COVID-19 DISCLOSURES

HOW HEALTH CARE BORROWERS CAN NAVIGATE FINANCIAL REPORTING IN AN UNCERTAIN ENVIRONMENT

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COVID-19: Impact on Nonprofit Health Care Credits

- In March 2020, The Centers for Medicare & Medicaid Services (CMS) and most states through emergency declarations and executive orders limited or stopped health care providers from performing elective procedures
- All three rating agencies have a negative outlook on the health care sector
  - Revenue declines due to canceling or postponing elective procedures
  - Expense increases due to higher staff costs and supply costs
  - Market declines impacting liquidity balances
  - High degree of uncertainty as to how long it will take to contain the virus and how long it will take the economy to recover

COVID-19: Impact on Nonprofit Health Care Credits

- Mitigating Impact and Relief for Hospitals
  - Medicare Accelerated Payment Program
  - Paycheck Protection Program
  - CARES Act
  - FEMA and other grants
- Market/Investor Reaction
  - Increased scrutiny of health care credits; only higher rated credits are currently accessing the market
  - Investors are focused on impact of COVID-19 on financial and operating condition of the borrower

Agenda

1. SEC Guidance on COVID-19 Disclosures in Corporate Market
2. Review of Federal Securities Laws for Municipal Market vs. Corporate Market
3. COVID-19 Accounting and Financial Reporting Implications
4. Timeline for Upcoming Financial Reporting
5. Best Practices for Developing COVID-19 Disclosures

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SEC GUIDANCE ON COVID-19 DISCLOSURES IN CORPORATE MARKET

SEC Urges Disclosure of COVID-19 Impact

- In a joint statement issued on April 8, 2020, SEC Chairman Jay Clayton and Division of Corporation Finance Director William Hinman released guidance urging public companies for the upcoming Q1 2020 earning season to:
  - provide as much information as is practicable regarding their current financial and operating status, as well as their future operational and financial planning
    - Disclose where the company stands today, operationally and financially
    - Disclose how the company’s COVID-19 response, including its efforts to protect the health and well-being of its workforce and its customers, is progressing
    - Disclose how its operations and financial condition may change as efforts to fight COVID-19 progress

SEC Urges Disclosure of COVID-19 Impact

- Clayton and Hinman noted that earnings reports and investor calls for Q1 2020 “will not be routine.”
- “In many cases, historical information may be substantially less relevant.”
- “Investors and analysts are thirsting to know where companies stand today, and importantly, how they have adjusted, and expect to adjust in the future, their operational and financial affairs to most effectively work through the COVID-19 health crisis.”
- “We recognize that producing forward-looking disclosures can be challenging and believe that taking on that challenge is appropriate.”

SEC Urges Disclosure of COVID-19 Impact

- Clayton and Hinman believe there are three reasons that companies should strive to provide, and update and supplement, as much forward-looking information as practicable:
  - The information will benefit investors
  - Market digestion of the information will benefit the company
  - Broad dissemination and exchange of firm-specific plans for addressing the effects of COVID-19 under various scenarios will substantially contribute to our nation’s collective effort to fight and recover from COVID-19
- On May 4, 2020, Clayton and the Director of the Office of Municipal Securities released a statement encouraging muni issuers to provide investors with the same robust disclosures they encouraged public companies to provide

FEDERAL SECURITIES LAWS FOR MUNICIPAL BONDS

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Federal Securities Laws for Municipal Bonds vs. Corporate Securities

- Securities Act of 1933
  - Registration requirement for most securities, but municipal bonds are excluded
- Securities Exchange Act of 1934
  - Creates ongoing disclosure requirements for public companies, and regulates brokers and dealers
    - Public companies are ***directly*** obligated by the 1934 Act to disclose on an annual and quarterly basis but municipal issuers and obligors are ***indirectly*** obligated to disclose if subject to a continuing disclosure agreement required to be obtained by underwriters under Rule 15c2-12 of the 1934 Act
- Both 1933 Act and 1934 Act contain antifraud provisions, which do apply to municipal securities

SEC Rule 10b-5

- The main antifraud provision – SEC Rule 10b-5 of the 1934 Act - applies to both municipal bonds and corporate securities:

  “It shall be unlawful for any person . . .

  a) To employ any device, scheme or artifice to defraud,

  b) To make any untrue statement of a material
  fact or to omit to state a ***material*** fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading . . . .”

