Inc. (successor to St. Luke's Hospital), insofar as they relate to accounting matters. However, our audit of the consolidated financial statements was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding Covenant Medical Center Obligated Group's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the master indenture dated July 15, 1991, insofar as they relate to accounting matters.

This report is intended solely for the information and use of management and the board of directors of Covenant HealthCare System and Subsidiaries and U.S. Bank National Association and is not intended to be, and should not be, used by anyone other than these specified parties.

Plante & Moran, PLLC

October 26, 2020

Independent Auditor's Report

To the Board of Directors and Management
Covenant HealthCare System and Subsidiaries

We have audited, in accordance with auditing standards generally accepted in the United States of America, the accompanying consolidated financial statements of Covenant HealthCare System and Subsidiaries (including Covenant Medical Center, Inc. and Covenant HealthCare Foundation, which comprise Covenant Medical Center Obligated Group), which comprise the consolidated balance sheet as of June 30, 2020 and the related consolidated statements of operations and changes in net assets and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon, with an unmodified opinion, dated October 26, 2020.

In connection with our audit of the consolidated financial statements referred to above, nothing came to our attention that caused us to believe that Covenant Medical Center Obligated Group failed to comply with the Historical Debt Service Coverage Ratio, as prescribed by Section 512(2) of the master indenture dated July 15, 1991 between U.S. Bank National Association (successor to Comerica Bank) and Covenant Medical Center, Inc. (successor to St. Luke's Hospital), insofar as they relate to accounting matters. However, our audit of the consolidated financial statements was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding Covenant Medical Center Obligated Group's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the master indenture dated July 15, 1991, insofar as they relate to accounting matters.

This report is intended solely for the information and use of management and the board of directors of Covenant HealthCare System and Subsidiaries and U.S. Bank National Association and is not intended to be, and should not be, used by anyone other than these specified parties.

Plante & Moran, PLLC

October 26, 2020

Covenant HealthCare System and Subsidiaries
Historical Debt Service Coverage Ratio of the Covenant Medical Center Obligated Group

Year Ended June 30, 2020
(In Thousands)

Excess of revenue over expenses		14,678
Adjustments:		
Depreciation and amortization		30,933
Interest expense		3,530
Unrealized losses on investments		1,089
Loss on extinguishment of debt		491
Total net revenue (1)	\$	<u>50,721</u>
Total Historical Principal and Interest Requirements (1)	\$	<u>10,240</u>
Historical Debt Service Coverage Ratio (1)		<u>4.95</u>

(1) - This term is defined in the "Master Indenture" dated as of July 15, 1991 between U.S. Bank National Association (successor to Comerica Bank) and Covenant Medical Center, Inc. (successor to St. Luke's Hospital). The methodology for computing the Historical Debt Service Coverage Ratio is prescribed by Section 101 of the Master Indenture.

COVENANT HEALTHCARE SYSTEM AND SUBSIDIARIES

Consolidated Balance Sheets

	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20		Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
<i>(In Thousands)</i>							
Assets				Liabilities and net assets			
Current assets:				Current liabilities:			
Cash and cash equivalents	\$30,880	\$35,116	\$113,066	Accounts payable and accrued expenses	\$18,274	\$13,017	\$27,645
Net patient accounts receivable	70,475	74,647	67,704	Advance Payments	0	0	61,681
Estimated third-party settlements	1,601	2,864	1,002	Estimated third-party payable	3,798	6,134	11,757
Current portion of funds held under bond agreements	3,665	-	-	Accrued compensation and related amounts	39,121	36,795	46,147
Inventories	16,463	16,554	16,063	Accrued interest payable and other current liabilities	1,490	1,434	1,012
Prepaid expenses and other	16,724	14,736	17,178	Current portion of accrued postretirement benefits	-	3,757	3,928
Total current assets	139,808	143,917	215,013	Current portion accrued pension obligation	-	7,439	599
				Current portion of long-term debt	6,505	6,710	4,510
Assets whose use is limited, less current portion:				Total current liabilities	69,188	75,286	157,279
Funds held under bond agreements	-	-	37,630	Long-term debt, less current portion	82,805	93,194	127,061
Professional liability fund	5,730	4,524	4,386				
Restricted assets	12,763	13,074	16,318	Other Liabilities:			
	18,493	17,598	58,334	Accrued post retirement benefits	30,976	28,362	27,216
Investments	403,212	423,710	450,235	Accrued pension	46,305	51,193	49,694
				Other noncurrent liabilities	48,782	44,052	49,665
Property and equipment	175,671	179,850	176,929	Total noncurrent liabilities	126,063	123,607	126,575
				Total Liabilities	278,056	292,087	410,915
Other assets				Net assets:			
Investments in unconsolidated affiliates	18,769	18,744	18,745	Net assets without donor restrictions	487,849	500,873	516,962
Other	22,714	22,215	24,939	Net assets with donor restrictions	12,762	13,074	16,318
	41,483	40,959	43,684	Total noncurrent liabilities	500,611	513,947	533,280
Total assets	778,667	806,034	944,195	Total liabilities and net assets	\$778,667	\$806,034	\$944,195

