

COMMONWEALTH HEALTHCARE CORPORATION
(A COMPONENT UNIT OF THE COMMONWEALTH
OF THE NORTHERN MARIANA ISLANDS)

REPORT ON THE AUDIT OF FINANCIAL
STATEMENTS IN ACCORDANCE
WITH THE UNIFORM GUIDANCE

YEAR ENDED SEPTEMBER 30, 2018

COMMONWEALTH HEALTHCARE CORPORATION
(A COMPONENT UNIT OF THE COMMONWEALTH
OF THE NORTHERN MARIANA ISLANDS)

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

YEARS ENDED SEPTEMBER 30, 2018 AND 2017

INDEPENDENT AUDITORS' REPORT

Ms. Esther L. Muna
Chief Executive Officer
Commonwealth Healthcare Corporation:

Report on the Financial Statements

We have audited the accompanying financial statements of the Commonwealth Healthcare Corporation (CHCC), a component unit of the Commonwealth of the Northern Mariana Islands (CNMI), which comprise the statements of net position as of September 30, 2018 and 2017, respectively, and the related statements of revenues, expenses and changes in net position and of cash flows for the years then ended and the related notes to the financial statements

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Basis for Qualified Opinion

Management has not adopted Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions*. As discussed in note 2 to the financial statements, CHCC has not recorded pension expense and related net pension asset or liability, deferred inflows of resources and deferred outflows of resources as of and for the years ended September 30, 2018 and 2017. GASB Statement No. 68 requires an employer to recognize its proportionate share of the collective pension expense, as well as the net pension asset or liability, deferred outflows of resources and deferred inflows of resources. The amount by which this departure would affect the assets and deferred outflows of resources, liabilities and deferred inflows of resources, net position and expenses of CHCC has not been determined.

CHCC did not conduct a physical inventory of its capital assets during the years ended September 30, 2018 and 2017. In addition, we were unable to determine the propriety of inventories and related expenses as of and for the years ended September 30, 2018 and 2017 as CHCC could not substantiate general ledger balances due to inadequacies in accounting records.

Qualified Opinion

In our opinion, except for the effects of the matters described in the “Basis for Qualified Opinion” paragraphs, the financial statements referred to above present fairly, in all material respects, the financial position of the Commonwealth Healthcare Corporation as of September 30, 2018 and 2017, and the changes in its net position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matters

Going Concern

The accompanying financial statements have been prepared assuming that CHCC will continue as a going concern. As discussed in note 12 to the financial statements, CHCC has incurred recurring losses and negative cash flows from operations that raise substantial doubt about its ability to continue as a going concern. Management’s plans in regard to these matters are also described in note 12. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

COVID-19

Economic uncertainties as a result of the COVID-19 coronavirus pandemic may negatively impact CHCC’s future financial results as described in note 13 to the financial statements.

Our opinion is not modified with respect to these matters.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 4 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by GASB who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of, and engagement to audit, the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 18, 2022 on our consideration of the CHCC'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 CHCC'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 CHCC's internal control over financial reporting and compliance.

Deloitte & Touche LLC

February 18, 2022



Commonwealth Healthcare Corporation

Commonwealth of the Northern Mariana Islands

1 Lower Navy Hill Road Navy Hill, Saipan, MP 96950



MANAGEMENT'S DISCUSSION AND ANALYSIS Year Ended September 30, 2018

INTRODUCTION

Public Law (PL) 16-51, as amended by PL 19-78, established a public corporation for healthcare and related public health services known as the Commonwealth Healthcare Corporation (CHCC). The mandate created CHCC to "coordinate the delivery of quality healthcare to all Commonwealth residents in a financially responsible manner... the Commonwealth Healthcare Corporation is intended to be a professionally managed, nationally accredited, independent public healthcare institution that is as financially self-sufficient and independent of the Commonwealth Government as is possible".

The following Management's Discussion & Analysis (MD&A) of CHCC's activities and financial performance will serve as an introduction and overview of the audited financial statements of CHCC for fiscal year 2018. The information contained in the MD&A has been prepared by management and should be considered in conjunction with the financial statements and notes which follow this section. Fiscal years 2017 and 2016 comparative information have been included where appropriate.

OVERVIEW OF FINANCIAL STATEMENTS AND FINANCIAL ANALYSIS

Financial Highlights

- CHCC's net position decreased from \$11,386,568 in fiscal year 2017 to \$6,851,281 in fiscal year 2018 due to an increase in operating expenses, primarily in wages and salaries. The significant increase in wages and salaries was primarily due to an increase in rates for providers and medical and other hospital staff to compete with other facilities in the region and minimize employee turnover.
- CHCC received a \$9,531,315 appropriation from the CNMI government, \$7,000,000 of which was earmarked for public health programs and the purchase of hospital equipment.
- CHCC's total assets increased from \$49,255,276 in fiscal year 2017 to \$52,145,334 in fiscal year 2018 and decreased from \$ 49,978,344 in 2016 to \$49,255,276 in fiscal year 2017. Total assets are composed of cash, receivables, advances, due from CNMI, inventories and depreciable capital assets, net of accumulated depreciation.
- CHCC's total liabilities increased from \$37,868,708 in fiscal year 2017 to \$45,294,053 in fiscal year 2018 and decreased from \$43,322,837 in fiscal year 2016 to \$37,868,708 in fiscal year 2017. \$35.6 million or 78.6% of CHCC's total liabilities are due to related parties.
- CHCC's operating revenues increased from \$43,571,827 in fiscal year 2017 to \$46,876,718 in fiscal year 2018 and increased from \$37,831,853 in fiscal year 2016 to \$43,571,827 in fiscal year 2017.

OVERVIEW OF FINANCIAL STATEMENTS AND FINANCIAL ANALYSIS, CONTINUED

Financial Highlights, Continued

- CHCC's operating expenses increased from \$49,343,813 in fiscal year 2017 to \$60,921,133 in fiscal year 2018 and from \$46,967,281 in fiscal year 2016 to \$49,343,813 in fiscal year 2017. The significant increase in expenses is related to support for public health activities funded by earmarked appropriations and an increase in wages and salaries.