  Must be “in connection with the purchase or sale of any security”

The “Materiality” Standard

- “[w]hether or not there is a substantial likelihood that a reasonable investor or prospective investor would consider the information important in deciding whether or not to invest.”
- Guidance comes primarily from court decisions and SEC enforcement cases
- Materiality is determined in context of all the facts and circumstances, but usually on a retroactive basis
- What is material is an evolving concept - materiality threshold

When Does SEC Rule 10b-5 Apply?

- SEC Rule 10b-5 applies whenever an issuer or obligor is “speaking to the market”
  - New public offerings
  - Reports and filings on EMMA under Continuing Disclosure Agreements
  - Voluntary filings on EMMA
  - Other circumstances
    - Public statements by officials
    - Investor website
  - Confidentiality and business concerns, and political sensitivity are not exceptions to application of disclosure rules

Health Care Borrowers Historically Have Looked to SEC Rules in Corporate Market as Best Practice

- Health care borrowers are required to provide quarterly disclosures to investors similar to public companies (but unlike others issuers and obligors in the municipal market)
- Health care borrowers generally follow SEC guidance for financial statements in offering documents for public offerings
  - Bonds are priced no more than 135 days after the date of the financial statements disclosed in offering document
- Health care borrowers can be more sophisticated and are treated more like public companies than other municipal issuers

COVID-19 ACCOUNTING AND FINANCIAL REPORTING IMPLICATIONS

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COVID-19 – Accounting and financial reporting implications

Revenue	Contract existence: New and existing contracts	Variable consideration Credit losses
Asset impairments and insurance	Goodwill, long-lived, and other intangibles	Inventory Deferred tax assets
Debt	Classification based on impacts to covenants	TDR, modifications, extinguishments
Financial instruments	CARES Act reporting Fair values, impairment	CECL application Hedge accounting
Leases	Rent concessions, lease modifications, lease abandonment	Incremental borrowing rate
Financial statement disclosures	Loss contingencies Risk and uncertainties	Going concern Subsequent events

Interim impairment considerations

- Effects of current economic environment may be an impairment indicator requiring an interim impairment test
- Interim impairment evaluation requires significant judgment
- Order in which assets generally are tested for impairment:

1. **Indefinite-lived intangible assets (ASC 350-30)***
   - Annually, or more frequently if impairment indicators exist
2. **Long-lived assets to be held and used (ASC 360)**
   - When impairment indicators exist
3. **Goodwill (ASC 350-20)**
   - Annually or more frequently if impairment indicators exist

* Other assets subject to impairment testing are tested at same time (e.g., inventory)

Asset impairments: Potential triggering events

If the answer to any of these questions is ‘yes’, a triggering event may have occurred and impairment testing may be required

Questions to Consider

- ❖ Has our supply chain been disrupted so that we cannot procure raw materials or components for finished goods?
- ❖ Has volatility in commodity prices negatively impacted revenues or production costs?
- ❖ Have workforce limitations impeded our ability to manufacture products or service our customers?
- ❖ Have we provided concessions to our customers that exceed normal business practice?
- ❖ Have we lost business due to event cancellations, store or facility closures, lower consumer sentiment, etc.?
- ❖ Are operations being curtailed temporarily, or assets mothballed?
- ❖ Have the circumstances significantly changed how we expect to use our long-lived assets?
- ❖ Are our customers struggling to pay their obligations or even remain in business?
- ❖ Has our stock price significantly decreased?
- ❖ Have we revised our earnings guidance downward?

