



*Report of Independent Auditors and  
Consolidated Financial Statements*

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers**

*August 31, 2019 and 2018*



# Table of Contents

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<b>REPORT OF INDEPENDENT AUDITORS</b> .....	1
<b>CONSOLIDATED FINANCIAL STATEMENTS</b>	
Consolidated balance sheets.....	4
Consolidated statements of operations.....	5
Consolidated statements of changes in net assets.....	6
Consolidated statements of cash flows.....	7
Notes to consolidated financial statements.....	8
<b>SINGLE AUDIT</b>	
Schedule of expenditures of federal awards.....	41
Notes to schedule of expenditures of federal awards.....	42
<b>REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF CONSOLIDATED FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i></b> .....	43
<b>REPORT OF INDEPENDENT AUDITORS ON COMPLIANCE FOR THE MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE AS REQUIRED BY THE UNIFORM GUIDANCE</b> .....	45
<b>SCHEDULE OF FINDINGS AND QUESTIONED COSTS</b> .....	47
<b>SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS</b> .....	49

## **Report of Independent Auditors**

The Board of Trustees  
Community Hospitals of Central California and Affiliated Corporations  
dba Community Medical Centers

### **Report on the Financial Statements**

We have audited the accompanying consolidated financial statements of Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers (CMC), which comprise the consolidated balance sheets as of August 31, 2019 and 2018, the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 consolidated balance sheets of CMC as of August 31, 2019 and 2018, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## ***Emphasis of Matter***

As discussed in Note 2 to the consolidated financial statements, as of August 31, 2019, CMC adopted Financial Accounting Standards Board ("FASB") Accounting Standards Update ("ASU") 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements for Not-for-Profit Entities*. The ASU has been applied retrospectively to all periods presented with the exception of the omission of certain information as permitted by the ASU. Our opinion is not modified with respect to this matter.

As discussed in Note 2 to the consolidated financial statements, for the year ended August 31, 2019, CMC adopted FASB ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The ASU has been applied using the modified retrospective transition approach in the year of adoption. Our opinion is not modified with respect to this matter.

## ***Other Matters***

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements of Federal Awards*, is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

## ***Other Reporting Required by Government Auditing Standards***

In accordance with Government Auditing Standards, we have also issued our report dated November 22, 2019 on our consideration of CMC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of CMC's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering CMC's internal control over financial reporting and compliance.

*Mass Adams LLP*

San Francisco, California  
November 22, 2019

## **Consolidated Financial Statements**

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**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Consolidated Balance Sheets (In Thousands)  
August 31, 2019 and 2018**

	2019	2018
<b>ASSETS</b>		
Current assets:		
Cash and equivalents	\$ 143,340	\$ 88,934
Short-term investments	17,150	14,305
Patient accounts receivable (less allowance for doubtful accounts of \$0 in 2019 and \$69,974 in 2018)	270,308	237,892
Due from State of California for supplemental funding	11,570	20,361
Other receivables	28,274	76,744
Inventories	14,903	16,047
Prepaid expenses and other	67,899	64,710
	<u>553,444</u>	<u>518,993</u>
Assets limited as to use:		
Board-designated assets	616,542	575,791
Assets held by trustee for:		
Self-insurance in captive insurance company	16,923	20,811
Donor-restricted assets	29,664	29,939
	<u>663,129</u>	<u>626,541</u>
Property, plant, and equipment, net	879,137	901,996
Construction in progress	107,301	47,882
Net pension benefit asset	-	13,442
Other assets	138,362	127,758
	<u>\$ 2,341,373</u>	<u>\$ 2,236,612</u>
<b>LIABILITIES AND NET ASSETS</b>		
Current liabilities:		
Accounts payable	\$ 69,883	\$ 63,454
Accrued compensation and employee benefits	99,057	90,420
Estimated third-party settlements	88,167	57,590
Other accrued liabilities and deferred revenue	150,316	222,556
Current maturities of long-term debt	11,905	9,890
	<u>419,328</u>	<u>443,910</u>
Long-term debt, less current maturities	532,887	537,701
Pension benefit obligation	13,837	-
Other long-term obligations	43,459	40,574
	<u>1,009,511</u>	<u>1,022,185</u>
Net assets:		
Without donor restrictions	1,302,198	1,184,488
With donor restrictions	29,664	29,939
	<u>1,331,862</u>	<u>1,214,427</u>
	<u>\$ 2,341,373</u>	<u>\$ 2,236,612</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Consolidated Statements of Operations (In Thousands)  
Years Ended August 31, 2019 and 2018**

	<u>2019</u>	<u>2018</u>
Revenues, gains, and other support without donor restrictions:		
Net patient service revenues	\$ 1,684,029	\$ 1,707,330
Less: Provision for bad debts	<u>-</u>	<u>(113,804)</u>
	<u>1,684,029</u>	<u>1,593,526</u>
Premium revenue	42,699	9,254
Investment income	27,459	16,585
Other revenue	<u>59,022</u>	<u>48,245</u>
	<u>1,813,209</u>	<u>1,667,610</u>
Expenses:		
Salaries, wages, and benefits	769,276	723,507
Supplies	308,472	276,282
Outside services	311,319	270,334
Insurance	8,050	14,451
Depreciation and amortization	80,447	74,631
Rental and lease	9,522	9,857
Interest	20,922	20,195
Utilities	17,750	16,862
Other	47,123	40,466
Quality assurance fee	<u>99,125</u>	<u>130,257</u>
	<u>1,672,006</u>	<u>1,576,842</u>
Excess of revenues, gains, and other support over expenses	<u>141,203</u>	<u>90,768</u>
Net change in unrealized gains and losses on investments	-	(64)
Net assets released from restrictions for equipment acquisition	3,123	6,537
Change in pension benefit obligation	(26,616)	11,254
Other	<u>-</u>	<u>1</u>
Change in net assets without donor restrictions	<u>\$ 117,710</u>	<u>\$ 108,496</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Consolidated Statements of Changes in Net Assets (In Thousands)  
Years Ended August 31, 2019 and 2018**

	Without donor restrictions	With donor restrictions	Total
Balance at August 31, 2017	\$ 1,075,992	\$ 22,609	\$ 1,098,601
Excess of revenues, gains, and other support over expenses	90,768	-	90,768
Net change in unrealized gains and losses on investments	(64)	-	(64)
Donor-restricted contributions	-	15,439	15,439
Net assets released from restrictions and used for operations	-	(1,572)	(1,572)
Net assets released from restrictions for equipment acquisition	6,537	(6,537)	-
Change in pension benefit obligation	11,254	-	11,254
Other	1	-	1
	<u>108,496</u>	<u>7,330</u>	<u>115,826</u>
Balance at August 31, 2018	<u>1,184,488</u>	<u>29,939</u>	<u>1,214,427</u>
Excess of revenues, gains, and other support over expenses	141,203	-	141,203
Donor-restricted contributions	-	4,387	4,387
Net assets released from restrictions and used for operations	-	(1,539)	(1,539)
Net assets released from restrictions for equipment acquisition	3,123	(3,123)	-
Change in pension benefit obligation	(26,616)	-	(26,616)
	<u>117,710</u>	<u>(275)</u>	<u>117,435</u>
Balance at August 31, 2019	<u>\$ 1,302,198</u>	<u>\$ 29,664</u>	<u>\$ 1,331,862</u>



**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Consolidated Statements of Cash Flows (In Thousands)  
Years Ended August 31, 2019 and 2018**

	2019	2018
Cash flows from operating activities:		
Change in net assets	\$ 117,435	\$ 115,826
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Net unrealized gains on investments	-	(64)
Donor-restricted contributions	(6,895)	(14,698)
Provision for bad debts	-	113,804
Depreciation and amortization	80,447	74,631
Amortization of bond premium	(1,890)	(2,229)
Net changes in operating assets and liabilities:		
Patient accounts receivable and other receivables	16,054	(162,638)
Due from State of California for supplemental funding	8,791	3,534
Inventories, prepaid expenses, and other	(15,498)	(39,387)
Accounts payable and other accrued liabilities	(62,926)	145,469
Accrued compensation and employee benefits	8,637	8,421
Pension benefit obligation	27,279	(28,366)
Estimated third-party settlements	30,577	10,787
Net cash provided by operating activities	202,011	225,090
Cash flows from investing activities:		
Purchases of property, plant, and equipment, net	(114,158)	(125,081)
Purchase of investments	(373,285)	(510,872)
Proceeds from sales of investments	333,852	438,089
Net cash used in investing activities	(153,591)	(197,864)
Cash flows from financing activities:		
Repayments of long-term debt	(12,088)	(21,571)
Proceeds from long-term debt	11,179	4,042
Proceeds from donor-restricted contributions	6,895	14,698
Net cash provided by (used in) financing activities	5,986	(2,831)
Cash and equivalents, beginning of year	54,406	24,395
	88,934	64,539
Cash and equivalents, end of year	\$ 143,340	\$ 88,934
Supplemental disclosure of cash flow information:		
Interest paid, net of amounts capitalized	\$ 25,398	\$ 23,919

# Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers

## Notes to Consolidated Financial Statements

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### NOTE 1 – ORGANIZATION

Community Hospitals of Central California and Affiliated Corporations, dba Community Medical Centers (CMC), is a not-for-profit multi-facility integrated health care organization located in Fresno, California. CMC has established an Obligated Group to access capital markets. Obligated Group members are jointly and severally liable for the long-term debt outstanding under the Obligated Group's master trust indenture. The Obligated Group members are denoted with an asterisk (\*). CMC includes the following consolidated entities:

**Acute care services** – Acute care services consist of a single corporate entity, Fresno Community Hospital and Medical Center\*, which operates as two general acute care hospitals that provide a full range of medical, surgical, intensive care, emergency room, burn and trauma, and obstetric services. These facilities also offer home health, psychiatric, rehabilitation, and a variety of other services. The acute care hospitals are:

- Community Regional Medical Center (CRMC)
- Clovis Community Medical Center (CCMC)

**Corporate activities** – Corporate activities consist of centralized shared services, real estate activities and retail pharmacy operations.

- Community Hospitals of Central California\* (CHCC)
- Community Health Enterprises (CHE)

**Community Insurance Services Company** – Community Insurance Services Company (CISC), is a wholly owned captive insurance company that maintains professional and general liability coverage and has no income tax obligation.

**Community Care Health Plan** – Community Care Health Plan (CCHP), is a wholly owned Knox-Keene licensed Health Maintenance Organization that provides health insurance coverage to the employees of CMC and entities partially owned by CMC, as well as to local employers.

**Development activities** – Development activities consist of a single corporate entity, Community Hospitals of Central California Foundation, which conducts fundraising activities for the not-for-profit organizations within the health system.

**Obligated Group members** – Obligated Group members are the parent corporations of certain consolidated entities that are not Obligated Group members. Accounting principles generally accepted in the United States of America (U.S. GAAP) require consolidation of all controlled subordinate corporations. Accordingly, the consolidated financial statements of CMC are the same as the Obligated Group financial statements under U.S. GAAP.

CMC also includes the following nonconsolidated entities:

**California Imaging Institute LLC (CII)** – Operates three freestanding outpatient imaging centers that provide comprehensive imaging services. It is owned in partnership with a physician-owned radiology medical group. Fresno Community Hospital and Medical Center accounts for this investment using the equity method.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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**Santé Health System (Santé)** – A management service organization (MSO) that provides independent physician association and physician practice management services. CMC accounts for the investment in Santé using the equity method.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of consolidation** – The consolidated financial statements include the accounts of CMC and affiliates as listed under Organization in Note 1. All significant intercompany accounts and transactions have been eliminated in consolidation.

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

**Cash and equivalents** – Cash and equivalents include all highly liquid investments with an original maturity of three months or less when purchased. Cash and equivalents purchased by CMC’s investment managers as part of their investment strategies are included in assets limited as to use and short-term investments. CMC regularly maintains balances in depository accounts in excess of the FDIC insurance limit.

**Accounts receivable** – CMC’s primary concentration of credit risk is patient accounts receivable and SB855 and SB1255 disproportionate share funds receivable, which consist of amounts owed by various government agencies, insurance companies and private patients. CMC manages the receivables by regularly reviewing its accounts and contracts and by providing appropriate allowances for uncollectible amounts. CMC provides for estimated losses on patient accounts receivable based on prior collections experience. Uncollectible receivables are charged-off when deemed uncollectible. Recoveries from previously charged-off accounts are recorded when received. The mix of receivables from third-party payors and patients at August 31, 2019 and 2018, is as follows:

	<u>2019</u>	<u>2018</u>
Medicare	12%	10%
Managed Medicare	6%	7%
Medi-Cal	8%	12%
Managed Medi-Cal	15%	16%
Contracts	54%	49%
Self-Pay and Others	<u>5%</u>	<u>6%</u>
Total	<u>100%</u>	<u>100%</u>

**Inventories** – Inventories are stated at the lower of cost, determined by the first-in, first-out method, or market.

# Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers Notes to Consolidated Financial Statements

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**Assets limited as to use and short-term investments** – Assets limited as to use consist principally of corporate debt securities, equity securities and U.S. government and agency securities, all of which are designated as trading securities and carried at fair market value. The fair values for these investments are based on quoted market prices. Investments also include repurchase agreements. Certain marketable securities are designated as assets held in trust. These include assets held by trustees in accordance with the professional liability self-insurance arrangement with a captive insurance company. In addition, certain investments are set aside by the board of trustees for future capital improvements.

Investment income is included in the excess of revenues, gains and other support over expenses unless the income is restricted by donor or law.

CMC has elected to report investments in debt and equity securities under Accounting Standards Codification (ASC) 825, *Financial Instruments*, such that unrealized gains and losses on trading securities are included in the excess of revenues, gains and other support over expenses unless the income is restricted by donor or law.

CMC has discretion to establish policies regarding which portion of assets limited as to use is classified as short-term investments. The amount classified as short-term investments consists of available cash held in investment accounts, money markets balances and highly liquid investment securities with an original maturity of three months or less.

**Property, plant, and equipment** – Property, plant, and equipment are stated at cost, or in the case of donated items, at fair market value at the date of donation. Routine maintenance and repairs are charged to expense as incurred. Expenditures that increase values, change capacities, or extend useful lives are capitalized, as is interest for significant construction projects. In 2019 and 2018, \$2,594,803 and \$5,255,000, respectively, of net interest expense was capitalized for construction projects.

Depreciation is computed by the straight-line method over the estimated useful lives of the assets, which range from 10 to 25 years for land improvements, 5 to 40 years for buildings and improvements, and an average of 8 years for equipment.

CMC's management regularly reviews long-lived assets for indications of impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Management estimates the fair value of legal asset retirement obligations that are conditional on a future event if the amount can be reasonably estimated, in accordance with Financial Accounting Standards Board (FASB). Estimates are developed through the identification of applicable legal requirements, identification of specific conditions requiring incremental cost at time of asset disposal, estimation of costs to remediate conditions and estimation of remaining useful lives or date of asset disposal.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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**Self-insurance and other benefit plans** – CMC is self-insured for workers' compensation claims and maintains a self-insured medical, dental, and vision care plan as an option for its employees. Claims are accrued under these plans as the incidents that give rise to them occur. Unpaid claim accruals are based on the actuarially estimated ultimate cost of settlement, including claim settlement expenses. CMC has reinsurance arrangements with insurance companies to limit its losses on claims for medical and workers' compensation expenses. The portion not expected to be paid within one year is included within other long-term obligations. As of August 31, 2019, CMC has a claims liability of \$50,650,000 and a corresponding insurance recovery receivable of \$3,148,000 for medical and workers' compensation claims that are insured by a third-party excess loss policy. As of August 31, 2018, CMC has a claims liability of \$44,422,000 and a corresponding insurance recovery receivable of \$1,047,000 for medical and workers' compensation claims that are insured by a third-party excess loss policy. The claims liability is classified in other accrued liabilities and deferred revenue and other long-term obligations and the insurance recovery receivable is classified in prepaid expenses and other and other assets, respectively, in the accompanying consolidated balance sheets.

**Professional and general liability insurance** – CISC, CMC's wholly owned captive insurance company, has issued claims-made policies to insure the professional and general liability risks of CMC's affiliates. Through August 31, 2016, CISC retained \$2,000,000 per incident and \$15,000,000 in the aggregate; effective September 1, 2016, CISC retained \$3,000,000 for the first incident and \$2,000,000 for subsequent incidents with \$15,000,000 in the aggregate; effective September 1, 2017, CISC retained \$4,000,000 for the first incident and \$2,000,000 for subsequent incidents with \$15,000,000 in the aggregate. CISC is reinsured up to \$80,000,000 per incident and in the aggregate with third-party reinsurers. As of August 31, 2019, CMC has recorded estimated liabilities for claims incurred and reported of \$12,881,000 and a corresponding insurance recovery receivable of \$1,698,000. As of August 31, 2018, CMC has recorded estimated liabilities for claims incurred and reported of \$27,619,000 and a corresponding insurance recovery receivable of \$10,914,000. The estimated liabilities for claims incurred and reported is classified in other accrued liabilities and deferred revenue and other long-term obligations and the insurance recovery receivable is classified in prepaid expenses and other and other assets, respectively, in the accompanying consolidated balance sheets.