A summary of the Statements of Net Position, of Revenues, Expenses and Changes in Net Position and of Cash Flows is presented below:

Statements of Net Position

Assets	2018	2017	2016
Current assets	\$ 19,424,684	\$ 15,720,390	\$ 14,866,927
Depreciable capital assets, net of accumulated depreciation	<u>32,720,650</u>	<u>33,534,886</u>	<u>35,111,417</u>
Total assets	\$ <u>52,145,334</u>	\$ <u>49,255,276</u>	\$ <u>49,978,344</u>
Liabilities and Net Position			
Liabilities:			
Current liabilities	\$ 42,994,358	\$ 35,978,352	\$ 41,646,793
Noncurrent portion of compensated absences	<u>2,299,695</u>	<u>1,890,356</u>	<u>1,676,044</u>
Total liabilities	<u>45,294,053</u>	<u>37,868,708</u>	<u>43,322,837</u>
Net position:			
Net investment in capital assets	32,720,650	33,534,886	35,111,417
Restricted	3,189,234	3,065,351	2,729,734
Unrestricted	<u>(29,058,603)</u>	<u>(25,213,669)</u>	<u>(31,185,644)</u>
Total net position	<u>6,851,281</u>	<u>11,386,568</u>	<u>6,655,507</u>
Total liabilities and net position	\$ <u>52,145,334</u>	\$ <u>49,255,276</u>	\$ <u>49,978,344</u>

Statements of Revenues, Expenses and Changes in Net Position

	2018	2017	2016
Operating revenues	\$ 46,876,718	\$ 43,571,827	\$ 37,831,853
Operating expenses	<u>60,921,133</u>	<u>49,343,813</u>	<u>46,967,281</u>
Operating loss	(14,044,415)	(5,771,986)	(9,135,428)
Nonoperating income (expense), net	<u>9,509,128</u>	<u>10,503,047</u>	<u>3,612,031</u>
Change in net position	(4,535,287)	4,731,061	(5,523,397)
Net position at beginning of year	<u>11,386,568</u>	<u>6,655,507</u>	<u>12,178,904</u>
Net position at end of year	\$ <u>6,851,281</u>	\$ <u>11,386,568</u>	\$ <u>6,655,507</u>

OVERVIEW OF FINANCIAL STATEMENTS AND FINANCIAL ANALYSIS, CONTINUED

Financial Highlights, Continued

Statements of Cash Flows

	2018	2017	2016
Cash flows from operating activities	\$ (4,252,797)	\$ (9,988,206)	\$ (207,127)
Cash flows from noncapital financing activities	9,509,128	10,503,047	3,462,031
Cash flows from capital and related financing activities	<u>(1,655,112)</u>	<u>(784,859)</u>	<u>(1,053,029)</u>
Net increase (decrease) in cash	3,601,219	(270,018)	2,201,875
Cash at beginning of year	<u>5,540,162</u>	<u>5,810,180</u>	<u>3,608,305</u>
Cash at end of year	\$ <u>9,141,381</u>	\$ <u>5,540,162</u>	\$ <u>5,810,180</u>

CHCC'S ANALYSIS AND FINANCIAL CONDITION

At the end of fiscal years 2018, 2017 and 2016, CHCC had total assets of \$52,145,334, \$49,255,276 and \$49,978,344, respectively. These are comprised of cash, receivables, net of allowance for doubtful accounts, advances, due from CNMI, inventories of medical and pharmaceutical supplies and depreciable capital assets, net of accumulated depreciation.

Current liabilities arise from obligations to CHCC's vendors, suppliers, retirement contributions and taxes.

CHCC has notes payable of \$2,850,000 due to the Marianas Public Land Trust (MPLT) resulting from an available line of credit from MPLT to CHCC. See note 5 to the financial statements for more detailed information on CHCC's notes payable to a related party.

Major expenses for CHCC are wages and salaries, benefits, including retirement contributions, payroll taxes, medical supplies including pharmaceuticals and utilities.

Despite being the only hospital in the CNMI, dependence on Medicaid funding and the fact that about half the population is uninsured or underinsured, government appropriations to CHCC have been grossly inadequate. This is illustrated in the operating losses experienced by the CNMI's lone hospital. CHCC has a cumulative \$58 million of unappropriated local Medicaid match from fiscal year 2011 to fiscal year 2017. Had CHCC received this match from the CNMI government, CHCC would have been able to afford payments to its related parties and still have reserve for hospital improvements.

Despite these conditions, CHCC has made tremendous strides to significantly increase operating revenues in recent years as compared to prior fiscal years. The consistent increase in revenues allowed CHCC to make the salaries of medical and hospital staff competitive. Over 90% of all operational expenses are for personnel, medical supplies, pharmaceutical supplies and other required services such as custodial and repair and maintenance services. As can be seen from this, CHCC cannot adopt a cost-reduction business model as reducing staff and medical supplies would be detrimental to hospital operations. Moreover, the community demands and needs the availability of expanded services, which CHCC is striving to achieve. Thus, CHCC's focus is improving revenue generation, seeking out new funding streams and continuing to work with the legislature to obtain direly needed appropriations. CHCC staff are highly committed and focused on striving to provide the highest level of quality for the CNMI's only healthcare system.

CHCC'S ANALYSIS AND FINANCIAL CONDITION, CONTINUED

Capital Assets

At September 30, 2018, 2017 and 2016, CHCC had \$32,720,650, \$33,534,886 and \$35,111,417, respectively, net investment in capital assets. See notes 2 and 4 to the financial statements for more detailed information on CHCC's capital assets.