COVENANT HEALTHCARE SYSTEM AND SUBSIDIARIES
Consolidated Statements Of Operations

	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
	<i>(In Thousands)</i>		
Revenue and support:			
Net patient service revenue	\$631,268	\$632,629	\$611,737
Other revenue	40,812	30,148	38,492
Grant revenue	0	0	22,959
Investment income	463	96	84
Realized and other than temporary losses, net	151	450	96
Total revenue & support	<u>672,694</u>	<u>663,323</u>	<u>673,368</u>
Expenses:			
Salaries & wages	299,618	313,488	328,378
Benefits	70,072	72,921	69,449
Professional fees	14,524	11,578	12,988
Supplies	132,208	135,689	129,421
Other purchased services	63,452	60,821	63,462
Other	12,219	13,956	13,244
Utilities	6,415	6,200	6,031
Insurance	6,005	1,634	6,800
Interest	3,658	3,504	3,530
Depreciation and amortization	29,693	29,988	31,016
Total expenses	<u>637,864</u>	<u>649,779</u>	<u>664,319</u>
Income (loss) from operations	34,830	13,544	9,049
Investment income	7,492	9,160	8,453
Realized and unrealized net gains on investments	15,273	11,990	9,526
Other non-operating gains (losses)	500	464	(3,289)
Net Periodic Pension Cost	(7,078)	(1,600)	(8,439)
Gain/(Loss) on refunding	-	-	(491)
Total Non Operating Income	<u>16,187</u>	<u>20,014</u>	<u>5,760</u>
Excess (deficit) of revenues over expenses	<u>\$51,017</u>	<u>\$33,558</u>	<u>\$14,809</u>

COVENANT MEDICAL CENTER
Statistical Summary

	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
Discharges - Acute	29,340	27,653	26,469
Discharges - Rehab	830	866	872
Discharges - Skilled Nursing	492	452	456
Total Discharges (Includes Newborn)	30,662	28,971	27,797
Patient Days - Acute	141,814	132,912	129,706
Patient Days - Rehab	10,499	10,561	10,442
Patient Days - Skilled Nursing	6,226	6,543	5,777
Total Patient Days (Includes Newborn)	158,539	150,016	145,925
Equivalent Discharges (Excluding Newborn)	58,049	58,338	54,520
Equivalent Patient Days (Excluding Newborn)	308,565	309,992	294,429
Average Length of Stay - Acute (Discharges)	4.83	4.81	4.90
Average Length of Stay - Total (Discharges)	5.17	5.18	5.25
Average Daily Census	434	411	399
Newborn Discharges	2,616	2,481	2,471
Newborn Patient Days	5,107	4,939	4,757
Total ECC Admissions	23,741	24,343	23,980
Total ECC Visits	93,467	93,757	86,859
Surgical Cases - Inpatient	5,894	5,836	5,496
Surgical Cases - Outpatient	8,381	8,673	7,393
Cath Lab-EP Lab Procedures	7,979	7,384	6,662
Physician Office Visits (MSO)	312,511	344,250	325,336
MedExpress	106,624	108,610	97,306
Total FTE's	4,005.0	3,988.0	3,951.0
Payor Mix			
Medicare	46.51%	45.76%	45.97%
Blue Cross	12.21%	12.28%	12.58%
Medicaid	18.51%	18.53%	19.00%
HMO and PPO	2.44%	2.88%	2.53%
Other	<u>12.39%</u>	<u>12.06%</u>	<u>11.71%</u>
Hospital Services	92.06%	91.51%	91.79%
Physician Services	<u>7.94%</u>	<u>8.48%</u>	<u>8.21%</u>
Other Services	7.94%	8.48%	8.21%
Total Services	100.00%	100.00%	100.00%
Percentage of Occupancy			
Licensed Beds	67.55%	63.92%	62.01%
Available Beds-Inc. NB	72.88%	68.96%	66.90%
Case Mix			
Medicare	1,7318	1,7572	1,8050
Total	1,5160	1,5425	1,5589

COVENANT HEALTHCARE SYSTEM AND SUBSIDIARIES**Consolidated Statements Of Operations**

	Audited	Audited	Audited
	Year Ended	Year Ended	Year Ended
	Jun-30-18	Jun-30-19	Jun-30-20
	<i>(In Thousands)</i>		
Revenue and support:			
Net patient service revenue	\$631,268	\$632,629	\$611,737
Other revenue	40,812	30,148	38,492
Grant revenue	-	-	22,959
Investment income	463	96	84
Realized and other than temporary losses, net	151	450	96
Total revenue & support	<u>672,694</u>	<u>663,323</u>	<u>673,368</u>
Expenses:			
Operating expenses	604,513	616,287	629,773
Depreciation and amortization	3,658	3,504	3,530
Interest	29,693	29,988	31,016
Total expenses	<u>637,864</u>	<u>649,779</u>	<u>664,319</u>
Income (loss) from operations	34,830	13,544	9,049
Investment income	7,492	9,160	8,453
Realized and unrealized net gains on investments	15,273	11,990	9,526
Net Periodic Pension Cost	(7,078)	(1,600)	(8,439)
Gain on refunding and other non-operating gains (losses)	500	464	(3,780)
Excess (deficit) of revenues over expenses	<u>\$51,017</u>	<u>\$33,558</u>	<u>\$14,809</u>