Should the reinsurance policies not be renewed or replaced with equivalent insurance, claims related to occurrences during the term of the claims-made policy but reported subsequent to its termination may be uninsured. Liabilities of \$4,329,000 and \$4,230,000 have been recorded for the actuarially-estimated incurred but not reported liability at August 31, 2019 and 2018, respectively. These liabilities are included within other long-term obligations in the accompanying consolidated balance sheets.

**Income taxes** – Most entities included in CMC are exempt from taxation under Section 501(c)(3) of the Internal Revenue Code and Section 23701d of the California Revenue and Taxation Code and are generally not subject to federal or state income taxes. However, the exempt organizations are subject to income taxes on any net income that is derived from a trade or business, regularly carried on and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the basic financial statements taken as a whole. CMC includes entities that are subject to income taxes; however, such income tax activities are not significant to the consolidated financial statements.

# Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers Notes to Consolidated Financial Statements

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**Donor gifts** – Unconditional promises to give cash and other assets to CMC are reported at fair market value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair market value at the date the gift is received and any conditions are substantially met. The gifts are reported as support with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified as net assets without donor restrictions.

**Fair value of financial instruments** – Unless otherwise indicated, the fair value of all reported assets and liabilities, which represent financial instruments, approximate their carrying values. CMC's policy is to recognize transfers in and transfers out of Levels 1 and 2 as of the end of the reporting period.

**Excess of revenues, gains, and other support over expenses** – Excess of revenues, gains, and other support over expenses reflected in the accompanying consolidated statements of operations includes all changes in net assets without donor restrictions other than net assets released from restrictions for equipment acquisition, changes in pension benefit obligation, and net change in unrealized gains and losses on investments.

**Reclassifications** – Certain amounts in the 2018 financial statements have been reclassified to conform to the 2019 presentation.

**Recent accounting pronouncements** – In May 2014, the FASB issued Accounting Standards Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (“ASU 2014-09”). As compared to existing guidance on revenue recognition, ASU 2014-09 will significantly enhance comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets. The largely principles-based guidance in ASU 2014-09 will provide a framework for addressing revenue recognition issues comprehensively for entities that apply U.S. GAAP in addition to those entities that apply International Financial Reporting Standards. The guidance in ASU 2014-09 also improves U.S. GAAP by reducing the number of requirements to which an entity must consider in recognizing revenue, as well as requires improved disclosures to help users of financial statements better understand the nature, amount, timing and uncertainty of revenue that is recognized. The effective date of ASU 2014-09 was deferred by ASU No. 2015-14, *Deferral of the Effective Date*, to annual periods beginning after December 15, 2017. The adoption is effective for CMC for fiscal year ended August 31, 2019. CMC adopted ASU 2014-09 as of September 1, 2018, using the modified retrospective method for all contracts existing as of that date. Nearly all amounts previously classified as provision for bad debts are now recorded as a direct reduction to net patient service revenue. This change did not have a material impact on the consolidated financial statements.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities* ("ASU 2016-14"), which improves the current net asset classification requirements and the information presented in financial statements and notes about an entity's liquidity, financial performance and cash flows. The update removes the requirement to present three classes of net assets with two classes, net assets with donor restrictions and net assets without donor restrictions. The update also removes the requirement to present or disclose the indirect method (reconciliation) if using the direct method for the statement of cash flows as well as added several additional enhanced disclosures to the notes. The adoption is effective for CMC for the fiscal year ended August 31, 2019. CMC adopted ASU 2016-14 for the fiscal year ended August 31, 2019 and has adjusted the presentation of the consolidated financial statements accordingly, including changes to the presentation of net asset classification, inclusion of information about liquidity and availability of resources and inclusion of information provided about expenses. In accordance with ASU 2016-14, net assets as of August 31, 2019 have been reclassified as follows (in thousands):

	As adjusted	
	Without Donor Restrictions	With Donor Restrictions
As previously reported:		
Unrestricted	\$ 1,184,488	\$ -
Temporarily and permanently restricted	-	29,939
	\$ 1,184,488	\$ 29,939

In accordance with ASU 2016-14, net assets as of August 31, 2018, have been reclassified as follows (in thousands):

	As adjusted	
	Without Donor Restrictions	With Donor Restrictions
As previously reported:		
Unrestricted	\$ 1,075,992	\$ -
Temporarily and permanently restricted	-	22,609
	\$ 1,075,992	\$ 22,609

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made* ("ASU 2018-08"), to clarify and improve the scope and the accounting guidance for contributions received and made. The amendments should assist entities in evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) within the scope of Topic 958, Not-for-Profit Entities, or as exchange (reciprocal) transactions subject to other guidance and also in determining whether a contribution is conditional. The adoption is effective for CMC for fiscal year ended August 31, 2019, for contributions received, and for fiscal year ending August 31, 2020, for contributions made. Management has adopted the update for contributions received, which did not have an impact on the consolidated financial statements, and is currently evaluating the impact of the provisions of ASU 2018-08 for contributions made on the consolidated financial statements.

# Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers Notes to Consolidated Financial Statements

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In January 2016, the FASB issued ASU No. 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities, Financial Instruments – Overall (Subtopic 825-10)* (“ASU 2016-01”), which enhances the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The update addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The adoption is effective for CMC for fiscal year ending August 31, 2020. Management is currently evaluating the impact of the provisions of ASU 2016-01 on the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (“ASU 2016-02”), which increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the statement of financial position and disclosing key information about leasing arrangements in the financial statements of lessees. ASU 2016-02 is effective for CMC for fiscal year ending August 31, 2020. CMC adopted the provisions of this new lease standard effective September 1, 2019 utilizing the modified retrospective transition method through a cumulative-effect adjustment. This allows CMC to continue to apply the legacy guidance in the previous standard (ASC 840), including its disclosure requirements, in the comparative periods presented in the year of adoption. CMC elected the package of practical expedients available under the transition provisions of the new lease standard, which include (a) not reassessing ASC 840 evaluations on whether expired or existing contracts contain leases, (b) not reassessing lease classification, under ASC 840 and (c) not revaluing initial direct costs for existing leases ASC 840. CMC also elected the practical expedient to carry forward its historical accounting for any land easements on existing contracts. CMC made an accounting policy election that keeps leases with an initial term of 12 months or less off of the balance sheet and will result in recognizing those lease payments in the consolidated statements of operations on a straight-line basis over the lease term.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments* (“ASU 2016-15”), which provides guidance on eight specific cash flow issues including: debt repayment or debt extinguishment costs, settlement of zero-coupon debt instruments, or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing, contingent consideration payments made after a business combination, proceeds from settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, distributions received from equity method investees, beneficial interests in securitization transactions and separately identifiable cash flows and application of the predominance principle. The adoption is effective for CMC for fiscal year ending August 31, 2020. Management is currently evaluating the impact of the provisions of ASU 2016-15 on the consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash* (“ASU 2016-18”), which requires the statement of cash flows to explain the change during the period in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. The adoption is effective for CMC for fiscal year ending August 31, 2020. Management is currently evaluating the impact of the provisions of ASU 2016-18 on the consolidated financial statements.



**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

---

In March 2017, the FASB issued ASU No. 2017-07, *Compensation – Retirement Benefits (Topic 715)*, to improve the presentation of net periodic pension cost and net periodic postretirement benefit cost. The update requires an employer to report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit costs are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. This update also allows only the service cost component to be eligible for capitalization. The adoption is effective for and will be adopted by CMC for fiscal year ending August 31, 2020. For the fiscal year ended August 31, 2019, pension expense of \$663,000 is included in salaries, wages and benefits expense. When this update is applied retrospectively to 2019, service cost of \$9,890,000 will be reported in salaries, wages and benefits expense and \$9,227,000 will be reclassified into nonoperating income.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Market Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirement for Fair Value Measurement (“ASU 2018-13”)*, to improve the effectiveness of disclosures in the note to the financial statements by facilitating clear communication of the information required by generally accepted accounting principles (GAAP). The adoption of ASU 2018-13 is effective for CMC for fiscal year ending August 31, 2020. Management is currently evaluating the impact of the provisions of ASU 2018-13 on the consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-14, *Compensation – Retirement Benefits – Defined Benefit Plans – General (Subtopic 715-20): Disclosure Framework – Changes to the Disclosure Requirements for Defined Benefit Plans (“ASU 2018-14”)*, to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by generally accepted accounting principles that is most important to users of each entity’s financial statements. This includes the development of a framework that promotes the Board’s consistent decisions about disclosure requirements and the appropriate exercise of discretion by reporting entities. The adoption of ASU 2018-14 is effective for CMC for the fiscal year ending August 31, 2022. Management is currently evaluating the potential impact of the provisions of ASU 2018-14 on the consolidated financial statements.