CHALLENGES AND ACCOMPLISHMENTS

Seven years after its establishment, the insufficient financial support of CHCC is essentially still a lingering factor in the agency's struggles and challenges. This continued throughout fiscal year 2018. CHCC is considered a "safety net" hospital, providing care for the indigent and uninsured population of the CNMI. The Emergency Treatment and Active Labor Act (EMTALA) mandates that CHCC see and treat all those with no ability to pay. Uninsured patients are pervasive in the CNMI and will always be a going concern unless appropriations are provided or businesses are mandated to provide basic insurance coverage to the employees. Moreover, the fact that CHCC does not receive a local match portion of Medicaid payments significantly impacts the CNMI's lone hospital's operations. Despite these continued challenges, there were accomplishments:

- a. Access and availability of hospital and health services continued, including ensuring staff are paid on time, supplies and diagnostic tests are available, health services are accessible, quality control monitoring was performed, repairs and maintenance were completed and overall, ensuring patient safety and quality care; all this while incurring significant uncompensated care costs;
- b. Plans of Correction were accepted by the Centers for Medicare & Medicaid Services (CMS) for the findings on seven hospital Conditions of Participation; CHCC continues to work and focus on CMS requirements to ensure continued certification. Extensions on certification were awarded through FY 2018;
- c. The End Stage Renal Disease (ESRD) program (Dialysis) continues to operate in compliance with CMS standards;
- d. CHCC credentialed and privileged several new members into its medical staff in FY 2018 thereby expanding services in psychiatry, emergency medicine, pediatrics, general surgery, dentistry and obstetrics/gynecology;
- e. The overall CHCC readmission rate in 2018 was 8.3%, compared to the national average of 15.3%;
- d. Hospital-Public Health collaboration and integration continues and are being strengthened with the goal of population health;
 - Immunization of delinquent students enrolled in CNMI schools and daycare centers decreased by 50% in the 2018-2019 school year, compared to the 2017-2018 school year.
 - The CNMI Women, Infants, and Children Program (WIC) has worked to successfully increase breastfeeding initiation rates (the proportion of infants who are ever breastfed) to 94% in 2018, surpassing the Healthy People 2020 target of 81.9%. Breastfeeding leads to healthier outcomes for both the mother and the baby, including reducing the risk of Sudden Infant Death Syndrome.

CHALLENGES AND ACCOMPLISHMENTS, CONTINUED

- In 2018, the CHCC Crisis Counseling Program YUTU provided in-home counseling to over 3,000 community members and conducted 126 group counseling sessions at events and community centers.

ECONOMIC OUTLOOK

CHCC continuously evaluates its service delivery methods and strives to continuously improve despite facing major challenges. Building capacity and expanding medical services is an overarching goal as well and this requires investing in personnel, technology, information systems and infrastructure.

Assuring accountability and compliance is also vital and a focus. CHCC is able to produce financial statements and financial system transactions are aligned to accounting principles. Audit issues are more understood as well and obtaining clean audits with unmodified opinions is another goal of CHCC. Findings and questioned costs are being reduced thereby reducing financial exposure as a result of questioned and disallowed costs emanating from CHCC's single audit.

Improved financial performance is always a goal of CHCC and this can be seen in the improvement in revenue generation compared to prior years. CHCC expects impacts in this regard to be seen more so in FY 2019 and beyond.

CHCC continues to strive for improved staffing development and reorganization, including providing proper tools to assist in the improvements. The contract worker (CW) permit issues will always be a concern, given a large portion of health professionals at CHCC are on the CW visa program. Transitioning CW workers to a more permanent status is essential for the organization.

Even with the severe financing challenges, CHCC has made significant strides towards financial stability, with further gains expected in the future. However, without improvements to Medicaid and other third-party reimbursements, and a reduction in the uninsured population, CHCC will be significantly encumbered when trying to meet its goals. Reducing the rate of uninsured patients in the CNMI through mechanisms such as employer-sponsored and government-sponsored health insurance coverage would significantly improve CHCC's financial stability.

The Management's Discussion and Analysis for the year ended September 30, 2017 is set forth in CHCC's report on the audit of financial statements, which is dated October 25, 2019. That Discussion and Analysis explains the major factors impacting the 2017 financial statements and can be viewed at the Office of the Public Auditor's website at www.opacnmi.com.

CONTACTING CHCC'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, patients and stakeholders a general overview of CHCC's finances and demonstrate its stewardship and accountability with public funds that it collects and receives. If you have any questions about this report or need additional information, please contact CHCC's Chief Executive Officer or Chief Financial Officer at (670) 234-8950, Monday through Friday, 8:00 am to 5:00 pm, except on recognized CNMI government holidays.

COMMONWEALTH HEALTHCARE CORPORATION

Statements of Net Position
September 30, 2018 and 2017

	<u>ASSETS</u>	<u>2018</u>	<u>2017</u>
Current assets:			
Cash		\$ 9,141,381	\$ 5,540,162
Patient accounts receivable, net of estimated uncollectibles of \$16,083,673 in 2018 and \$14,740,800 in 2017		7,474,344	7,684,495
Other receivables		369,258	380,053
Advances		710,889	546,614
Due from CNMI		252,880	202,965
Inventories		1,475,932	1,366,101
Total current assets		19,424,684	15,720,390
Depreciable capital assets, net of accumulated depreciation		32,720,650	33,534,886
Total assets		<u>\$ 52,145,334</u>	<u>\$ 49,255,276</u>
<u>LIABILITIES AND NET POSITION</u>			
Current liabilities:			
Notes payable to a related party		\$ 2,850,000	\$ 2,850,000
Current portion of compensated absences		1,184,691	1,158,606
Accounts payable		5,087,051	3,890,428
Accrued payroll		956,699	587,757
Accrued taxes and other liabilities		10,314,367	7,265,967
Due to related parties		22,415,691	20,225,594
Unearned revenue		185,859	-
Total current liabilities		42,994,358	35,978,352
Compensated absences, net of current portion		2,299,695	1,890,356
Total liabilities		<u>45,294,053</u>	<u>37,868,708</u>
Commitments and contingencies			
Net position:			
Net investment in capital assets		32,720,650	33,534,886
Restricted		3,189,234	3,065,351
Unrestricted		(29,058,603)	(25,213,669)
Total net position		<u>6,851,281</u>	<u>11,386,568</u>
		<u>\$ 52,145,334</u>	<u>\$ 49,255,276</u>

See accompanying notes to financial statements.

