

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**
Independent Auditor's Report and Financial Statements
February 28, 2021 and February 29, 2020

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas
February 28, 2021 and February 29, 2020**

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Independent Auditor's Report

Board of Trustees
Harris County Hospital District,
d/b/a Harris Health System
Houston, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities and the aggregate discretely presented component units of Harris County Hospital District, d/b/a Harris Health System (the System), collectively a component unit of Harris County, Texas, as of and for the years ended February 28, 2021 and February 29, 2020, and the related notes to the financial statements, which collectively comprise the System's basic financial statements as listed in the table of contents.

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 opinions on these financial statements based on our audits. We did not audit the financial statements of the Harris County Hospital District Foundation (Foundation), a discretely presented component unit of the System, which represent 11.7 percent and 13.6 percent of total assets, 20.4 percent and 28.0 percent of net position and 0.2 percent and 0.3 percent of revenues, respectively, of the aggregate discretely presented component units for the years ended February 28, 2021 and February 29, 2020. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Foundation, is based solely on the report of the other auditors. 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 audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. The financial statements of the discretely presented component units, which are included in the System's financial statements, were not audited in accordance with *Government Auditing Standards*.

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 System'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 System's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the aggregate discretely presented component units of the System as of February 28, 2021 and February 29, 2020, and the respective changes in financial position and, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, pension and other postemployment benefit information, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, 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 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.

Board of Trustees
Harris County Hospital District,
d/b/a Harris Health System
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Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 24, 2021, on our consideration of the System'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 the System'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 the System's internal control over financial reporting and compliance.

BKD, LLP

Dallas, Texas
June 24, 2021

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas
Management's Discussion and Analysis
February 28, 2021 and February 29, 2020**

Introduction

This section of the Harris Health System's (the System or Harris Health) financial report presents background information and management's analysis of the System's financial results for the fiscal years ended February 28, 2021 and February 29, 2020. This section should be read in conjunction with the System's financial statements.

Significant Activities and Initiatives in Fiscal Year 2021

On March 2, 2020, the first business day of the new fiscal year 2021, the System welcomed its new President and Chief Executive Officer, Dr. Esmail Porsa. Ten days later, in response to a confirmed community-spread case of COVID-19 in Montgomery County, the City of Houston and Harris County issued local public health disaster declarations. On March 20, Harris Health established an Incident Command Center for COVID-19 response and admitted the first six COVID-19 positive patients to Ben Taub and LBJ Hospitals. By mid-July, the capacity of the System's intensive care units was about 90% full and COVID-19 patients accounted for 35% of the total inpatient census. The same scenario played out again in January-February 2021 during the second, prolonged peak of the COVID-19 pandemic in the Houston area.

The rise in COVID-19 cases in Houston in fiscal 2021 stressed Harris Health's clinical operations and triggered multi-phase surge plans. This led to suspension of non-emergent procedures and facility closures across the System. However, it also brought out the best of creativity and extraordinary solutions to meet patient needs in the new environment. Harris Health's team of teams built a brand new telemedicine platform and facilitated over 470 thousand telehealth visits; delivered medications directly to patient homes or hospital beds prior to discharge; partnered with the Harris County Public Health Department to operate a 24/7 nurse call center; provided curbside food delivery through the Food Farmacy program; deployed nurse navigators to support COVID patients; and implemented a work-from-home program for members of Harris Health's staff.

Financially, Harris Health experienced a more subdued downside effect from the volume losses than many of its counterparts within the Houston area. Since the majority of the System's patient population do not have the ability to pay for services, Harris Health's diversity of funding sources comprised of property tax revenue and governmental supplemental programs allowed it to weather the storm with fewer disruptions. In addition, federal funding received for uninsured COVID-19 patients from the Provider Relief Fund provided for sustained operational support.

While the COVID-19 pandemic strained the System's capacity and resources, management's resolve to move through the challenges coupled with the imperative to improve patient safety and outcomes, continues to inform its vision and strategy for fiscal 2022 and beyond. Based on the solid financial foundation built over the last six fiscal years, Harris Health is optimistic about the next fiscal year despite some uncertainty still in the air.

Harris Health’s component units, the Community Health Choice HMOs (Community Health Choice Texas, Inc. – the Medicaid Managed Care HMO, and Community Health Choice, Inc. – the Health Insurance Marketplace and commercial HMO) experienced a membership increase of approximately 18.9 percent and a decrease of approximately 8.6 percent in calendar year 2020 and 2019, respectively.