**Subsequent events** – Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. CMC recognizes in the consolidated financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the consolidated balance sheet, including the estimates inherent in the process of preparing the consolidated financial statements. CMC’s consolidated financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the consolidated balance sheet but arose after the balance sheet date and before the consolidated financial statements are issued. CMC has evaluated subsequent events through November 22, 2019, which is the date the consolidated financial statements are issued.

# Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers

## Notes to Consolidated Financial Statements

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### NOTE 3 – NET PATIENT SERVICE AND PREMIUM REVENUES

**Net patient service revenues** – Net patient service revenue is reported at the amount that reflects the consideration to which CMC 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, the CMC 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.

Performance obligations are determined based on the nature of the services provided by CMC. Revenue for performance obligations satisfied over time is recognized based on actual charges incurred in relation to total expected (or actual) charges. CMC 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 hospitals receiving inpatient acute care services or patients receiving services in our outpatient centers or in their homes (home care). CMC measures the performance obligation from admission into the hospital, or the commencement of an outpatient service, 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. 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 CMC 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, CMC has elected to apply the optional exemption provided in FASB ASC 606-10-50-14a 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 previously 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.

CMC 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 CMC's policy and implicit price concessions provided to uninsured patients. CMC determines its estimates of contractual adjustments and discounts based on contractual agreements, its discount policies and historical experience. CMC determines its estimate of implicit price concessions based on its historical collection experience with this class of patients.

Agreements with third-party payors typically provide for payments at amounts less than established charges. A summary of the payment arrangements with major third-party payors follows:

- Medicare. Certain inpatient acute care services are paid at prospectively determined rates per discharge based on clinical, diagnostic and other factors. Certain services are paid based on cost-reimbursement methodologies subject to certain limits. Outpatient services are paid using prospectively determined rates.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

---

- Medi-Cal. Reimbursements for Medi-Cal services are generally paid at prospectively determined rates per discharge or per occasion of service. Additionally, CMC is allocated certain funds available from a pool of state of California funds for disproportionate share hospital services under the SB855 and Private Hospital Fund programs based upon an annual determination for eligibility. Revenues under the SB855 program and SB1255/Private Hospital Fund totaled \$48,514,000 and \$9,638,000, respectively, for the year ended August 31, 2019 and \$56,708,000 and \$9,708,000, respectively, for the year ended August 31, 2018. As of August 31, 2019 and 2018, CMC recorded receivables of \$11,570,000 and \$20,361,000, respectively, for amounts due from the State of California for SB855, SB1255, and other programs. See also “Hospital Fee Program” below.
- Other. Payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations provide for payment using prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

Laws and regulations concerning government programs, including Medicare and Medi-Cal, are complex and subject to varying interpretation. As a result of investigations by governmental agencies, various health care organizations have received requests for information and notices regarding alleged noncompliance with those laws and regulations, which, in some instances, have resulted in organizations 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 CMC'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 CMC. In addition, the contracts CMC 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 CMC'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. Net patient service revenue increased \$1,484,000 in 2019 and decreased \$1,759,000 in 2018, related to updates of prior years' cost report reserves and decreased by \$394,000 in 2019 and increased \$732,000 in 2018, related to successful appeals of prior years' cost report settlements.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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Generally, patients who are covered by third-party payors are responsible for related deductibles and coinsurance, which vary in amount. CMC also provides services to uninsured patients and offers those uninsured patients a discount, either by policy or law, from standard charges. CMC 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 patient service revenue in the period of the change. Adjustments arising from a change in the transaction price were not significant in 2019 or 2018. Subsequent changes that are determined to be the result of a change in the patient's ability to pay due to a bankruptcy are recorded as bad debt expense, which is classified in other expenses in the accompanying consolidated statements of operations.

Consistent with CMC's mission, care is provided to patients regardless of their ability to pay. Therefore, CMC 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 CMC expects to collect based on its collection history with those patients.

Patients who meet CMC'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. Unpaid costs of charity are the estimated costs of services provided to such patients. The estimated cost of providing these services was \$12,007,000 and \$4,492,000 for the years ended August 31, 2019 and 2018, respectively, calculated by multiplying the ratio of cost to gross charges by the gross uncompensated charges associated with providing charity care to patients.

CMC has determined that the nature, amount, timing and uncertainty of revenue and cash flows are affected primarily by the payors. The following table provides details of this factor.

The composition of consolidated net patient revenue by major payor group for the years ended August 31, 2019 and 2018, is as follows:

	<u>2019</u>	<u>2018</u>
Medicare	\$ 436,858	\$ 425,722
Managed Medicare	109,364	87,954
Medi-Cal	368,485	302,804
Managed Medi-Cal	216,297	218,008
Third-Party Contracts	552,634	549,736
Self-Pay and Others	<u>391</u>	<u>123,106</u>
Total	<u>1,684,029</u>	<u>1,707,330</u>
Less: Provision for Bad Debts	<u>-</u>	<u>(113,804)</u>
Total	<u>\$ 1,684,029</u>	<u>\$ 1,593,526</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

---

Revenue from patient's deductibles and coinsurance are included in the preceding categories based on the primary payor.

On a routine basis, CMC evaluates whether it received overpayments and whether any such overpayments should be reported to the payor and repaid, pertaining to certain patient services provided. For the years ended August 31, 2019 and 2018, liabilities related to this matter of \$1,452,000 and \$2,605,000, respectively, are included in other accrued liabilities and deferred revenue.

CMC 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 CMC'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, CMC 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.

**Premium revenue** – CMC has an agreement with a Medicare Advantage plan to provide certain acute care services to plan members for calendar year 2019. Under this agreement, CMC receives monthly capitation payments that are recognized as revenue during the period regardless of whether services are actually performed by CMC. CMC also records purchased services expense for services provided to these members outside of CMC's facilities. CMC also has an agreement with an independent physician association (IPA) to provide acute care services to certain IPA members. Under this agreement, CMC receives monthly capitation payments that are recognized as revenue during the period regardless of whether services are actually performed by CMC.

CMC reports premium revenue at the amount that reflects the consideration to which it expects to be entitled in exchange for providing access to health care services to its contracted members. These amounts are due from the Medicare Advantage plan and IPA according to contractual terms. CMC receives a premium payment amount each month, which is based upon fixed rates per enrollee or a percentage of premium of the health plan. Revenues for performance obligations are satisfied over the period of time that CMC is contracted to provide access to health care services to its members using the time-elapsed output method.

**Hospital Fee Program** – In November 2009, the California Hospital Fee Program (the Program) was signed into California state law. The Program provides supplemental Medi-Cal payments to certain California hospitals. The Program is funded by a quality assurance fee (the Fee) paid by participating hospitals and by matching federal funds. Hospitals receive supplemental payments from either the California Department of Health Care Services (DHCS), managed care plans, or a combination of both.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

---

California enacted a thirty-six-month quality assurance fee program (36-month Program or QAF4) for the period January 1, 2014, through December 31, 2016. Final approval by CMS for the fee for service portion of this program occurred in December 2014; approval for the non-expansion portion of the first six months of the managed care portion of this program occurred in June 2015, approval for the expansion portion of the first six months of the managed care portion occurred in April 2016, approval for the non-expansion portion of state fiscal year 14-15 and the first six months of the expansion portion of state fiscal year 14-15 occurred in November 2016. No managed care approvals occurred during the year ended August 31, 2018, but approvals for all remaining time periods were received during the year ended August 31, 2019. For the fee for service portion for the years ended August 31, 2019 and 2018, no estimated supplemental payments are included in net patient service revenue as all were reported in prior years. For the managed care portion for the years ended August 31, 2019 and 2018, estimated supplemental payments of \$167,337,000 and \$0, respectively, are included in net patient service revenue. For the years ended August 31, 2019 and 2018, estimated fees and pledge expense of \$31,335,000 and \$0 are included in quality assurance fee expense. As of August 31, 2019, CMC has recorded all activity for QAF4.