COMMONWEALTH HEALTHCARE CORPORATION

Statements of Revenues, Expenses and Changes in Net Position
Years Ended September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Operating revenues:		
Net patient service revenue, net of contractual adjustments and provision for bad debts of \$70,373,398 in 2018 and \$49,464,023 in 2017	\$ 44,625,470	\$ 41,526,713
Other operating revenues:		
Dental services	158,823	309,552
Cafeteria food sales	264,257	206,841
Medical record services	219,716	161,195
Other hospital services	1,113,268	532,390
Contributions	53,000	120,800
Other revenue	442,184	714,336
Total operating revenues, net	<u>46,876,718</u>	<u>43,571,827</u>
Operating expenses:		
Wages and salaries	31,864,445	25,772,829
Supplies	7,249,783	6,377,009
Employee benefits	5,981,684	4,837,892
Utilities	4,749,549	4,542,710
Depreciation	2,469,348	2,361,390
Professional services	2,279,581	1,817,719
Repair and maintenance	839,186	898,271
Cleaning services	809,496	628,799
Cost of sales	532,412	-
Travel	506,243	336,340
Recruitment/repatriation	401,579	156,630
Food items	362,361	362,093
Machinery and equipment	342,521	155,222
Rentals	298,442	128,541
Building improvements	243,602	227,053
Communications	225,002	208,003
Fuel and lubricants	162,484	101,385
Office equipment	151,853	20,163
Printing and photocopying	107,839	75,359
Licenses and fees	107,405	190,852
Freight and handling	106,512	49,111
Furniture and fixtures	64,162	15,409
Vehicles	1,000	-
Miscellaneous	1,064,644	81,033
Total operating expenses	<u>60,921,133</u>	<u>49,343,813</u>
Operating loss	<u>(14,044,415)</u>	<u>(5,771,986)</u>
Nonoperating income (expense):		
Federal grant contributions	17,236,860	17,508,654
CNMI appropriation	9,531,315	10,034,486
Interest expense	(142,500)	(154,212)
Federal grant expenses	(17,116,547)	(16,885,881)
Total nonoperating income (expense), net	<u>9,509,128</u>	<u>10,503,047</u>
Change in net position	<u>(4,535,287)</u>	<u>4,731,061</u>
Net position at beginning of year	<u>11,386,568</u>	<u>6,655,507</u>
Net position at end of year	<u>\$ 6,851,281</u>	<u>\$ 11,386,568</u>

See accompanying notes to financial statements.

COMMONWEALTH HEALTHCARE CORPORATION

Statements of Cash Flows
Years Ended September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Cash received from customers	\$ 47,233,608	\$ 42,051,743
Cash payments to suppliers for goods and services	(14,444,642)	(21,671,193)
Cash payments to employees for services	(37,041,763)	(30,368,756)
Net cash used for operating activities	<u>(4,252,797)</u>	<u>(9,988,206)</u>
Cash flows from noncapital financing activities:		
Cash received from the CNMI	9,531,315	10,034,486
Federal and other contributions received	13,726,126	14,652,281
Payments made under federal programs	(13,605,813)	(14,029,508)
Interest paid on notes payable	(142,500)	(154,212)
Net cash provided by noncapital financing activities	<u>9,509,128</u>	<u>10,503,047</u>
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(1,655,112)	(784,859)
Net cash used for capital and related financing activities	<u>(1,655,112)</u>	<u>(784,859)</u>
Net increase (decrease) in cash	3,601,219	(270,018)
Cash at beginning of year	<u>5,540,162</u>	<u>5,810,180</u>
Cash at end of year	<u>\$ 9,141,381</u>	<u>\$ 5,540,162</u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (14,044,415)	\$ (5,771,986)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Bad debts	1,345,278	6,489,016
Depreciation	2,469,348	2,361,390
(Increase) decrease in assets:		
Receivables:		
General	(1,135,127)	(7,936,360)
Other	10,795	(68,789)
Advances	(164,275)	(70,775)
Due from CNMI	(49,915)	46,573
Inventories	(109,831)	416,854
Increase (decrease) in liabilities:		
Compensated absences	435,424	108,534
Accounts payable	1,196,623	(1,604,199)
Accrued payroll	368,942	133,431
Accrued taxes and other liabilities	3,048,400	(2,440,512)
Due to related parties	2,190,097	(1,651,383)
Unearned revenue	185,859	-
Net cash used for operating activities	<u>\$ (4,252,797)</u>	<u>\$ (9,988,206)</u>
Supplemental disclosure of noncash transactions:		
During the years ended September 30, 2018 and 2017, respectively, CHCC recorded the following noncash transactions:		
Noncash increase in federal grant expenditures	\$ 3,510,734	\$ 2,856,373
Noncash increase in federal grant revenue	(3,510,734)	(2,856,373)
	<u>\$ -</u>	<u>\$ -</u>

See accompanying notes to financial statements.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(1) Organization and Purpose

The Commonwealth Healthcare Corporation (CHCC) is responsible for providing healthcare services in the Commonwealth of the Northern Mariana Islands (CNMI), and was created through CNMI Public Law 16-51, which was amended by CNMI Public Law 19-78. CHCC is governed by a five-member Board of Trustees appointed by the Governor of the CNMI with the advice and consent of the Senate.

(2) Summary of Significant Accounting Policies

The accounting policies of CHCC conform to accounting principles generally accepted in the United States of America, as applicable to governmental entities, specifically proprietary funds. CHCC utilizes the flow of economic resources measurement focus. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Basis of Accounting

All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operation of this fund are included on the statements of net position. Proprietary fund operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net position. The accrual basis of accounting is utilized for proprietary funds. Under this method, revenues are recorded when earned and expenses recorded at the time liabilities are incurred.