Goodwill: Examples of events suggesting possible impairment

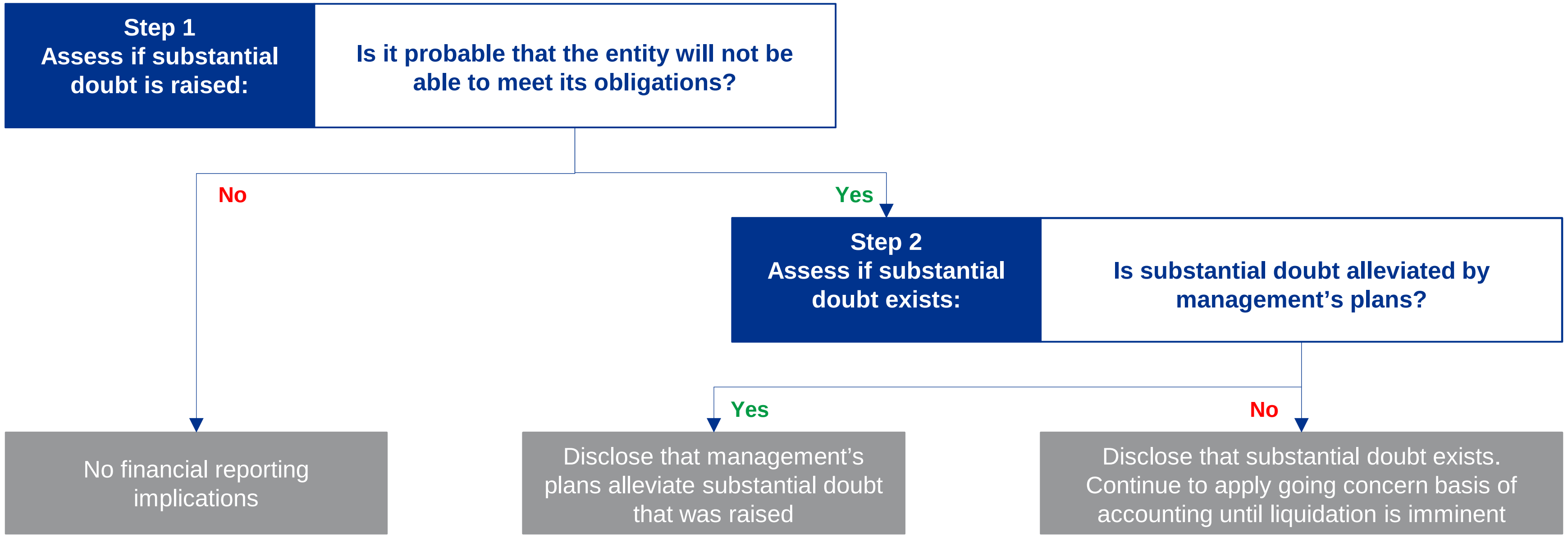
Reminder: Goodwill must be tested between annual tests if an event occurs or circumstances change to indicate that it is more likely than not that an impairment loss has been incurred (i.e. a triggering event).

Macroeconomic conditions	Deterioration in general economic conditions; limitations on accessing capital; fluctuations in foreign exchange rates; other developments in equity and credit markets.
Industry and market considerations	Deterioration in the environment in which an entity operates; an increased competitive environment; a decline in market-dependent multiples or metrics (absolute terms and/or relative to peers); a change in the market for an entity's products or services; a regulatory or political development.
Cost factors	Increases in raw materials, labor or other costs that have a negative effect on earnings and cash flows.
Financial performance	Negative or declining cash flows or a decline in actual or planned revenue or earnings compared with actual and projected results of relevant prior periods.
Entity-specific events	Changes in management, key personnel, strategy or customers; contemplation of bankruptcy; litigation.
Events affecting a reporting unit	Changes in the composition or carrying amount of net assets; a more-likely-than-not expectation of selling or disposing of all, or a portion, of a RU; the testing for recoverability of a significant asset group within a RU; recognition of a goodwill impairment loss in the financial statements of a component subsidiary.
Share price	A sustained decrease in share price (absolute terms and/or relative to peers). The capital markets downturn as a result of the COVID-19 outbreak may be a triggering event that requires goodwill testing for impairment. However, a single day's market capitalization might not be the best indication of fair value in volatile markets; instead, it might be appropriate to use an average market price over a reasonable period of time preceding the measurement date.