California enacted a thirty-month quality assurance fee program (30-month Program or QAF5) for the period January 1, 2017 through June 30, 2019. Final approval by CMS for the fee for service portion of this program occurred in December 2017; no managed care approvals have yet occurred. For the fee for service portion for the years ended August 31, 2019 and 2018, estimated supplemental payments of \$94,069,000 and \$184,258,000, respectively, are included in net patient service revenue. For the years ended August 31, 2019 and 2018, estimated fees and pledge expense of \$67,790,000 and \$130,246,000, respectively, are included in quality assurance fee expense. As of August 31, 2019, CMC has a receivable of \$52,305,000 and a liability of \$111,997,000, which are included in other assets and other accrued liabilities and deferred revenue, respectively, relating to the 30-month Program.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

**NOTE 4 – ASSETS LIMITED AS TO USE**

Assets limited as to use include marketable securities that are carried at fair value, based on quoted market prices. Pledges receivable are carried at net realizable value. The composition of assets limited as to use at August 31, 2019 and 2018, is as follows (in thousands):

	<u>2019</u>	<u>2018</u>
	Fair value and carrying value	Fair value and carrying value
Cash and equivalents	\$ 38,760	\$ 39,133
U.S. Treasury bills and notes	74,311	76,838
U.S. government agency debt	32,008	23,344
Corporate debt securities	293,723	259,410
Equity securities	73,737	74,388
Mutual funds	<u>156,402</u>	<u>153,864</u>
 Total cash and marketable securities	 668,941	 626,977
 Less amounts classified as short-term investments	 (17,150)	 (14,305)
Pledges receivable, net	<u>11,338</u>	<u>13,869</u>
	<u>(5,812)</u>	<u>(436)</u>
 Total assets limited as to use	 <u>\$ 663,129</u>	 <u>\$ 626,541</u>

CMC adopted ASC 820, *Fair Value Measurements and Disclosure*, on September 1, 2008 for fair value measurements of financial assets and liabilities. ASC 820 established a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to measurements involving significant unobservable inputs (Level 3). The three levels of fair value hierarchy are as follows:

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

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

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

The following table presents financial assets measured at fair value as of August 31 (in thousands):

Investments	2019			Fair value total
	Level 1	Level 2	Level 3	
Cash and equivalents	\$ 16,539	\$ -	\$ -	\$ 16,539
U.S. Treasury and U.S. agency fixed income:				
U.S. Treasury bills and notes	70,596	-	-	70,596
U.S. government agency debt	-	32,008	-	32,008
	70,596	32,008	-	102,604
Corporate debt securities:				
Health care	-	27,884	-	27,884
Energy	-	41,775	-	41,775
Financials	-	132,817	-	132,817
Industrials	-	21,100	-	21,100
Information technology	-	3,060	-	3,060
Telecommunications	-	14,894	-	14,894
Consumer discretionary	-	13,724	-	13,724
Consumer staples	-	11,955	-	11,955
Materials	-	7,821	-	7,821
Real estate	-	1,597	-	1,597
Utilities	-	4,050	-	4,050
Transportation	-	3,617	-	3,617
Other	-	2,592	-	2,592
	-	286,886	-	286,886
Equity securities:				
Health care	8,286	-	-	8,286
Financials	9,030	-	-	9,030
Consumer staples	6,874	-	-	6,874
Consumer discretionary	3,864	-	-	3,864
Materials	1,011	-	-	1,011
Energy	4,005	-	-	4,005
Information technology	19,035	-	-	19,035
Industrials	8,983	-	-	8,983
Telecommunications	3,579	-	-	3,579
Specialty real estate	1,634	-	-	1,634
Utilities	1,501	-	-	1,501
Other	-	111	-	111
	67,802	111	-	67,913



**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

Investments	2019			Fair value total
	Level 1	Level 2	Level 3	
Mutual funds:				
Alternative	59,072	-	-	59,072
Emerging Markets	3,337	-	-	3,337
Mid cap core	4,940	-	-	4,940
Small cap core	12,740	-	-	12,740
Large cap	37,819	-	-	37,819
Foreign	38,494	-	-	38,494
	<u>156,402</u>	<u>-</u>	<u>-</u>	<u>156,402</u>
	<u>311,339</u>	<u>319,005</u>	<u>-</u>	<u>630,344</u>
Other board-designated investments				
U.S. Treasury bills and notes	-	3,715	-	3,715
Corporate debt securities	-	6,837	-	6,837
Equity securities	5,824	-	-	5,824
Cash and equivalents	22,221	-	-	22,221
	<u>28,045</u>	<u>10,552</u>	<u>-</u>	<u>38,597</u>
Total	<u>\$ 339,384</u>	<u>\$ 329,557</u>	<u>\$ -</u>	<u>\$ 668,941</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

The following table presents financial assets measured at fair value as of August 31 (in thousands):

Investments	2018			total
	Level 1	Level 2	Level 3	
Cash and equivalents	\$ 14,331	\$ -	\$ -	\$ 14,331
U.S. Treasury and U.S. agency fixed income:				
U.S. Treasury bills and notes	76,838	-	-	76,838
U.S. government agency debt	-	23,344	-	23,344
	76,838	23,344	-	100,182
Corporate debt securities:				
Health care	-	30,286	-	30,286
Energy	-	20,959	-	20,959
Financials	-	123,946	-	123,946
Industrials	-	14,116	-	14,116
Information technology	-	3,038	-	3,038
Telecommunications	-	13,371	-	13,371
Consumer discretionary	-	9,588	-	9,588
Consumer staples	-	8,201	-	8,201
Materials	-	5,937	-	5,937
Real estate	-	7,409	-	7,409
Utilities	-	4,051	-	4,051
Transportation	-	980	-	980
Other	-	7,156	-	7,156
	-	249,038	-	249,038
Equity securities:				
Health care	8,404	-	-	8,404
Financials	9,628	-	-	9,628
Consumer staples	4,427	-	-	4,427
Consumer discretionary	5,089	-	-	5,089
Materials	1,750	-	-	1,750
Energy	4,525	-	-	4,525
Information technology	21,638	-	-	21,638
Industrials	7,667	-	-	7,667
Telecommunications	2,548	-	-	2,548
Specialty real estate	1,406	-	-	1,406
Utilities	1,538	-	-	1,538
Other	96	-	-	96
	68,716	-	-	68,716

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

Investments	2018			Fair value total
	Level 1	Level 2	Level 3	
Mutual funds:				
Alternative	53,632	-	-	53,632
Emerging Markets	3,389	-	-	3,389
Mid cap core	5,948	-	-	5,948
Small cap core	21,946	-	-	21,946
Large cap	21,249	-	-	21,249
Foreign	47,700	-	-	47,700
	<u>153,864</u>	<u>-</u>	<u>-</u>	<u>153,864</u>
	<u>313,749</u>	<u>272,382</u>	<u>-</u>	<u>586,131</u>
<u>Other board-designated investments</u>				
Corporate debt securities	-	10,372	-	10,372
Equity securities	5,672	-	-	5,672
Cash and equivalents	24,802	-	-	24,802
	<u>30,474</u>	<u>10,372</u>	<u>-</u>	<u>40,846</u>
<b>Total</b>	<u>\$ 344,223</u>	<u>\$ 282,754</u>	<u>\$ -</u>	<u>\$ 626,977</u>

The scheduled maturities of the debt securities as of August 31 (in thousands):

	2019	2018
Due within 1 year or less	\$ 24,688	\$ 35,569
Due after 1 year through 5 years	310,445	271,485
Due after 5 years	<u>30,133</u>	<u>29,992</u>
	365,266	337,046
Mortgage-backed securities, accrued interest, and other	<u>34,776</u>	<u>22,546</u>
	<u>\$ 400,042</u>	<u>\$ 359,592</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

---

Investment income is composed of the following for the years ended August 31 (in thousands):

	<u>2019</u>	<u>2018</u>
Interest income	\$ 11,665	\$ 8,522
Net unrealized and realized gains/losses	4,827	1,668
Dividends	9,755	4,486
Other	<u>1,212</u>	<u>1,909</u>
	<u>\$ 27,459</u>	<u>\$ 16,585</u>

**NOTE 5 – PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment consist of the following as of August 31 (in thousands):

	<u>2019</u>	<u>2018</u>
Land and land improvements	\$ 45,021	\$ 44,695
Buildings and improvements	975,259	958,640
Equipment	<u>598,429</u>	<u>573,234</u>
	1,618,709	1,576,569
Accumulated depreciation	<u>(739,572)</u>	<u>(674,573)</u>
	<u>\$ 879,137</u>	<u>\$ 901,996</u>

**NOTE 6 – OTHER ASSETS**

Other assets consist of the following as of August 31 (in thousands):

	<u>2019</u>	<u>2018</u>
Investment in rental properties	\$ 53,301	\$ 54,509
Real estate held for development	27,265	27,265
Intangible assets, net	6,515	6,091
Investment in joint ventures	29,873	27,695
Loan receivables	17,452	6,581
Other	<u>3,956</u>	<u>5,617</u>
	<u>\$ 138,362</u>	<u>\$ 127,758</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

---

CMC owns rental properties, recorded at cost, net of accumulated depreciation. Investments in rental properties consist of the following as of August 31, 2019 and 2018 and are included in other assets in the accompanying consolidated balance sheets (in thousands):