Financial Highlights

- The System's net position increased approximately \$323 million (65.7 percent) in fiscal 2021 and increased \$91 million (22.7 percent) in fiscal 2020. The increase in net position for fiscal year 2021 is primarily due to increases in operating revenue as discussed below.
- Total assets and deferred outflows of resources increased \$531 million (28.8 percent) and \$235 million (14.6 percent) in fiscal year 2021 and fiscal year 2020, respectively, due to increases in reimbursement for patient services. This resulted in cash reinvested in operations, i.e. in capital assets and short-term investments. During fiscal 2021 and 2020, the System invested \$95 million and \$82 million, respectively, in facility related projects, critical information technology and medical equipment. Significant capital acquisitions and resource investments are discussed in the “Capital Assets and Debt Financing” section below.
- The ad-valorem tax base increased approximately 3.7 percent and 3.9 percent in fiscal 2021 and fiscal 2020, respectively. In fiscal 2021, the base rate for maintenance and operations remained the same as fiscal 2020 at 16.491 cents per one hundred dollars of assessed value. The System’s tax rate to fund debt service requirements for the Series 2016 and Series 2020 Certificates of Obligation was adjusted upward due to the issuance of the Series 2020 Certificates of Obligation.

Financial Statements

The System's financial statements are prepared on the accrual basis of accounting and present the System's operational activities in a manner similar to that of private sector companies. The financial statements consist of three statements: (1) statements of net position, (2) statements of revenues, expenses and changes in net position and (3) statements of cash flow. The statements provide information about the activities of the System, the Harris County Hospital District Foundation (the Foundation), and the Community Health Choice HMOs, which are reported as discretely presented component units. The statements of net position and the statements of revenues, expenses and changes in net position reflect the System's financial position at the end of the fiscal year and report the net position and changes as a result of the revenues and expenses for the year. The statement of net position presents the assets, deferred outflows, liabilities, deferred inflows and net position of the System at the end of the year. The net position section presents assets plus deferred outflows of resources, less liabilities, less deferred inflows of resources. Increases or decreases in net position are an indicator of whether financial health is improving or deteriorating. Other nonfinancial factors should be considered, however, in evaluating financial health, such as changes in the System's patient base, changes in economic conditions, taxable property values and tax rates, and changes in government legislation. The statement of cash flows reports cash receipts, cash payments, and net changes in cash resulting from operations, investing and noncapital/capital financing activities. The statement explains where cash came from, how it was used and the change in cash balance during the year.

Table 1
Condensed Statements of Net Position
(In millions)

	2021	2020	Dollar Change	Total Percentage Change	2019	Dollar Change	Total Percentage Change
Assets							
Current and other assets	\$ 1,660	\$ 1,244	\$ 416	33.4%	\$ 1,064	\$ 180	16.9%
Capital assets	526	492	34	6.9%	466	26	5.6%
Total assets	2,186	1,736	450	25.9%	1,530	206	13.5%
Deferred outflows of resources:							
Derivative financial instrument	16	19	(3)	-15.8%	8	11	137.5%
Resources related to pension	38	26	12	46.2%	60	(34)	-56.7%
Resources related to OPEB	126	53	73	137.7%	-	53	0.0%
Unamortized loss on refunding debt	8	9	(1)	-11.1%	10	(1)	-10.0%
Total deferred outflows	188	107	81	75.7%	78	29	37.2%
Total assets and deferred outflows of resources	\$ 2,374	\$ 1,843	\$ 531	28.8%	\$ 1,608	\$ 235	14.6%
Liabilities							
Long-term debt outstanding	\$ 329	\$ 305	\$ 24	7.9%	\$ 316	\$ (11)	-3.5%
Current liabilities	358	267	91	34.1%	165	102	61.8%
Other liabilities	759	724	35	4.8%	726	(2)	-0.3%
Total liabilities	1,446	1,296	150	11.6%	1,207	89	7.4%
Deferred inflows of resources:							
Resources related to pension	90	30	60	200.0%	-	30	100.0%
Resources related to OPEB	23	25	(2)	-8.0%	-	25	100.0%
Total deferred inflows	113	55	58	105.5%	-	55	-100.0%
Net investment in capital assets	204	174	30	17.2%	179	(5)	-2.8%
Restricted	34	33	1	3.0%	33	-	0.0%
Unrestricted	577	285	292	102.5%	189	96	50.8%
Total net position	815	492	323	65.7%	401	\$ 91	22.7%
Total liabilities and deferred inflows of resources and net position	\$ 2,374	\$ 1,843	\$ 531	28.8%	\$ 1,608	\$ 235	14.6%