Going concern assessment

- ❖ To be a going concern, companies must have the ability to meet its obligations as they come due within one year after the financial statements are issued (available to be issued for non-SEC filers).
- ❖ Management has a responsibility to determine whether there are conditions and events that raise “substantial doubt” about the company’s ability to continue as a going concern.
- ❖ Annual financial statements to be issued may require management to consider the COVID-19 outbreak in their going concern evaluations. The severity and prolonged effects of the outbreak will likely require a close monitoring of the going concern assessment throughout 2020.

The following diagram represents how the going concern assessment is conducted.



CMS Accelerated and Advanced Payment Program

- Under the program, qualifying providers can receive an advance payment from CMS for up to 100% of the Medicare payment amount for up to a 6 month period. After a delay period of 120 days, CMS will begin to recoup the advance by offsetting it against newly submitted claims.
- Advance should be treated as a contract liability as it represents consideration received from the customer (or its representative) in advance of services provided.
- Companies should consider estimating a refund liability if it is not probable that newly submitted claims will be sufficient to allow CMS to recoup the advance within the terms of the agreement.

$175 billion allocation

Allocation	Amount	Accounting
Unallocated	$102.6 billion	Terms and conditions are not known and/or accounting treatment is still under discussion.
Unknown allocation for others (dentists, SNF’s etc.)		
Unknown allocation for treatment of the uninsured		
Allocation for Indian Health Services	$400 million	
Allocation for rural providers	$10 billion	Legal terms and conditions vary. All subject to the same accounting conditions and treatment as the General Distribution Fund
Allocation for hospitals serving more low income and uninsured patients	$2 billion	
Allocation for COVID-19 High Impact Areas	$10 billion	
Remainder to be distributed to providers that have already received money via application process	$20 billion	Total $50 billion - Referred to as the “General Distribution Fund” Legal terms and conditions vary. All subject to the same accounting conditions and treatment.
Distribution on April 24 to certain providers based on 2018 cost report revenues		
Initial distribution based on Medicare FFS Revenue	$30 billion	

CARES Act - $50 billion general distribution

- Not-for-profit providers should apply the guidance in ASC 958-605, *Not-For-Profit Entities – Revenue Recognition*, to account for the distribution.
  - Condition - Payment is only to be "used to prevent, prepare for, and respond to coronavirus, and shall reimburse the Recipient only for health care related expenses or lost revenues that are attributable to coronavirus."
    - Lost revenues defined as "*a reasonable method of estimating the revenue during March and April compared to the same period had COVID-19 not appeared. For example, if you have a budget prepared without taking into account the impact of COVID-19, the estimated lost revenue could be the difference between your budgeted revenue and actual revenue. It would also be reasonable to compare the revenues to the same period last year.*
  - Classification – Other operating revenue

CARES Act - $50 billion general distribution

- For-profit entities should account for the distribution as a government grant by analogy to IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*
  - Government grants are recognized when there is reasonable assurance that the grant will be received, and the entity will comply with any conditions attached to the grant.
  - Condition – same as for not-for-profits
  - Classification – IAS 20 provides that grants related to income can be presented in one of two ways:
    - A credit in the income statement, either separately or under a general heading, such as “other income”
    - A reduction to the related expense

Subsequent events disclosures

Events occurring after the balance sheet date but before the financial statements are issued (available to be issued for non-SEC filers) require disclosure or possibly recognition.