Budgets

In accordance with Public Law 3-68, the Planning and Budgeting Act of 1983, CHCC is required to submit annual budgets to the CNMI Office of the Governor.

Concentrations of Credit Risk

Custodial credit risk is the risk that, in the event of a bank failure, CHCC's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the depositor-government's name.

Taxes

Per Public Law 16-51, Section 2811, CHCC is exempt from the Northern Marianas Territorial Income Tax. Therefore, no provision has been made for gross receipts or income taxes in the accompanying financial statements.

Cash

For purposes of the statements of net position and cash flows, cash is defined as cash held in demand deposits and savings. At September 30, 2018 and 2017, total cash was \$9,141,381 and \$5,540,162, respectively, and the corresponding bank balances were \$9,081,172 and \$5,597,803, respectively. All bank balances are maintained in financial institutions subject to Federal Deposit Insurance Corporation (FDIC) insurance. CNMI law does not require component unit funds to be collateralized and thus CHCC's funds, in excess of FDIC insurance, are uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

Patient Accounts Receivable

Accounts receivable for services provided to patients covered under the Medicare and Medicaid programs, privately sponsored managed care programs for which payment is made based on terms defined under formal contracts, and other payers (including self-pay) are recorded at their estimated realizable values based on CHCC's standard fees. A provision for uncollectible accounts is based on management's evaluation of the collectability of current accounts and historical trends. Finance charges or interest is not accrued for past due accounts.

Management believes there are no significant credit risks associated with receivables from government programs. Receivables from managed care programs and others are from various payers who are subject to differing economic conditions. They do not represent any concentrated credit risk to CHCC. Management continually monitors and adjusts the estimated allowances for contractual adjustments and uncollectible accounts.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is stated at an amount that management believes will be adequate to absorb possible losses on accounts receivable that may become uncollectible based on evaluations of the collectability of these accounts and prior collection experience. The allowance is established through an allowance for doubtful accounts charged to bad debts expense. Bad debts are written-off against the allowance based on the specific identification method.

Inventories

Inventories are stated at the lower of cost or market using the first-in/first-out (FIFO) method.

Capital Assets

In accordance with CNMI Public Law 16-51, the CNMI is required to transfer all real properties owned by the CNMI Department of Public Health, and all other real and personal property used exclusively for the functions and duties assumed by CHCC, to CHCC. CHCC has adopted a policy to capitalize items with costs in excess of \$5,000.

Retirement Plan

CHCC contributed to the Northern Mariana Islands Retirement Fund's (NMIRF) defined benefit plan (DB Plan), a cost-sharing, multiple-employer plan established and now administered by the CNMI. On September 30, 2013, the DB Plan was transferred to the Northern Mariana Islands Settlement Fund (NMISF). CHCC also contributes to a defined contribution plan (DC Plan).

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

Retirement Plan, Continued

On August 30, 2012, Public Law 17-79 was enacted to amend Title I of the Commonwealth Code to include the intent of the CNMI to participate in the retirement insurance system established by Title II of the U.S. Federal Insurance Contributions Act (FICA) and for participation to be extended to elected officials, employees, political subdivisions and instrumentalities of the CNMI. On September 11, 2012, Public Law 17-82 *CNMI Pension Reform Recovery Act of 2012* was enacted. Unless specifically exempted or authorized by federal law, Public Law 17-82 provides for mandatory membership of CNMI Government employees and elected officials in the U.S. Social Security system and authorizes employees, who elect to, to buy quarters of service in the U.S. Social Security system from contributions made to the DB Plan. In addition, Public Law 17-82 provides active and inactive DB Plan members the option to voluntarily terminate membership in the DB Plan, withdraw or roll over contributions to the DC Plan and to participate in the U.S. Social Security system without termination of employment or penalty. Further, Public Law 17-82 allows the CNMI Government to continue remitting its 4% employer contribution to the DC Plan unless the employee ceases to contribute its employee share.

On March 11, 2013, Public Law 18-02 was enacted to amend Public Law 17-82 to clarify those provisions necessary to expedite the refunds and to prevent any further frustration of the process. Included in the public law is the amendment of Section 203(a) of Title 1, Division 8, Part 3, which states that the government obligation to withhold and remit the employee's portion to the employee's defined account shall continue with respect to employees who do not terminate membership in the DB Plan. All but nine active CHCC employees voluntarily terminated membership in the DB Plan and CHCC contributed \$266,503 and \$267,317 to the DB Plan during the years ended September 30, 2018 and 2017, respectively.

Defined Contribution Plan (DC Plan)

On June 16, 2006, Public Law No. 15-13 was enacted which created the DC Plan, a multi-employer pension plan and is the single retirement program for all employees whose first time CNMI government employment commences on or after January 1, 2007. Each member of the DC Plan is required to contribute to the member's individual account an amount equal to 10% of the member's compensation. Public Law 17-82 requires CHCC to contribute to each member's individual account an amount equal to 4% unless the employee ceases to contribute its employee share. CHCC's recorded DC contributions for the years ended September 30, 2018 and 2017 were \$738,391 and \$555,810, respectively.

Members of the DC Plan, who have completed five years of government service, have a vested balance of 100% of both member and employer contributions plus any earnings thereon.

Net Position

CHCC's net position is classified as follows:

- Net investment in capital assets: capital assets, net of accumulated depreciation.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

Net Position, Continued

- Restricted: net position subject to externally imposed stipulations that can be fulfilled by actions pursuant to those stipulations or that expire by the passage of time. A restricted net position of \$3,189,234 and \$3,065,351 is recorded at September 30, 2018 and 2017, respectively, based on the differential between recorded restricted receipts and restricted expenses.
- Unrestricted: net position that is not subject to externally imposed stipulations.

Compensated Absences

Vested or accumulated vacation leave that is expected to be liquidated with expendable available financial resources is reported as an expenditure and a liability. Compensated absences are recorded as a long-term liability in the statements of net position with amounts to be paid during the next fiscal year reported as current. CHCC recorded a liability of \$3,484,386 and \$3,048,962 as of September 30, 2018 and 2017, respectively.