Net Position

Total net position represents the residual interest in the System's assets and deferred outflows after liabilities and deferred inflows are deducted. As stated previously, net position increased \$323 million (65.7 percent) and increased \$91 million (22.7 percent) in fiscal 2021 and 2020, respectively.

Total assets and deferred outflows of resources increased approximately \$531 million (28.8 percent) between fiscal 2020 and fiscal 2021 and increased approximately \$235 million (14.6 percent) between fiscal 2019 and fiscal 2020.

- Current and other assets increased \$416 million (33.4 percent) from fiscal 2020 to fiscal 2021. Cash equivalents and short-term investments increased \$359 million (56.6 percent) from fiscal 2020 to fiscal 2021 due to cash inflows from patient service revenues and Medicaid supplemental program revenues that were invested. Restricted cash increased over \$18 million (50.0 percent) from 2020 to 2021 due to cash held for the benefit of the Harris County Hospital District Local Provider Participation Fund at February 28, 2021. Assets limited as to use decreased \$9 million (16.0 percent) due to the use of the 2016 bond proceeds for the Ben Taub Hospital construction projects offset with the issuance of the Series 2020 certificates of obligation discussed in detail in “Capital Assets and Debt Financing” below.

- Current and other assets increased \$180 million (16.9 percent) from fiscal 2019 to fiscal 2020. Short-term investments increased \$177 million (44.4 percent) from fiscal 2019 to fiscal 2020 due to cash inflows from patient service revenues and Medicaid supplemental program revenues that were invested. Restricted cash increased over \$35 million (100.0 percent) from 2019 to 2020 due to cash held for the benefit of the newly established Harris County Hospital District Local Provider Participation Fund at February 28, 2020. Assets limited as to use decreased \$39 million (41.0 percent) due to the use of the 2016 bond proceeds for the Ben Taub Hospital construction projects.
- Capital assets are discussed in detail following Table 3.
- Deferred outflows of resources consist of the fair market value of derivatives, unamortized losses on refunding of debt and resources related to the System's pension and postemployment health benefit liability plans. In fiscal 2021, deferred outflows related to derivatives decreased \$3 million due to current interest rates, pension increased \$12 million due to actual versus projected investment performance and changes in assumptions, and postemployment health benefit increased \$73 million due to changes in actuarial assumptions. In fiscal 2020, deferred outflows related to derivatives increased \$11 million due to current interest rates, pension decreased \$34 million due to actual versus projected investment performance, and postemployment health benefits increased \$53 million due to changes in actuarial assumptions.

Total liabilities and deferred inflows of resources increased \$208 million (15.4 percent) and \$144 million (11.9 percent) in fiscal 2021 and 2020, respectively.

- In 2021, increases in bond-related debt reflect scheduled debt service payments offset with the issuance of the Series 2020 certificates of obligation. See “Capital Assets and Debt Financing” below for a detailed discussion.
- Other liabilities increased \$35 million or 4.8 percent in fiscal 2021 and decreased \$2 million or 0.3 percent in fiscal 2020.
 - The System's net obligation for the provision of certain postemployment healthcare benefits increased \$102 million in fiscal 2021 and increased \$42 million in fiscal 2020, primarily due to change in actuarial assumptions.
 - The System's net pension liability decreased \$63 million in fiscal 2021 and \$55 million in fiscal 2020, primarily due to change in net investment income and changes in actuarial assumptions.
 - The derivative liability decreased \$3 million in fiscal 2021 and increased \$11 million in fiscal 2020 primarily due to current interest rates.
- Deferred inflows of resources related to pension and postemployment health benefit increased \$58 million in fiscal 2021 and increased \$55 million in fiscal 2020, due to actual versus projected investment performance and changes in assumptions.

Summary of Revenues, Expenses and Changes in Net Position

The following table summarizes the System's revenues and expenses for each of the years ended February 28, 2021, February 29, 2020 and February 28, 2019, and the changes in net position during each of those years.