	2019	2018
Land	\$ 6,597	\$ 6,835
Buildings and land improvements	70,050	68,198
Equipment	972	947
	77,619	75,980
Accumulated depreciation	(24,318)	(21,471)
	\$ 53,301	\$ 54,509

CMC leases certain rental properties to other parties under noncancelable operating leases. Future minimum payments scheduled to be received at August 31 by fiscal year and in the aggregate, under noncancelable operating leases consist of the following (in thousands):

<u>Fiscal year</u>		
2020	\$	7,763
2021		7,147
2022		5,191
2023		4,358
2024		3,582
Thereafter		10,207
	\$	38,248

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

**NOTE 7 – LONG-TERM DEBT**

Long-term debt consists of the following as of August 31 (in thousands):

	<u>2019</u>	<u>2018</u>
California Municipal Finance Authority Certificates of Participation (Community Hospitals of Central California Project) Series 2017, interest ranging from 4.00% to 5.00% payable semi-annually; principal payable in installments ranging from \$7,125,000 in 2020 to \$28,690,000 in 2047, collateralized by gross revenues.	\$ 377,900	\$ 386,570
Unamortized bond premium	<u>28,710</u>	<u>30,488</u>
Total certificates of participation	406,610	417,058
California Municipal Finance Authority Certificates of Participation (Community Hospitals of Central California Project) Series 2015, interest ranging from 4.25% to 5.00% payable semi-annually; principal payable in installments ranging from \$2,005,000 in 2020 to \$11,500,000 in 2040, collateralized by gross revenues.	120,260	120,260
Unamortized bond premium	<u>6,712</u>	<u>7,112</u>
Total certificates of participation	126,972	127,372
Other long-term debt	<u>13,667</u>	<u>5,901</u>
	547,249	550,331
Less unamortized financing costs, net	<u>(2,457)</u>	<u>(2,740)</u>
	544,792	547,591
Less current maturities	<u>(11,905)</u>	<u>(9,890)</u>
	<u>\$ 532,887</u>	<u>\$ 537,701</u>

Under the terms of the master trust indenture associated with the certificates of participation, certain members of CMC are designated as members of the Obligated Group. There are restrictive covenants requiring compliance by the Obligated Group. These include, among other things, limitations on the issuance of additional debt and the maintenance of certain financial ratios.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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Scheduled principal repayments on long-term debt and payments on capital lease obligations by fiscal year are as follows (in thousands):

	Long-term Debt
2020	\$ 11,905
2021	12,553
2022	13,137
2023	13,347
2024	13,187
Thereafter	447,698
	511,827
Add net unamortized bond premium	35,422
	\$ 547,249

**NOTE 8 – LINE OF CREDIT**

CMC has a credit agreement with a bank that allows CMC to borrow up to \$40,000,000. Under this agreement, credit card borrowings are interest-free and due monthly. All other borrowings bear interest on a LIBOR base. Amounts applied for letter of credit agreements totaled \$2,707,000 as of both August 31, 2019 and 2018. The letter of credit agreements are effective through September 2020. Outstanding credit card borrowings were \$3,327,000 and \$3,345,000 as of August 31, 2019 and 2018, respectively. There were no LIBOR-based borrowings as of these dates. A note securing the line of credit has been issued under the master trust indenture. The agreement expires on June 18, 2020.

**NOTE 9 – PENSION PLAN**

CMC maintains a contributory defined benefit cash balance pension plan that, prior to January 1, 2017, covered substantially all employees upon their retirement. Effective January 1, 2017, CMC discontinued new enrollment to the defined benefit plan and implemented a new contributory defined contribution plan. Current employees were required to make a one-time choice between the two plans and those who did not choose to move to the new defined contribution plan remain in the defined benefit plan. All new employees will enter the new contributory defined contribution plan.

**Defined benefit plan** – Benefit payments for participants in the plan are determined by the balance in the participant's account at retirement or separation. In addition to normal retirement benefits, under certain circumstances, the plan also provides early retirement, disability, death and spousal benefits. Employees of CMC that are eligible for this plan become eligible to participate in the plan on January 1 or July 1 following the completion of 1,000 hours and one year of service. The vesting period is three years.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

Mandatory contributions are made to the plan by the employees as specified in the plan documents. Total employee contributions to the plan for the years ended August 31, 2019 and 2018, were \$4,114,000 and \$4,459,000, respectively. Total employer contributions to the plan for the years ended August 31, 2019 and 2018, were \$0 and \$17,200,000, respectively. Total benefits paid for the years ended August 31, 2019 and 2018, were \$17,416,000 and \$16,158,000, respectively. The funded status is presented as a net pension benefit asset in the accompanying consolidated balance sheet as of August 31, 2018 and the unfunded status is presented as a noncurrent liability in the accompanying consolidated balance sheet as of August 31, 2019.

The following tables set forth the plan's benefit obligation, fair value of plan assets and funded status as of August 31 (in thousands):

	<u>2019</u>	<u>2018</u>
Change in projected benefit obligation (PBO):		
PBO at beginning of year	\$ 264,096	\$ 268,280
Employer service cost	9,890	9,891
Interest cost	9,608	7,562
Actuarial gain	17,956	(9,867)
Plan participants' contributions	4,114	4,459
Benefits paid from plan assets	(17,416)	(16,158)
Administrative expenses paid	(77)	(71)
	<u>288,171</u>	<u>264,096</u>
PBO at end of year	\$ 288,171	\$ 264,096
Change in plan assets:		
Fair value of assets at beginning of year	\$ 277,538	\$ 253,356
Actual return on assets	10,175	18,752
Employer contributions	-	17,200
Plan participants' contributions	4,114	4,459
Benefits paid	(17,416)	(16,158)
Administrative expenses paid	(77)	(71)
	<u>274,334</u>	<u>277,538</u>
Fair value of assets at end of year	\$ 274,334	\$ 277,538
Funded accumulated benefit obligation	\$ 4,078	\$ 32,159
Pension benefit (obligation) asset recognized in consolidated balance sheets	\$ (13,837)	\$ 13,442
Accumulated benefit obligation at end of year	\$ 270,256	\$ 245,379

The weighted average assumptions used to determine benefit obligations as of August 31 are as follows:

	<u>2019</u>	<u>2018</u>
Discount rate	2.99%	4.13%
Expected long-term rate of return on assets	7.00%	7.25%
Rate of compensation increase	3.00%	4.00%



**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

The weighted average assumptions used to determine net periodic benefit cost as of August 31 are as follows:

	<u>2019</u>	<u>2018</u>
Discount rate	4.13%	3.43%
Expected return on plan assets	7.25%	7.25%

Net periodic pension cost for the plan for 2019 and 2018 is included in salaries, wages and benefits in the accompanying consolidated statements of operations. Components of net periodic pension cost include the following at August 31 (in thousands):

	<u>2019</u>	<u>2018</u>
Service cost	\$ 9,890	\$ 9,891
Interest cost	9,608	7,562
Expected return on plan assets	(19,546)	(19,122)
Amortization of prior service cost	17	41
Recognized net actuarial losses	694	1,716
	<u>\$ 663</u>	<u>\$ 88</u>
Amounts recognized in net assets:		
Net actuarial loss	\$ 62,150	\$ 35,517
Net prior service cost	-	17
	<u>\$ 62,150</u>	<u>\$ 35,534</u>
Amounts recognized as changes in net assets:		
Net loss (gain)	\$ 27,327	\$ (9,497)
Amortization of prior service cost	(17)	(41)
Amortization of net loss	(694)	(1,716)
	<u>\$ 26,616</u>	<u>\$ (11,254)</u>

The estimated net loss and prior service cost that will be amortized from net assets into net periodic pension cost in the year ending August 31, 2020 is \$3,019,435 and \$0, respectively.

CMC's pension plan asset allocations at August 31 by asset category are as follows:

	<u>2019</u>	<u>2018</u>
Cash and equivalents	4%	0%
Debt securities	36%	35%
Equity securities	60%	65%
	<u>100%</u>	<u>100%</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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The asset allocation policy for the pension plan is as follows: fixed income securities 30% to 60% (which may include U.S. government securities and U.S. government agency bonds, corporate notes and bonds, mortgage-backed bonds, preferred stock and the fixed income securities of foreign governments and corporations); equity securities 30% to 70% (which may include domestic common stock, convertible notes and bonds, convertible preferred stocks, foreign equity securities); mutual funds and limited liability companies or partnerships that invest in allowed securities as defined above and alternative investments 0% to 15%.

CMC's investment strategy for pension plan assets is designed to emphasize long-term growth of principal while avoiding excessive risk. The investment performance of the total portfolio, as well as asset class components, is measured against commonly accepted performance benchmarks.