Annual leave accumulates at the rate of thirteen working days for each year of service for up to three years of service, nineteen and a half working days for each year of service for three to six years of service, and twenty-six working days for each year of service for more than six years of service. Accrued annual leave is limited to forty-five working days, with any amounts over forty-five days transferred to sick leave.

Operating and Non-Operating Revenue and Expenses

CHCC considers revenues and costs that are directly related to patient and other healthcare operations and exchange transactions to be operating revenues and expenses. Revenues and expenses related to financing and other activities are reflected as non-operating. Revenues are recorded net of contractual adjustments and provision for bad debts of \$70,373,398 and \$49,464,023 for the years ended September 30, 2018 and 2017, respectively.

GASB Statement No. 68

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions* and in November 2013, GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date - an amendment of GASB Statement No. 68*, which revised and established new financial reporting requirements for most governments that provided their employees with pension benefits through plans that are administered through trusts. Management has determined that the CNMI is legally responsible for making contributions to NMISF as a non-employer entity and that net pension obligations are allocated in total to the CNMI. Management acknowledges the requirement to recognize revenue in an amount equal to the non-employer contributing entities' (CNMI) total proportionate share of the collective pension expense that is associated with CHCC. CHCC has not recorded related revenues and pension expense for the years ended September 30, 2018 and 2017 as amounts were not available.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements
September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards

During the year ended September 30, 2018, CHCC implemented the following pronouncements:

- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, which replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*, and provides guidance on reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments.
- GASB Statement No. 81, *Irrevocable Split-Interest Agreements*, which improves accounting and financial reporting for irrevocable split-interest agreements by providing recognition and measurement guidance for situations in which a government is a beneficiary of the agreement.
- GASB Statement No. 85, *Omnibus 2017*, which address practice issues that have been identified during implementation and application of certain GASB Statements including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits).
- GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*, which improves consistency in accounting and financial reporting for in-substance defeasance of debt.

The implementation of these statements did not have a material effect on CHCC's financial statements.

In November 2016, GASB issued Statement No. 83, *Certain Asset Retirement Obligations*, which addresses accounting and financial reporting for certain asset retirement obligations (AROs) associated with the retirement of a tangible capital asset. The provisions in Statement No. 83 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In January 2017, GASB issued Statement No. 84, *Fiduciary Activities*, which establishes criteria for identifying fiduciary activities of all state and local governments. The provisions in Statement No. 84 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2017, GASB issued Statement No. 87, *Leases*, which establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. The provisions in Statement No. 87 are effective for fiscal years beginning after December 15, 2019. Management has yet to determine whether the implementation of this statement will have a material effect on the financial statements.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(2) Summary of Significant Accounting Policies, Continued

New Accounting Standards, Continued

In April 2018, GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*, which improves the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. The provisions in Statement No. 88 are effective for fiscal years beginning after June 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In June 2018, GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, which requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. The provisions in Statement No. 89 are effective for fiscal years beginning after December 15, 2019. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

In August 2018, GASB issued Statement No. 90, *Majority Equity Interests – an Amendment of GASB Statements No. 14 and No. 61*, which improves the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and the relevance of financial statement information for certain component units. The provisions in Statement No. 90 are effective for fiscal years beginning after December 15, 2018. Management does not believe that the implementation of this statement will have a material effect on the financial statements.

Estimates

The preparation of 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(3) Patient Accounts Receivable

CHCC grants credit without collateral to its patients, many of whom are CNMI residents and are insured under third-party payer agreements. Patient accounts receivable at September 30, 2018 and 2017, consist of:

	<u>2018</u>	<u>2017</u>
Third party insurers	\$ 18,658,741	\$ 18,987,752
Patient guarantors	4,101,174	2,444,484
Medicare	<u>798,102</u>	<u>993,059</u>
	23,558,017	22,425,295
Less allowance for uncollectible accounts	<u>(16,083,673)</u>	<u>(14,740,800)</u>
	\$ <u>7,474,344</u>	\$ <u>7,684,495</u>

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements
September 30, 2018 and 2017(4) Capital Assets

Capital asset balances consist of the following as of September 30, 2018 and 2017:

	<u>Estimated Useful Lives</u>	<u>Balance October 1, 2017</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance September 30, 2018</u>
Capital assets being depreciated:					
Building	15 - 50 years	\$ 36,684,165	\$ 415,880	\$ -	\$ 37,100,045
Machinery and equipment	5 - 10 years	4,035,452	954,142	-	4,989,594
Computer software	5 - 10 years	1,255,290	285,090	-	1,540,380
Vehicles	5 - 10 years	215,774	-	-	215,774
		42,190,681	1,655,112	-	43,845,793
Less accumulated depreciation		(8,655,795)	(2,469,348)	-	(11,125,143)
Total capital assets, net		\$ 33,534,886	\$ (814,236)	\$ -	\$ 32,720,650
	<u>Estimated Useful Lives</u>	<u>Balance October 1, 2016</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance September 30, 2017</u>
Capital assets being depreciated:					
Building	15 - 50 years	\$ 36,625,365	\$ 58,800	\$ -	\$ 36,684,165
Machinery and equipment	5 - 10 years	3,309,393	726,059	-	4,035,452
Computer software	5 - 10 years	1,255,290	-	-	1,255,290
Vehicles	5 - 10 years	215,774	-	-	215,774
		41,405,822	784,859	-	42,190,681
Less accumulated depreciation		(6,294,405)	(2,361,390)	-	(8,655,795)
Total capital assets, net		\$ 35,111,417	\$ (1,576,531)	\$ -	\$ 33,534,886

On November 18, 2013, CHCC was advised that properties deeded to CHCC from the CNMI in January 2012 may revert to the CNMI and to the Department of Public Lands. The two properties deeded are located adjacent to the hospital and are currently encumbered by CHCC's loan with MPLT. The primary reason for this change is to increase the properties' earning potential. Management has not yet determined the effect of this change on the accompanying financial statements; however, the property has not been recorded due to the incomplete status of the transfer document between CHCC and the CNMI.