Table 2
Condensed Summary of Revenues, Expenses and Changes in Net Position
(In thousands)

	2021	2020	2019
Operating Revenues			
Net patient service revenue	\$ 695,234	\$ 591,357	\$ 477,758
Medicaid supplemental programs revenues	563,923	290,557	194,478
Other operating revenues	34,168	32,938	27,147
Total operating revenues	<u>1,293,325</u>	<u>914,852</u>	<u>699,383</u>
Operating Expenses			
Salaries, wages and benefits	894,277	838,483	760,390
Purchased services, supplies and other	826,853	716,439	616,352
Depreciation and amortization	59,751	54,650	53,349
Total operating expenses	<u>1,780,881</u>	<u>1,609,572</u>	<u>1,430,091</u>
Operating Loss	<u>(487,556)</u>	<u>(694,720)</u>	<u>(730,708)</u>
Nonoperating Revenues			
Ad valorem tax revenues - net	780,713	767,515	739,022
Tobacco settlement revenues	12,924	13,797	15,248
Provider Relief Fund revenue	22,134	-	-
Investment income	4,434	15,089	11,423
Total nonoperating revenues	<u>820,205</u>	<u>796,401</u>	<u>765,693</u>
Nonoperating Expenses			
Interest expense	(10,920)	(10,866)	(11,168)
Other	1,517	(604)	(97)
Total nonoperating expenses	<u>(9,403)</u>	<u>(11,470)</u>	<u>(11,265)</u>
Income Before Capital Contributions	323,246	90,211	23,720
Capital contributions	-	-	769
Change in net position	<u>323,246</u>	<u>90,211</u>	<u>24,489</u>
Net Position - Beginning of Year, as Previously Stated	491,545	401,334	507,935
Prior period adjustment	-	-	(131,090)
Net Position - Beginning of Year, as Restated	<u>491,545</u>	<u>401,334</u>	<u>376,845</u>
Net Position - End of Year	<u>\$ 814,791</u>	<u>\$ 491,545</u>	<u>\$ 401,334</u>

Operating Revenues

Operating revenues increased \$378 million (41.4 percent) during the fiscal year ended February 28, 2021. During the year ended February 29, 2020, the System's total operating revenue increased \$215 million (30.8 percent).

- Net patient service revenue increased \$104 million in fiscal 2021 and \$114 million in fiscal 2020. The increase was attributed to \$115 million in COVID-19 claims reimbursement for the uninsured, provided by the federal Health Resources & Services Administration (HRSA) program as a response to the COVID-19 pandemic. In fiscal 2020, approximately \$50 million of growth in Medicare disproportionate share (DSH) add-on payments was due to the phased-in adoption by the Centers for Medicare and Medicaid Services (CMS) of the Medicare cost report uncompensated care methodology. The revised calculations typically benefit large urban safety net hospitals, such as the

System. The three-year transition to the new allocation methodology for Medicare DSH finalized with the close of federal fiscal year 2020 in September 2020.

- The System participates in the Uncompensated Care (UC) Pool, Medicaid Disproportionate Share (Medicaid DSH), Delivery System Reform Incentive Payment (DSRIP) Pool, Network Access Improvement Program (NAIP), Uniform Hospital Rate Increase Program (UHRIP) and Graduate Medical Education (GME) Medicaid supplement programs. Revenue from government programs increased \$273 million in fiscal 2021 due to the resizing of the State's UC pool and the charity allocation changes that started in federal fiscal year 2020, as well as the higher federal medical assistance percentage (FMAP) provided under the CARES Act. In fiscal 2020, supplemental program revenue increased by \$96 million due to the UC program changes described above.

Operating Expenses

Total operating expenses increased \$171 million (10.6 percent) during the fiscal year ended February 28, 2021. During the year ended February 29, 2020, the System's total operating expenses increased \$179 million (12.6 percent).