	Definition	Financial statement effects
Recognized (Type 1) subsequent events	Provide additional evidence about conditions that existed as of the date of the balance sheet, including estimates inherent in financial reporting. Subsequent events affecting the realization of assets (e.g. receivables or inventories) or the settlement of expected liabilities are recognized if they represent the culmination of conditions that existed over a relatively long period of time.	The financial statements are adjusted for any events or changes in estimates resulting from recognized subsequent events.
Nonrecognized (Type 2) subsequent events	Provide evidence about conditions that did not exist at the date of the balance sheet, but arose after the balance sheet date but before financial statements are issued (available to be issued). Examples include changes in fair value or foreign exchange rates after the balance sheet date.	The nature of the event, and an estimate of its financial effect, or a statement that such an estimate cannot be made, is disclosed if the financial statements would otherwise be misleading.

Subsequent events disclosures (continued)

	Not Yet Issued Calendar-Year Financial Statements	Quarter Ended March 31, 2020
COVID-19 – • Declared a global health emergency in January 2020	Financial reporting impacts will likely be limited to nonrecognized subsequent events that should be disclosed.	The COVID-19 outbreak is a current period event that will require ongoing evaluation to determine the extent to which developments after the respective reporting date should be recognized in that reporting period.
Medicare Accelerated and Advanced Payments • Application process began in late March	Financial reporting impacts will be limited to nonrecognized subsequent events that should be disclosed.	Unless payment was received prior to March 31, financial reporting impacts will be limited to nonrecognized subsequent events that should be disclosed.
CARES Act - $50 billion general distribution • CARES Act enacted March 27, 2020 • Programs to distribute the $100 billion health care fund not created until April 2020	Financial reporting impacts will be limited to nonrecognized subsequent events that should be disclosed.	A provider likely did not have enough information prior to actual receipt of the funds in April 2020 to determine how much, if any, funds would be received or the terms and conditions required to retain the funds. Financial reporting impact will be limited to nonrecognized subsequent events that should be disclosed.

TIMELINE FOR UPCOMING FINANCIAL REPORTING

Upcoming Financial Reporting Timeline

- Borrowers that are subject to Continuing Disclosure Agreements will be obligated to file annual or quarterly disclosures to EMMA in May
  - Annual Reports for Borrowers with FY ended December 31, 2019 are due by mid- to late-May
  - Quarterly Reports for FQ ended March 31, 2020 also are due in mid- to late-May
    - *Quarterly Reports for FQ ended December 31, 2019 were filed on EMMA by beginning of March, prior to the outbreak of COVID-19 in the U.S.*
- Some borrowers additionally may be obligated to file material event notices
    - New Lines of Credit
    - Amendments to existing “financial obligations”

Factors to consider

Labor	• Reduced workforce, either through illness, furlough or permanent reductions? • Are registry services being used? • What policies are in place to support the health and safety of employees? Forward planning around those policies.
Financial Risks and Scenario Planning	• What scenario planning is the borrower doing – near, transition and normalization? • Understand the array of financial and operational risks and how management is addressing under different scenarios (e.g. liquidity and access to capital, exposure to third parties, etc.). • Covenant analysis and management, including asset impairments that may pose significant risks (e.g. investments, goodwill and other intangibles, and pensions).
Understand Key Operational Risks	• What measures are being taken to stabilize the supply chain? • Are technology capabilities able to support an increase in telehealth visits and remote working? • What physical plant changes were made to prepare for COVID-19 patients? Planning around transition to "normal" operations.
Ensure Board is Apprised of Proposed Disclosure	• Understand the scope of the crisis and how management is responding (both internally and externally). • Consider the potential impact of the COVID-19 crisis on the board's operations and effectiveness (e.g. contingency plans in order to meet virtually).
Assess Financial Reporting and Disclosure Impacts	• The SEC has called on companies to monitor the necessity for disclosures regarding the current and potential effects of COVID-19, as well as the adequacy of the company's disclosure controls and procedures in the reporting of this information. • Consider if economic uncertainties and market volatility have or will affect accounting conclusions (e.g. key assumptions and sensitivities). • Consider disclosures related to subsequent events and internal controls over financial reporting.