(5) Notes Payable to a Related Party

	<u>2018</u>	<u>2017</u>
Note payable to the Marianas Public Land Trust (MPLT), bearing interest at 5% per annum, due on October 31, 2023. The note is collateralized by CHCC's real properties for CHCC's operational and bridge capital pursuant to CNMI Public Law No. 17-76.	\$ 2,850,000	\$ -
Note payable to the Marianas Public Land Trust (MPLT), bearing interest at 5% per annum, due on June 12, 2018. The note is collateralized by future distributable income in fiscal year 2018 and CHCC's real properties for CHCC's operational and bridge capital pursuant to CNMI Public Law No. 17-76.	-	2,850,000
	<u>\$ 2,850,000</u>	<u>\$ 2,850,000</u>

Loan proceeds extinguished a prior loan obtained for operations.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(6) Long-Term Liability

Changes in long-term liability for the years ended September 30, 2018 and 2017, are as follows:

	Balance October <u>1, 2017</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2018</u>	Due Within <u>One Year</u>
Compensated absences	\$ <u>3,048,962</u>	\$ <u>2,201,149</u>	\$ <u>(1,765,725)</u>	\$ <u>3,484,386</u>	\$ <u>1,184,691</u>
	Balance October <u>1, 2016</u>	<u>Additions</u>	<u>Reductions</u>	Balance September <u>30, 2017</u>	Due Within <u>One Year</u>
Compensated absences	\$ <u>2,940,428</u>	\$ <u>1,969,207</u>	\$ <u>(1,860,673)</u>	\$ <u>3,048,962</u>	\$ <u>1,158,606</u>

(7) Risk Management

CNMI Public Law 16-51 established CHCC as a public corporation with certain limitations on liability provided by the CNMI Government Liability Act (GLA) and immunity from seizure of its property to pay judgment debts. CHCC employees are covered by CNMI Public Law 15-22, which amended the GLA, which provides that employees who have been personally sued for actions taken within the scope of their employment may have the government substituted as the defendant and the employee dismissed from the suit. CHCC is "self-insured" meaning it has no insurance coverage. When a malpractice action is filed naming an individual health care provider who works for the government as a defendant, Public Law 15-22 requires that the health care provider be dismissed from the lawsuit, and the government substituted as the defendant, upon certification by the CNMI Attorney General that the provider was acting within the scope of his or her employment at the time of the alleged negligence. Public Law 15-22 operates to substitute the CNMI government, not CHCC, as the defendant in place of the individual CHCC employee. Public Law 16-51 is clear that CHCC is a CNMI government corporation covered by the immunities reserved to the government under the GLA. The GLA provides that judgments against CNMI public corporations are treated as judgments against the CNMI for the purpose of enforcement and payment. A judgment against CHCC may only be paid upon a specific appropriation by the CNMI Legislature for that purpose. Absent an appropriation by the legislature, CHCC is prohibited from paying a judgment rendered against it.

CHCC will report all of its risk management activities, if and when such occurs. Claims expenditures and liabilities will be reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Losses, if reported, would include an estimate of claims that have been incurred but not reported. No losses as a result of these risks have occurred or have been reported within the last three years.

(8) Related Party Transactions

Total related party transactions for the years ended September 30, 2018 and 2017, and the related receivable and payable balances, are as follows:

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements
September 30, 2018 and 2017(8) Related Party Transactions, Continued

	2018			
	<u>Revenues and Other Contributions</u>	<u>Expenses</u>	<u>Payables</u>	<u>Receivables</u>
Commonwealth Utilities Corporation	\$ -	\$ 4,749,549	\$ 19,234,412	\$ -
CNMI Government	<u>9,531,315</u>	<u>-</u>	<u>3,181,279</u>	<u>252,880</u>
	<u>\$ 9,531,315</u>	<u>\$ 4,749,549</u>	<u>\$ 22,415,691</u>	<u>\$ 252,880</u>
	2017			
	<u>Revenues and Other Contributions</u>	<u>Expenses</u>	<u>Payables</u>	<u>Receivables</u>
Commonwealth Utilities Corporation	\$ -	\$ 4,542,710	\$ 14,772,748	\$ -
CNMI Government	<u>10,034,486</u>	<u>487,011</u>	<u>5,452,846</u>	<u>202,965</u>
	<u>\$ 10,034,486</u>	<u>\$ 5,029,721</u>	<u>\$ 20,225,594</u>	<u>\$ 202,965</u>

Notes payable to MPLT aggregate \$2,850,000 at September 30, 2018 and 2017. Related interest expense for the years ended September 30, 2018 and 2017 amounted to \$142,500 and \$154,212, respectively.

CHCC recorded contributions from the CNMI of \$9,531,315 and \$10,034,486 during the years ended September 30, 2018 and 2017, respectively. Due from CNMI of \$252,880 and \$202,965 relates to unreconciled amounts at September 30, 2018 and 2017, respectively. Due to the CNMI relates to the 1% Public Auditor fee \$-0- and \$2,232,608 at September 30, 2018 and 2017, respectively, and CHCC's contribution to the DB Plan of \$3,181,279 and \$3,220,238, respectively (see note 11).

(9) Patient Service Revenue

CHCC has agreements with third-party payers that provide for payments to CHCC at amounts different from its established rates. A summary of the payment arrangements with major third-party payers follows:

- Medicare - CHCC is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by CHCC and audits thereof by the Medicare administrative contractor. Professional services are reimbursed based on a fee schedule. The estimated amounts due to or from CHCC are reviewed and adjusted annually based on the status of such audits and any subsequent appeals. Differences between final settlements and amounts accrued in previous years are reported as adjustments to patient service revenue in the year examination is substantially completed.
- Medicaid - CHCC is reimbursed by the CNMI Medicaid Program for agreed monthly capitation payments. Based on the CNMI State Plan, CHCC is paid only the Federal portion of the certified public expenditures. The unreimbursed amounts are recorded as charity care.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(9) Patient Service Revenue, Continued

Gross patient revenue from the Medicare and Medicaid programs accounted for approximately 22 percent and 40 percent, respectively, of CHCC's gross patient revenue for the year ended September 30, 2018, and 29 percent and 21 percent, respectively, of CHCC's gross patient revenue for the year ended September 30, 2017. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term.