- Overall, the System spent \$165 million in total cost related to the COVID-19 pandemic in fiscal 2021. Purchased services, supplies, and other operating expenses increased \$110 million (15.4 percent) in fiscal 2021, primarily due to increases in physician cost, purchased medical and non-clinical services, and medical insurance subsidies. In fiscal 2020, the same category of expenses increased \$100 million (16.2 percent).
- In fiscal 2021, the System's salaries and wages increased \$47 million (7.8 percent) as a direct response to the COVID-19 pandemic. In addition to regularly scheduled merit increases, the System implemented programs related to retention of nursing and other clinical staff, incurred COVID surge pay differentials and provided emergency facility closure time-off benefits to staff. In fiscal 2020, salaries and wages increased \$52 million (9.3 percent) as a result of wage market adjustments, staffing growth due to the CMS resurvey preparedness activities, and an update in the paid time-off accrual methodology at year end.
- Related benefits increased \$9 million (3.7 percent) in fiscal 2021 primarily due to increase in the labor cost and increased postretirement health benefits as a result of updated actuarial estimates. In fiscal 2020, benefits increased \$26 million (12.9 percent) primarily due to the staffing growth and increased pension and postretirement health benefits.

Overall, the System's operating loss improved 29.8 percent from 2020 to 2021 and improved 4.9 percent from 2019 to 2020 as a result of the items discussed above. The System receives property tax revenues to subsidize the cost of services provided to qualified uninsured patients. Although the costs incurred to provide these services are reflected above as operating expenses, the property tax revenues are required to be reported as non-operating revenues.

Non-operating Revenues (Expenses)

Non-operating revenues and expenses consist of revenues and expenses related to financing and investing types of activities, including grants and donations for activities not considered as operating activities, and include property tax revenue, investment income, tobacco settlement funds, interest expense, and gains or losses on disposal of assets.

Tax revenues, net of related expenses, increased over \$13 million, or 1.7 percent, in fiscal 2021 and \$28 million, or 3.9 percent, in fiscal 2020. The current tax rate for maintenance and operations of 16.491 cents per one hundred dollars of assessed value remained the same as in fiscal 2020. Despite the flat tax rate, tax revenues increased due to the corresponding growth in the ad-valorem tax base in Harris County

and the slight increase in the debt service portion of the tax rate due to the issuance of Series 2020 certificates of obligation.

The System received approximately \$13 million and \$14 million in tobacco settlement revenue in fiscal year 2021 and 2020, respectively.

On March 27, 2020, President Trump signed into law the *Coronavirus Aid, Relief, and Economic Security Act* (CARES ACT). The System received grants totaling approximately \$78 million pursuant to the CARES Act provider relief fund provisions, as well as under \$3 million in in-kind donations and insurance reimbursement. At February 28, 2021, the System recognized \$22 million of the CARES proceeds to cover costs associated with preventing, preparing for and responding to coronavirus as reimbursement for eligible health care related expenses.

Capital Assets and Debt Financing

During fiscal 2021 and 2020, the System invested \$95 million and \$82 million, respectively, in information technology, equipment, and facility expansion and renovation.

Table 3 summarizes the changes in the System's capital assets between February 28, 2021, February 29, 2020 and February 28, 2019:

Table 3
Changes in Capital Assets
(In thousands)

	2021	2020	Dollar change	Total percentage change	2019	Dollar change	Total percentage change
Land and improvements	\$ 46,829	\$ 46,180	\$ 649	1.4%	\$ 45,435	\$ 745	1.6%
Buildings and fixed equipment	722,584	706,083	16,501	2.3%	659,640	46,443	7.0%
Major movable equipment	420,188	410,477	9,711	2.4%	387,639	22,838	5.9%
Subtotal	1,189,601	1,162,740	26,861	2.3%	1,092,714	70,026	6.4%
Less accumulated depreciation	(742,149)	(710,212)	(31,937)	4.5%	(688,486)	(21,726)	3.2%
Construction in progress	79,032	39,922	39,110	98.0%	62,068	(22,146)	-35.7%
Capital assets - net	\$ 526,484	\$ 492,450	\$ 34,034	6.9%	\$ 466,296	\$ 26,154	5.6%

Harris Health continuously assesses its facilities, equipment and technology to determine the priorities for replacement, repair and any new acquisitions. The assessment and prioritization methodology addresses patient safety, building and code compliance requirements, planned equipment obsolescence, and new technology. Given the current demand for major infrastructure improvement and modernization, along with planned facilities renovation and construction, Harris Health will invest \$176 million in capital projects in fiscal 2022. The System's average age of plant stands at almost 13 years compared to the industry standard of ten years, which calls for acceleration of capital investment ahead of the schedule. Harris Health's capital program structure, lack of additional debt plans, and solid balance sheet also inform and support this recommendation.