Allow time for key constituents to contribute

- Given the SEC's urging for more robust disclosure of COVID-19 impact, consider which internal constituents should provide input, in addition to finance:
  - Human resources
  - Medical staff leadership and nursing administration
  - Supply and inventory management
  - Information technology
  - Plant operations
  - Legal and risk management
  - Governing board

BEST PRACTICES FOR DEVELOPING COVID-19 DISCLOSURES

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General approach to COVID-19 disclosures

- Impact of COVID-19 on a health care borrower’s operating and financial condition likely to be “material”
  - Even if not “material,” investors will be expecting disclosure of the impact to the organization and SEC is encouraging disclosure
- Borrowers need to evaluate specific facts and circumstances and develop disclosure that is complete and accurate in all material respects, while taking into account the ***total mix of information available in the market***
- Disclosure of the related risks and circumstances will be different for each borrower, depending on state regulation and local regulations, the outbreak in the communities served, the organization's preparedness response, availability of equipment and supplies, etc.

General approach to COVID-19 disclosures (cont'd)

- Three timelines to analyze:

    - Historical: Quarter ended March 31
    - Today
    - Future: Transition to stabilizing operations

Analyze information for quarter ended March 31

- Does it provide an accurate financial and operational snapshot as of March 31, in light of everything occurring in the borrower's facilities and in the communities served by the borrower?
  - What additional context would be required in order to understand financial results?
    - What material factors contributed to financial performance during that time, including volumes in various service lines, payor mix, investment performance, collection of A/R, and preparedness expenses?
    - Has COVID-19 impacted capital and liquidity resources?
    - What legal or regulatory orders impacted operations?
  - If quarterly covenants are required under any debt, even if not required to be reported to bondholders on EMMA, how did borrower perform?

Analyze information today

- Are post-March 31 financial statements or operating information available?
- If not, are there any events that have occurred since March 31?
  - Receipt of governmental funding: CARES Act, Medicare Accelerated Payment Program, Paycheck Protection Program
    - Any others to which application has been made but funds not received?
  - Liquidity: obtaining new facilities, drawing on existing facilities, issuing or incurring new debt
  - Initiatives to reduce expenses, expand access to equipment and supplies, flex labor resources
  - Impact to financial performance of postponement of elective procedures
  - Non-routine litigation relating to COVID-19

Analyze information today (cont'd)

- Consider the appropriateness of disclosing any of this information
  - Is it accurate?
    - Does it contain estimates or accounting assumptions?
      - SEC has indicated that, with appropriate disclosure regarding the basis for estimates, reconciling preliminary GAAP results that include provisional amounts based on reasonable estimates or a range of reasonable estimates is acceptable
  - Is it complete?
    - Is additional context required for the information to be comprehensible?
  - Is it material?
  - If it has not been presented to the governing board, should it?

Look beyond today (forward-looking statements)

- How do you expect COVID-19 to affect assets on the balance sheet and the ability to timely account for those assets?
  - Any impact to pension funding?
  - Impact on investment performance?
- Projections around returning to elective procedures and projected volume associated with such procedures
- If funds have been received under the Medicare APP, what will be the impact to liquidity when the "earn out" of those funds begins later this calendar year?
- Has litigation relating to COVID-19 been filed by patients, employees or others, naming the organization?