COVENANT MEDICAL CENTER**Utilization Data**

The data is derived from the Medical Center's internal reports

	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
Beds Licensed	643	643	643
Beds Staffed	596	596	596
Discharges			
Acute Care	26,724	25,172	23,998
Rehabilitation	830	866	872
Transitional Care Unit	492	452	456
	<u>28,046</u>	<u>26,490</u>	<u>25,326</u>
Newborn	2,616	2,481	2,471
Total Discharges	<u>30,662</u>	<u>28,971</u>	<u>27,797</u>
Patient Days			
Acute Care	136,707	127,973	124,949
Rehabilitation	10,499	10,561	10,442
Transitional Care Unit	6,226	6,543	5,777
	<u>153,432</u>	<u>145,077</u>	<u>141,168</u>
Newborn	5,107	4,939	4,757
Total Patient Days	<u>158,539</u>	<u>150,016</u>	<u>145,925</u>
Percent of Occupancy			
Based on Staffed Beds	73%	69%	67%
Acute Care Average Length of Stay	4.83	4.81	4.90
Surgical Procedures			
Inpatient	5,894	5,836	5,496
Outpatient	8,381	8,673	7,393
Outpatient Visits	503,745	510,255	464,893
Emergency Room Visits	93,467	93,757	86,859
Case Mix Index (all Medicare patients)	1.73	1.76	1.81

COVENANT HEALTHCARE SYSTEM AND SUBSIDIARIES

Days Cash, Debt to Capitalization, Sources of Revenue

	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
	<i>(In Thousands)</i>		
Cash and cash equivalents	\$30,880	\$35,116	\$113,066
Investments	415,975	436,784	466,553
Total Cash	446,855	471,900	579,619
Less: Restricted Cash from Foundation	5,730	4,524	4,386
Total Unrestricted Cash	\$441,125	\$467,376	\$575,233

Days Cash on Hand	254	264	319
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	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
	<i>(In Thousands)</i>		
Long-term debt (including current maturities)			
Series 2020 K Bonds	\$ -	\$ -	\$ 40,110
Series 2020 J Bonds	-	-	55,325
Series 2010 H Bonds	\$58,975	56,780	-
Series 2014 I Bonds	23,490	19,970	16,375
2019 PNC Debt	-	17,075	1,675
JPM 2015 Loan	6,995	6,205	5,390
Unamortized Premium/Debt issuance cost	(150)	(126)	12,696
Total long-term debt	89,310	99,904	131,571
Unrestricted net assets	487,849	500,873	516,962
Total Capitalization	\$577,159	\$600,777	648,533

Debt to Capitalization	15.47%	16.63%	20.29%
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	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
Sources of Revenue			
Hospital Services			
Medicare	46.51%	45.76%	45.97%
Blue Cross	12.21%	12.28%	12.58%
Medicaid	18.51%	18.53%	19.00%
HMO and PPO	2.44%	2.88%	2.53%
Other	12.39%	12.06%	11.71%
Hospital Services	92.06%	91.51%	91.79%
Other Services			
Physician Services	7.94%	8.48%	8.21%
Home Health and Other	0.00%	0.00%	0.00%
Total	100.00%	100.00%	100.00%

COVENANT HEALTHCARE SYSTEM OBLIGATED GROUP

Maximum Annual Debt Service Coverage

	Audited Year Ended Jun-30-18	Audited Year Ended Jun-30-19	Audited Year Ended Jun-30-20
	<i>(In Thousands)</i>		
Excess (deficit) of revenue over expenses	\$49,907	\$32,670	\$14,678
Depreciation and amortization	29,639	29,935	30,933
Interest	3,658	3,504	3,530
(Gain)/loss on bond refunding	-	-	491
Excess before interest, depreciation, and amortization	<u>83,204</u>	<u>66,109</u>	<u>49,632</u>
Unrealized losses on investments	-	-	1,089
Realized (losses) on investment transactions related to other than temporary investments	-	-	-
Earnings before interest, depreciation, amortization, refunding loss, and adjustments for other than temporary losses on investments	<u>\$83,204</u>	<u>\$66,109</u>	<u>\$50,721</u>
Divided by:			
Maximum annual debt service (1)	<u>\$10,010</u>	<u>\$12,090</u>	<u>\$12,395</u>
Maximum Annual Debt Service Coverage (2)	8.3	5.5	4.1

(1) The maximum annual debt service includes debt service on the Series 2014 I Bonds, Series 2020K Bond initiated March 2020, Series 2020J Bond initiated April 2020, JPMorgan taxable loan initiated in May 2015 and the PNC Term Loan which was initiated June 25, 2019. The fiscal year 2020 maximum debt service amount represents twelve months of the annual debt service total.

(2) Based on annualized earnings before interest, depreciation, amortization and adjustments for other than temporary losses on investments for fiscal year ending 2020.