As a result, the System's overall capital budget for fiscal 2022 includes a \$131 million investment in renovations of current facilities, \$21 million in information technology, and \$18 million in medical equipment.

On April 7, 2020, the System issued the combination tax and revenue Certificates of Obligation, Series 2020 (the Series 2020 certificates of obligation) in the amount of \$36 million (inclusive of a \$5 million premium) to fund the construction and equipping of certain facilities at Ben Taub Hospital and the purchase and installation of certain medical equipment in Harris County's jail facilities as well as the

purchase and installation of an upgraded electronic medical record system, among other facility improvements. The Series 2020 certificates of obligation mature in various amounts annually starting February 15, 2021 through February 15, 2030, with a stated coupon rate of 5.0 percent and are collateralized by the levy of ad valorem tax revenue and a lien on and pledge of surplus revenues.

At February 28, 2021 and February 29, 2020, the System had \$226 million and \$233 million, respectively, in outstanding revenue bonds. Moody's has an underlying rating of Aa1, Fitch of AA, and Standard and Poor's has a rating of AA- on the revenue bond obligations. The debt is scheduled to be repaid in 2042. The debt is issued in the name of the Harris County Hospital District. Any issuance of debt requires the approval of the System's Board of Trustees and the Harris County Commissioners' Court.

An interest rate swap and derivative liability are associated with the Series 2010 refunding and revenue bonds. The fair value of the interest rate swap was reported as a derivative liability of \$16 million and \$19 million at February 28, 2021 and February 29, 2020, respectively. An off-market element associated with the swap is reported as a borrowing payable in the amount of \$9 million at February 28, 2021 and February 29, 2020.

Table 4 below summarizes the System's debt obligations at February 28, 2021, February 29, 2020 and February 28, 2019:

Table 4
Long-Term Debt Obligations
(In thousands)

	2021	2020	2019
Series 2010 revenue bonds	\$ 82,525	\$ 84,975	\$ 87,325
Series 2016 revenue bonds	154,841	159,786	164,559
Series 2016 certificates of obligation	57,621	60,631	63,551
Series 2020 certificates of obligation	33,470	-	-
Other	48	98	174
Total long-term debt and other long-term obligations	328,505	305,490	315,609
Less current portion	(11,958)	(8,930)	(8,546)
Noncurrent portion	\$ 316,547	\$ 296,560	\$ 307,063

Economic Conditions and Plan for Fiscal 2022

The approved fiscal 2022 operating and capital budget represent Harris Health's unwavering commitment to patient safety and advancement in the health status of the residents of Harris County. The budget reflects Harris Health's essential status within the overall healthcare market of Harris County and underscores the strength of its operations and financial stability despite the ongoing COVID-19 pandemic and other economic challenges. The planned 2.0 percent operating margin of \$38 million will allow the System to continue with its infrastructure modernization and delivery of high-quality healthcare to Harris County residents. Management projects a stable cash flow performance for fiscal 2022 and maintenance of the required days cash on hand under the System's revenue bond covenants.

Contacting the System's Financial Management

This financial report is designed to provide taxpayers, creditors and patients with a general overview of the Harris Health System's finances and to demonstrate the System's accountability for funds it receives. The report is available at <https://www.harrishealth.org>. If you have questions about this report or need further financial information, contact the Harris Health System, 4800 Fourance Place, Bellaire, Texas 77401, Attention: Michael Norby, Executive Vice President and Chief Financial Officer (Michael.Norby@harrishealth.org).

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**
Statements of Net Position
February 28, 2021 and February 29, 2020
(In thousands)