Tools for addressing additional considerations

- Even if continuing disclosure undertaking does not require, the following may be useful for borrowers to provide context to financial and operating performance
- MD&A
  - An effective MD&A will identify known trends, demands, commitments or events
  - Likely that most borrowers would want to clarify that past performance is not indicative of future performance
  - Specific items to address: liquidity, capital resources, near-term cash and debt needs, constraints on access to liquidity or capital, accounting assumptions affecting net revenues or net assets

Tools for addressing additional considerations (cont'd)

- Risk factors
  - Consider whether specific risks exist and would be significant in making an investment decision and avoid industry and other "boilerplate" risks
- Projections
  - Consider how operations and financial condition may change as efforts to fight COVID-19 evolve over next 3-12 months and beyond
    - Anticipated un-budgeted expenses
    - Challenges collecting A/R
    - Changes to demand, including telehealth capabilities, and associated changes to infrastructure
- Review COVID-19 disclosure in primary offering documents

Key take-aways

- Remember that accuracy and completeness of disclosure is analyzed in light of the total mix of information available. Do not provide a historical picture of the COVID-19 pandemic – focus on how it has affected your organization.
- SEC is committing substantial resources to safeguard against potential fraud in the securities market. Any enforcement action or lawsuit will have the benefit of hindsight by regulators and investors.
  - Carefully analyze key factors affecting financial position and financial performance
  - Recognize that otherwise standard disclosure may not be appropriate, in light of COVID-19 impact
  - Scrutinize forward-looking statements . . .

Key take-aways (cont'd)

- Use of forward-looking statements warrants careful consideration
  - SEC is encouraging inclusion of forward-looking statements as beneficial to issuers/borrowers, investors and the capital markets
    - SEC released Public Statement on May 4, directed to the municipal securities industry, encouraging municipal issuers to provide forward-looking information regarding the potential future impact of COVID-19 on their financial and operating conditions
    - Recognition that historical information may not enable investors to assess current and expected future financial condition
  - On the other hand, safe harbors for forward-looking statements by public companies do not apply to issuers and borrowers in the municipal securities market
    - Reasonable basis for projections and disclaimers will be critical

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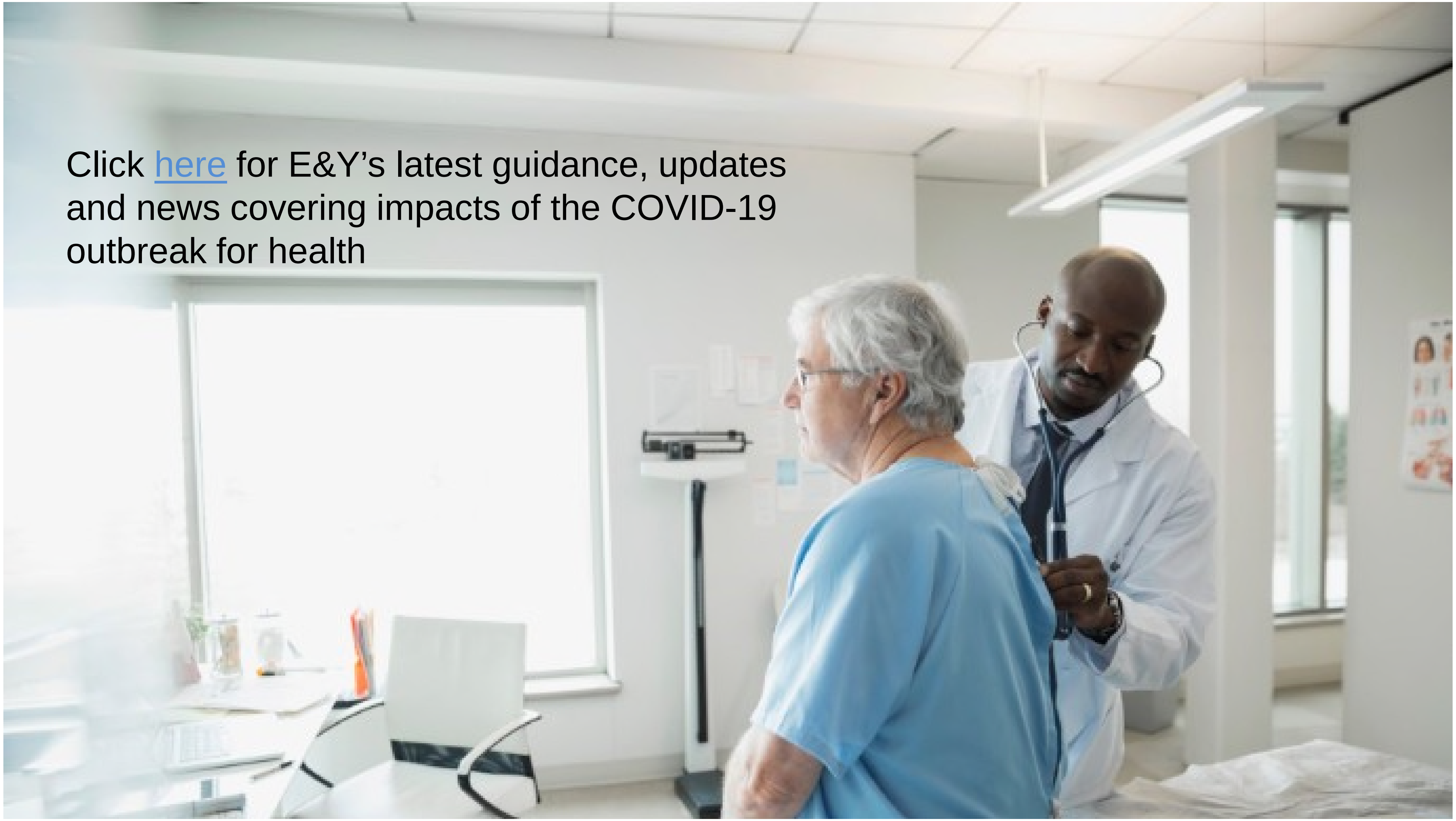
EY Health Resources