CHCC also has entered into payment agreements with certain commercial insurance carriers. Commercial insurance companies reimbursed CHCC at negotiated charges.

Patient service revenues for the years ended September 30, 2018 and 2017 are as follows:

	<u>2018</u>	<u>2017</u>
Services provided to Medicare patients	\$ 24,882,120	\$ 26,306,049
Services provided to Medicaid patients	28,316,811	18,903,357
Services provided to third-party payer	20,401,315	22,498,747
Services provided to self-pay and other patients	<u>24,608,513</u>	<u>23,282,583</u>
	98,208,759	90,990,736
Less contractual adjustments and provisions for uncollectible accounts	<u>(53,583,289)</u>	<u>(49,464,023)</u>
Net patient service revenue	\$ <u>44,625,470</u>	\$ <u>41,526,713</u>

(10) Commitments

CHCC leases a portion of its office space, located on the second floor of the Commonwealth Health Center. The lease agreement provides for an annual rental of \$79,500 during the term of the lease. Total lease income for the years ended September 30, 2018 and 2017 is \$92,161 and \$79,500, respectively. Minimum future lease income is \$13,250 for the year ending September 30, 2019.

CHCC engages in various contracts to sustain hospital operations. Future contract commitments for the year ended September 30, 2018 have not been determined.

(11) Contingencies

At September 30, 2018 and 2017, CHCC recorded outstanding Medicare liabilities of \$2,571,911 and \$78,686, respectively.

CHCC participates in a number of federally assisted grant programs funded by the United States Government. These programs are subject to financial and compliance audits to ascertain if Federal laws and guidelines have been followed. Cumulative questioned costs of \$1,489,403 have been set forth in CHCC's Single Audit Report for the year ended September 30, 2018 and is comprised of questioned costs of \$791,456 for fiscal year 2018, \$685,575 for fiscal year 2017 and \$12,372 for fiscal year 2015. The ultimate disposition of these questioned costs can be determined only by final action of the respective grantor agencies. Therefore, no provision for any liability that may result upon resolution of this matter has been made in the accompanying financial statements.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements September 30, 2018 and 2017

(11) Contingencies, Continued

In April 2012, a court order was issued by the CNMI Superior Court authorizing autonomous agencies to remit employer contributions of 30% of covered payroll to NMIRF. On September 30, 2013, the United States District Court for the Northern Mariana Islands approved a Settlement agreement in a Class Action Settlement (Settlement), between a retiree (individually and on behalf of similarly-situated persons) and the CNMI, NMIRF and others. The Settlement includes the creation of the Settlement Fund to accept the transfer of NMIRF assets, receive annual contributions and payments by the CNMI and to carry out the consent judgment entered by the District Court. Further, Section 8.1 of the Settlement assigns the CNMI the rights to collect deficient employer contributions and related costs as of August 6, 2013 from autonomous agencies.

At September 30, 2018 and 2017, CHCC recorded outstanding and deficient employer contributions due to the CNMI of \$3,181,279 and \$3,220,238, respectively. The amount confirmed by the CNMI was \$6,842,972 (inclusive of interest totaling \$174,483) resulting in a variance of \$3,661,693 and \$3,622,734 at September 30, 2018 and 2017, respectively. An assessment of the outstanding and deficient employer contributions has not been determined and, accordingly, employer contributions of \$3,661,693 and \$3,622,734 are not reflected in the accompanying financial statements at September 30, 2018 and 2017, respectively.

CHCC records expenditures for sick leave when the leave is actually taken. Sick leave is compensated absence during work hours arising from employee illness or injury. No liability is recorded for nonvesting accumulating rights to receive sick pay benefits. CHCC could not determine the amount of accumulated unused sick leave as of September 30, 2018 and 2017.

(12) Going Concern

CHCC incurred operating losses of \$14,044,415 and \$5,771,986 and negative cash flows from operations of \$4,252,797 and \$9,988,206 for the years ended September 30, 2018 and 2017, respectively. On May 21, 2014, the CNMI Superior Court issued a temporary restraining order (TRO) and preliminary injunction prohibiting CUC from disconnecting any utility services provided to CHCC. On June 2, 2014, the Superior Court ordered CHCC to make timely payments of monthly billings, exclusive of interest or penalties, and determine non-essential meters to be terminated. On March 19, 2015, the Superior Court found CHCC to be in contempt of the court's orders issued on June 2, 2014 and January 20, 2015 and ordered sanctions subject to conditions stipulated in the order.

CHCC management has taken the following actions and measures to address losses and negative cash flows from operations:

- Continue evaluation of the fee structure to determine if changes/adjustments are necessary;
- Continued evaluation of the billing system and collection processes to determine changes to be made;
- Enhancement of the personnel structure and invest in staff and expansion;
- Implementation of the business and strategic plan; and
- Develop plans for alternative revenue generating methods.

CHCC is dependent on the CNMI Government to provide additional funding for operations.

COMMONWEALTH HEALTHCARE CORPORATION

Notes to Financial Statements
September 30, 2018 and 2017

(13) Subsequent Events

On November 1, 2018, MPLT renewed CHCC's line of credit totaling \$2,850,000 with interest at 5% per annum and due on September 1, 2023.

Economic uncertainties have arisen as a result of the COVID-19 coronavirus pandemic. CHCC expects this matter to negatively impact its future financial results; however, the related financial impact cannot be reasonably estimated at this time. Other financial impacts could occur though such potential impact is unknown.