	2021				2020			
	Component Units				Component Units			
	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.
Assets and Deferred Outflows of Resources								
Current Assets								
Cash and cash equivalents	\$ 990,615	\$ 171	\$ 76,528	\$ 310,313	\$ 331,524	\$ 107	\$ 47,713	\$ 138,389
Short-term investments	99,969	-	-	20,783	574,041	-	25,341	25,637
Accounts receivable – net of allowance for uncollectible accounts of \$48,789 and \$51,835	114,312	-	-	-	77,348	-	-	-
Current portion of ad valorem taxes receivable – net of allowance for uncollectible taxes of \$6,307 and \$7,826	33,449	-	-	-	32,872	-	-	-
Inventories	13,356	-	-	-	10,296	-	-	-
Medicaid supplemental programs receivable	202,278	-	-	-	44,171	-	-	-
Prepaid expenses and other current assets	18,270	2,497	145,431	36,979	20,970	1,298	111,754	32,530
Estimated third-party payor settlements	48,606	-	-	-	35,284	-	-	-
Due from Community Health Choice, Inc.	24,402	-	-	386	13,161	-	-	-
Due from Community Health Choice Texas, Inc.	-	-	-	-	-	-	5,884	-
Restricted cash and cash equivalents - Local Provider Participation Fund	54,279	-	-	-	35,894	-	-	-
Current portion of assets limited as to use or restricted	7,050	-	-	-	6,834	-	-	-
Total current assets	<u>1,606,586</u>	<u>2,668</u>	<u>221,959</u>	<u>368,461</u>	<u>1,182,395</u>	<u>1,405</u>	<u>190,692</u>	<u>196,556</u>
Assets Limited as to Use or Restricted – Net of Current Portion								
Debt service	25,604	-	-	-	25,627	-	-	-
BT level I trauma	-	-	-	-	7,895	-	-	-
Series 2020 capital asset fund	20,500	-	-	-	-	-	-	-
Cash on deposit with county - project management	10	-	-	-	21,736	-	-	-
Other	923	71,838	3,325	600	924	52,468	3,425	600
Total assets limited as to use or restricted – net	<u>47,037</u>	<u>71,838</u>	<u>3,325</u>	<u>600</u>	<u>56,182</u>	<u>52,468</u>	<u>3,425</u>	<u>600</u>

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**
Statements of Net Position (Continued)
February 28, 2021 and February 29, 2020
(In thousands)

	2021				2020			
	Component Units				Component Units			
	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.
Assets and Deferred Outflows of Resources (Continued)								
Capital Assets								
Land and improvements	\$ 46,829	\$ -	\$ -	\$ -	\$ 46,180	\$ -	\$ -	\$ -
Buildings and fixed equipment	722,584	-	-	-	706,083	-	-	-
Major movable equipment	420,188	-	-	-	410,477	-	-	-
Less accumulated depreciation	(742,149)	-	-	-	(710,212)	-	-	-
Total depreciable capital assets – net	447,452	-	-	-	452,528	-	-	-
Construction in progress	79,032	-	-	-	39,922	-	-	-
Capital assets – net	526,484	-	-	-	492,450	-	-	-
Other Assets								
Ad valorem taxes receivable – net of current portion and allowance for uncollectible taxes of \$40,105 and \$34,195	1,748	-	-	-	268	-	-	-
Long-term investments	-	-	-	13,018	-	-	-	9,698
Other assets	4,849	6,034	-	-	4,660	9,395	-	-
Total other assets	6,597	6,034	-	13,018	4,928	9,395	-	9,698
Total assets	2,186,704	80,540	225,284	382,079	1,735,955	63,268	194,117	206,854
Deferred Outflows of Resources								
Derivative financial instrument	15,861	-	-	-	19,115	-	-	-
Resources related to pension	37,651	-	-	-	25,659	-	-	-
Resources related to OPEB	125,818	-	-	-	53,026	-	-	-
Loss on refunding revenue bonds	8,213	-	-	-	8,891	-	-	-
Total deferred outflows of resources	187,543	-	-	-	106,691	-	-	-
Total assets and deferred outflows of resources	\$ 2,374,247	\$ 80,540	\$ 225,284	\$ 382,079	\$ 1,842,646	\$ 63,268	\$ 194,117	\$ 206,854

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas
Statements of Net Position (Continued)
February 28, 2021 and February 29, 2020
(In thousands)**