The expected long-term rate of return on plan assets is the expected average rate of return on the funds invested currently and on funds to be invested in the future in order to provide for the benefits included in the projected benefit obligation. The CMC pension plan used 7.25% in calculating the 2019 and 2018 expense amounts. This assumption is based on capital market assumptions and the plan's target asset allocation. CMC continues to monitor the expected long-term rate of return if changes in those parameters cause 7.25% to be outside of a reasonable range of expected returns, or if actual plan returns over an extended period of time suggest general market assumptions are not representative of expected plan results.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

The following table presents the plan assets measured at fair value at August 31, 2019, (in thousands):

Investments	2019			Fair value total
	Level 1	Level 2	Level 3	
Cash and equivalents	\$ 10,195	\$ -	\$ -	\$ 10,195
U.S. Treasury and U.S. agency fixed income:				
U.S. Treasury bills and notes	27,669	-	-	27,669
U.S. government agency debt	-	21,986	-	21,986
	27,669	21,986	-	49,655
Corporate fixed income:				
Asset-backed securities	-	9,003	-	9,003
Mortgage-backed	-	179	-	179
Municipal	-	2,413	-	2,413
Other	-	38,079	-	38,079
	-	49,674	-	49,674
Common stocks:				
ADRs	5,491	-	-	5,491
Health care	7,834	-	-	7,834
Utilities	1,653	-	-	1,653
Financials	12,591	-	-	12,591
Consumer staples	5,725	-	-	5,725
Consumer discretionary	9,312	-	-	9,312
Materials	1,279	-	-	1,279
Energy	5,025	-	-	5,025
Information technology	22,404	-	-	22,404
Industrials	7,205	-	-	7,205
Telecommunication services	1,477	-	-	1,477
	79,996	-	-	79,996
Mutual funds:				
Small Cap	8,183	-	-	8,183
Mid Cap	5,577	-	-	5,577
ETF	37,169	-	-	37,169
Foreign	33,885	-	-	33,885
	84,814	-	-	84,814
	<u>\$ 202,674</u>	<u>\$ 71,660</u>	<u>\$ -</u>	<u>\$ 274,334</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

The following table presents the plan assets measured at fair value at August 31, 2018, (in thousands):

Investments	2018			Fair value total
	Level 1	Level 2	Level 3	
Cash and equivalents	\$ 852	\$ -	\$ -	\$ 852
U.S. Treasury and U.S. agency fixed income:				
U.S. Treasury bills and notes	24,169	-	-	24,169
U.S. government agency debt	-	18,861	-	18,861
	24,169	18,861	-	43,030
Corporate fixed income:				
Asset-backed securities	-	8,980	-	8,980
Mortgage-backed	-	550	-	550
Municipal	-	2,192	-	2,192
Other	-	42,770	-	42,770
	-	54,492	-	54,492
Common stocks:				
ADRs	3,644	-	-	3,644
Health care	9,776	-	-	9,776
Utilities	1,576	-	-	1,576
Financials	14,184	-	-	14,184
Consumer staples	4,685	-	-	4,685
Consumer discretionary	10,627	-	-	10,627
Materials	2,430	-	-	2,430
Energy	5,294	-	-	5,294
Information technology	25,390	-	-	25,390
Industrials	7,382	-	-	7,382
Telecommunication services	1,398	-	-	1,398
	86,386	-	-	86,386
Mutual funds:				
Mid Cap	5,610	-	-	5,610
ETF	39,426	-	-	39,426
Foreign	47,742	-	-	47,742
	92,778	-	-	92,778
	<u>\$ 204,185</u>	<u>\$ 73,353</u>	<u>\$ -</u>	<u>\$ 277,538</u>

For information about the valuation techniques and inputs to measure fair value of the plan assets, see discussion included in the fair value measurement discussion at Note 5.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

The following pension benefit payments reflect expected future service. Payments expected to be paid over the next ten years are as follows (in thousands):

2020	\$ 21,812,464
2021	\$ 20,192,700
2022	\$ 21,651,084
2023	\$ 22,155,182
2024	\$ 22,860,062
2025-2029	\$ 121,640,527

CMC expects to contribute approximately \$8,745,000 to the pension plan during the 2020 fiscal year.

**Defined contribution plan** – Employees of CMC that are eligible for this plan become eligible to participate in the plan on January 1 or July 1 following the completion of 1,000 hours and one year of service. The vesting period is three years. Mandatory contributions are made to the plan by the employees as specified in the plan documents. Total employer contributions to the plan for the years ended August 31, 2019 and 2018, were \$9,903,000 and \$8,405,000, respectively.

**Other plans** – CMC provides various supplemental executive retirement plans (SERPs). During 2013, it entered into a collateral assignment split dollar agreement with an executive. CMC has invested \$4,958,000 into this plan and is entitled to receive a return of these funds, plus interest at a rate of 2.55%, upon the death of the executive. In 2019 CMC entered into a collateral assignment split dollar agreement with eleven executives. CMC invested \$10,193,000 into these plans and is entitled to receive a return of these funds, plus interest ranging from 2.91% to 3.31% upon the death of these executives. Other executives have SERPs with terms that vary by participant. During fiscal years 2019 and 2018, CMC contributed approximately \$1,303,000 and \$873,000, respectively, to these plans.

At August 31, 2019 and 2018, the aggregate liability for all plans was \$2,230,000 and \$2,050,000, respectively.

**NOTE 10 – NET ASSETS WITH DONOR RESTRICTIONS**

Net assets with donor restrictions are available for the following purposes as of August 31 (in thousands):

	2019	2018
Net assets with donor restrictions for specified programs:		
Patient care	\$ 12,487	\$ 10,005
Purchase of equipment	713	961
Scholarships and other education	3,390	4,152
Other	12,690	14,437
	29,280	29,555
Net assets with donor restrictions to be maintained in perpetuity	384	384
	\$ 29,664	\$ 29,939

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

**NOTE 11 – FUNCTIONAL CLASSIFICATION OF OPERATING EXPENSES**

The following is a summary of management’s estimated functional classification of operating expenses for the year ended August 31, 2019 (in thousands):

	Management and general	Fundraising	Program services	Total
Salaries, wages, and benefits	\$ 2,756	\$ 2,270	\$ 764,250	\$ 769,276
Supplies	4,768	82	303,622	308,472
Outside services	16,131	451	294,737	311,319
Insurance	178	-	7,872	8,050
Depreciation and amortization	3,746	40	76,661	80,447
Rental and lease	125	4	9,393	9,522
Interest	118	1	20,803	20,922
Utilities	658	3	17,089	17,750
Other	2,375	318	44,430	47,123
Quality assurance fee	-	-	99,125	99,125
	<u>\$ 30,855</u>	<u>\$ 3,169</u>	<u>\$ 1,637,982</u>	<u>\$ 1,672,006</u>

The following is a summary of management’s estimated functional classification of operating expenses for the year ended August 31, 2018 (in thousands):

Program services	\$ 1,404,902
Management and general	166,852
Fundraising	<u>5,088</u>
	<u>\$ 1,576,842</u>

CMC has determined that the corporate structure described in Note 1 supports the functional classification as follows:

- Program services - Acute care services
- Management and general – Corporate activities, CISC, CCHP
- Fundraising – Development activities

Costs not directly attributable to a function, including insurance expense, are allocated to a function on the basis of time and effort.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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**NOTE 12 – OPERATING LEASES**

CMC leases certain property and equipment under noncancelable operating leases that expire in various years through 2024. Future minimum payments at August 31, 2019 by fiscal year and in the aggregate, under noncancelable operating leases with initial terms of one year or more consist of the following (in thousands):

<u>Fiscal year</u>	
2020	\$ 4,696
2021	4,600
2022	4,628
2023	3,167
2024	3,195
Thereafter	<u>908</u>
	<u>\$ 21,194</u>

Total operating lease expense in 2019 and 2018 was \$9,482,000 and \$10,666,000, respectively.

**NOTE 13 – COMMITMENTS AND CONTINGENCIES**

**Claims and regulatory environment** – CMC is involved in various claims and litigation, as both plaintiff and defendant, arising in the ordinary course of business. The health care industry is subjected to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services and Medicare fraud and abuse. Government activity remains at a high level with respect to investigations and allegations across the nation concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

As disclosed in Notes 2 and 3, Medicare and Medi-Cal government reimbursement programs account for a substantial amount of CMC's net patient service revenue. Expenditure reduction efforts and budget concerns within the United States and California legislature continue to create uncertainty over the volume of future health care funding. It is at least reasonably possible that future reimbursements for patient services under these programs could be negatively impacted.