Click here for E&Y’s latest guidance, updates and news covering impacts of the COVID-19 outbreak for health



Orrick's COVID-19 Resource Center

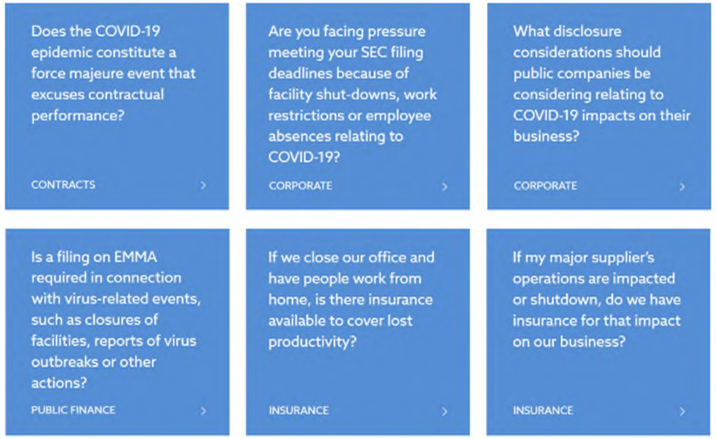
The COVID-19 pandemic is forcing companies and government entities to grapple with disruption while trying to protect employees, business continuity for customers and the long-term health of their businesses.

We launched the [COVID-19 Resource Center] to help guide clients and communities through this quickly moving public health crisis.

The Resource Center features webinars, podcasts, featured blog posts and articles, and resources organized by practice about issues such as:

- **Best practices** for employers managing essential business operations, facility closures and business continuity
- **SBA Loan** applications and other fiscal stimulus and relief programs
- **Employment** issues including workforce reduction planning
- **Global privacy considerations** related to medical disclosures and recordkeeping, and medical testing
- **Insurance coverage** planning, understanding force majeure clauses and supply chain disruption mitigation
- **Disclosure** requirements and SEC filing compliance
- **Commercial tenant** considerations
- **Antitrust** compliance

A growing FAQ collection



Tracking state orders, legislation and courts

We compile and track state-by-state orders, including shelter-in-place comparisons, state legislative updates and schedule changes, and the operating status of the US Supreme and Federal courts.

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