**Pledges to Medical Foundation** – CMC has made significant pledges to the Santé Health Foundation (SHF) to support its efforts to recruit needed specialists and primary care physicians to the Fresno area as well as its efforts to install electronic health record systems in local physicians' offices. Pledges of \$31,979,000 and \$26,929,000 and pledge payments of \$33,629,000 and \$37,677,000 were made in 2019 and 2018, respectively. Two of the Board members of SHF are also members of the Board of CMC or executive management of CMC.

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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CMC provides a \$7,000,000 line of credit (LOC) to SHF that expires on May 31, 2024. At December 31 of each year in which SHF takes an advance that remains unpaid, the principal and accrued interest balance convert to a ten-year note payable in equal annual installments. The aggregate outstanding principal balances of all LOC advances and notes payable may not exceed \$7,000,000 at any time. All borrowings bear interest at the applicable federal rate and are secured by the accounts receivable of SHF. As of August 31, 2019 and 2018, \$3,238,000 and \$2,108,000 was due to CMC, respectively.

As of September 1, 2016, CMC became the sole member of SHF but does not have control over the operations nor the appointment of Board members. Due to the lack of control, SHF is not consolidated into CMC's consolidated financial statements.

**Capital projects in progress** – As of August 31, 2019, CMC spent \$73,652,000 related to various construction and other capital projects in progress. CMC estimates an additional \$430,660,000 will be required through fiscal 2022 to complete the projects. As of August 31, 2019, CMC has outstanding commitments with contractors for approximately \$298,752,000 related to these projects.

**NOTE 14 – LIQUIDITY AND AVAILABILITY**

As of August 31, 2019, CMC has working capital of \$134,116,000 and average days (based on normal expenditures) cash on hand of 178.

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

	<u>2019</u>
Cash and equivalents	\$ 143,340
Patient accounts receivable	270,308
Due from State of California for supplemental funding	11,570
Other receivables	28,274
Short-term investments	17,150
Board-designated assets	<u>614,106</u>
 Total liquid and available	 <u><u>\$ 1,084,748</u></u>

CMC has other assets limited to use for donor-restricted purposes, debt service and for the professional and general liability captive insurance program. These assets limited to use, which are more fully described in Note 4, are not available for general expenditure within the next year and are not reflected in the amounts above.



**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Consolidated Financial Statements**

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

Additionally, CMC maintains a \$40,000,000 line of credit, as discussed in more detail in Note 8. As of August 31, 2019, \$33,966,000 remained available on CMC's line of credit.

As of August 31, 2019, management believes that CMC was in compliance with bond covenants.

## **Single Audit**

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**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Schedule of Expenditures of Federal Awards  
Year Ended August 31, 2019**

<u>FEDERAL GRANTOR/PASS-THROUGH GRANTOR/CLUSTER - PROGRAM TITLE</u>	<u>Award Period</u>	<u>CFDA Number</u>	<u>Pass-Through or Award Number</u>	<u>Passed Through to Subrecipients</u>	<u>Federal Expenditures</u>
<i>U.S. Department of Health and Human Services</i>					
Coordinated Services and Access to Research for Women, Infants, Children, and Youth	8/1/18 - 7/31/19	93.153	H12HA24778-06-00	\$ 328,895	\$ 343,753
Coordinated Services and Access to Research for Women, Infants, Children, and Youth	8/1/19 - 8/31/19	93.153	H12HA24778-07-00	<u>30,748</u>	<u>31,850</u>
				<u>359,643</u>	<u>375,603</u>
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	4/1/18 - 3/31/19	93.918	H76HA00765-16-03	302,305	316,903
Grants to Provide Outpatient Early Intervention Services with Respect to HIV Disease	4/1/19 - 3/31/20	93.918	H76HA00765-17-01	<u>226,463</u>	<u>232,488</u>
				<u>528,768</u>	<u>549,391</u>
Subtotal Direct Programs				<u>888,411</u>	<u>924,994</u>
Pass-Through Programs From California Department of Public Health:					
HIV Care Formula Grants	4/1/18 - 3/31/19	93.917	15-11084	398,909	425,150
HIV Care Formula Grants	4/1/19 - 3/31/20	93.917	15-11084	<u>246,485</u>	<u>246,485</u>
				<u>645,394</u>	<u>671,635</u>
HIV Care Formula Grants - Supplemental (X08)	9/30/17 - 9/29/18	93.917	17-10772	50,601	50,601
HIV Care Formula Grants - Supplemental (X09)	9/30/18 - 9/29/19	93.917	17-10772	<u>148,909</u>	<u>151,692</u>
				<u>199,510</u>	<u>202,293</u>
Subtotal Pass-Through Programs				<u>844,904</u>	<u>873,928</u>
<i>Total U.S. Department of Health and Human Services</i>				<u>1,733,315</u>	<u>1,798,922</u>
<i>Total Expenditures of Federal Awards</i>				<u>\$ 1,733,315</u>	<u>\$ 1,798,922</u>

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Notes to Schedule of Expenditures of Federal Awards**

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**NOTE 1 - BASIS OF PRESENTATION**

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal award activity of Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers (CMC) under programs of the federal government for the year ended August 31, 2019. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of CMC, it is not intended to and does not present the financial position, changes in net assets, or cash flows of CMC.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

**NOTE 3 - INDIRECT COST RATE**

CMC has elected not to use the 10-percent de minimis indirect cost rate as allowed under Uniform Guidance.

## **Report of Independent Auditors on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards***

To the Board of Trustees  
Community Hospitals of Central California and Affiliated Corporations  
dba Community Medical Centers

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers (CMC), which comprise the consolidated balance sheet as of August 31, 2019, the related consolidated statements of operations, 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 dated November 22, 2019.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the consolidated financial statements, we considered CMC's internal control over financial reporting, (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of CMC's internal control. Accordingly, we do not express an opinion on the effectiveness of CMC's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of CMC's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether CMC's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of this Report**

The purpose of that report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of CMC's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering CMC's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Moss Adams LLP*

San Francisco, California  
November 22, 2019

## **Report of Independent Auditors on Compliance for the Major Program and on Internal Control Over Compliance as Required by the Uniform Guidance**

The Board of Trustees  
Community Hospitals of Central California and Affiliated Corporations  
dba Community Medical Centers

### **Report on Compliance for the Major Federal Program**

We have audited Community Hospitals of Central California and Affiliated Corporations dba Community Medical Centers' (CMC) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on CMC's major federal program for the year ended August 31, 2019. CMC's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

#### ***Management's Responsibility***

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for CMC's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about CMC's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of CMC's compliance.

### ***Opinion on the Major Federal Program***

In our opinion, CMC complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended August 31, 2019.

### **Report on Internal Control over Compliance**

Management of CMC is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered CMC's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of CMC's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

*Mass Adams LLP*

San Francisco, California  
November 22, 2019



**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Schedule of Findings and Questioned Costs  
Year Ended August 31, 2019**

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**Section I – Summary of Auditor’s Results**

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***Financial Statements***

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP: Unmodified

Internal control over financial reporting:

- Material weakness(es) identified?  Yes  No
- Significant deficiency(ies) identified?  Yes  None reported

Noncompliance material to financial statements noted?  Yes  No

***Federal Awards***

Internal control over major federal programs:

- Material weakness(es) identified?  Yes  No
- Significant deficiency(ies) identified?  Yes  None reported

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?  Yes  No

**Community Hospitals of Central California  
and Affiliated Corporations  
dba Community Medical Centers  
Schedule of Findings and Questioned Costs  
Year Ended August 31, 2019**

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**Identification of the Major Federal Program and Type of Auditor's Report Issued on Compliance for the Major Federal Program:**

<i>CFDA Number</i>	<i>Name of Federal Program or Cluster</i>	<i>Type of Auditor's Report Issued on Compliance for the Major Federal Program</i>
93.917	HIV Care Formula Grants	Unmodified

Dollar threshold used to distinguish between Type A and Type B programs

\$750,000

Auditee qualified as low-risk auditee?

Yes

No

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**SECTION II – FINANCIAL STATEMENT FINDINGS**

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None noted

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**SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS**

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None noted



**COMMUNITY MEDICAL CENTERS**  
**Summary Schedule of Prior Audit Findings**  
**August 31, 2019**

**FINDING**  
**2018-001:**

Medicare Cost Report

*Condition:* This finding was a significant deficiency over Medicare cost report reserves. There were insufficient detailed review controls over certain aspects of the Medicare cost report preparation which resulted in overpayments in the Medicare outpatient outlier payments.

*Recommendation:* Management should implement policies and controls concerning the review of Medicare cost reports to ensure all adjustments are properly reviewed in sufficient detail and authorized.

*Current Status:* Corrective action was taken. No similar findings were noted in the 2019 audit.

Debbie Moffett, Vice President, Finance Administration