Liabilities, Deferred Inflows of Resources and Net Position	2021				2020			
	Component Units				Component Units			
	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.
Current Liabilities								
Accounts payable and accrued liabilities	\$ 111,934	\$ 396	\$ 26,050	\$ 18,701	\$ 109,104	\$ 50	\$ 20,840	\$ 14,959
Interest payable	393	-	-	-	472	-	-	-
Employee compensation and related benefit liabilities	55,365	-	-	-	46,788	-	-	-
Postemployment health benefit liability	16,430	-	-	-	16,423	-	-	-
Compensated absences	46,816	-	-	-	46,902	-	-	-
Medicaid supplemental programs revenue received in advance	1,875	-	-	-	1,367	-	-	-
Intergovernmental transfer obligation	62,305	-	-	-	35,894	-	-	-
Medical claims liability	-	-	59,666	148,740	-	-	70,965	95,736
Liabilities related to the Affordable Care Act	-	-	26,791	-	-	-	15,870	-
Provider Relief Funds received in advance	55,771	-	-	-	-	-	-	-
Due to Harris Health System	-	-	15,207	-	-	-	13,785	-
Due to Community Health Choice Texas, Inc.	-	-	386	-	-	-	-	-
Due to Community Health Choice, Inc.	-	-	-	-	-	-	-	5,884
Estimated third-party payor settlements	8,570	-	-	-	9,644	-	-	-
Current portion of long-term debt and capital leases	11,958	-	-	-	8,930	-	-	-
Total current liabilities	371,417	396	128,100	167,441	275,524	50	121,460	116,579
Other Long-Term Liabilities								
Postemployment health benefit liability	572,176	-	-	-	470,007	-	-	-
Net pension liability	162,134	-	-	-	224,938	-	-	-
Borrowing payable	8,879	-	-	-	9,612	-	-	-
Derivative liability	15,861	-	-	-	19,115	-	-	-
Other	-	-	-	-	32	-	-	-
Long-Term Debt								
Series 2010 refunding revenue bonds	79,975	-	-	-	82,525	-	-	-
Series 2016 refunding revenue bonds - including premium of \$11,246 and \$12,171	150,626	-	-	-	155,766	-	-	-
Series 2016 certificates of obligation - including premium of \$5,026 and \$5,626	55,091	-	-	-	58,221	-	-	-
Series 2020 certificates of obligation - including premium of \$4,525 and \$0	30,845	-	-	-	-	-	-	-
Other long-term obligations – capital leases	10	-	-	-	48	-	-	-
Total liabilities	1,447,014	396	128,100	167,441	1,295,788	50	121,460	116,579

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**
Statements of Net Position (Continued)
February 28, 2021 and February 29, 2020
(In thousands)

Liabilities, Deferred Inflows of Resources and Net Position (Continued)	2021				2020			
	Component Units				Component Units			
	Community			Community	Community			Community
	Harris Health System	Foundation	Health Choice, Inc.	Choice Texas, Inc.	Harris Health System	Foundation	Health Choice, Inc.	Choice Texas, Inc.
Deferred Inflows of Resources								
Resources related to pension	\$ 89,893	\$ -	\$ -	\$ -	\$ 30,310	\$ -	\$ -	\$ -
Resources related to OPEB	22,549	-	-	-	25,003	-	-	-
Total deferred inflows of resources	112,442	-	-	-	55,313	-	-	-
Commitments and Contingencies								
Net Position								
Net investment in capital assets	204,352	-	-	-	173,532	-	-	-
Restricted for debt service	32,654	-	-	-	32,461	-	-	-
Restricted – other	923	36,166	3,325	600	924	33,425	3,425	600
Unrestricted	576,862	43,978	93,859	214,038	284,628	29,793	69,232	89,675
Total net position	814,791	80,144	97,184	214,638	491,545	63,218	72,657	90,275
Total liabilities, deferred inflows of resources and net position	\$ 2,374,247	\$ 80,540	\$ 225,284	\$ 382,079	\$ 1,842,646	\$ 63,268	\$ 194,117	\$ 206,854

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**
Statements of Revenues, Expenses and Changes in Net Position
Years Ended February 28, 2021 and February 29, 2020
(In thousands)

	2021				2020			
	Component Units				Component Units			
	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.	Harris Health System	Foundation	Community Health Choice, Inc.	Community Health Choice Texas, Inc.
Operating Revenues								
Net patient service revenue	\$ 695,234	\$ -	\$ -	\$ -	\$ 591,357	\$ -	\$ -	\$ -
Medicaid supplemental programs revenue	563,923	-	-	-	290,557	-	-	-
Premium revenue	-	-	705,567	1,232,364	-	-	745,403	976,421
Other operating revenues	34,168	2,863	383	-	32,938	4,977	981	-
Total operating revenues	1,293,325	2,863	705,950	1,232,364	914,852	4,977	746,384	976,421
Operating Expenses								
Salaries, wages, and benefits	894,277	486	17,994	58,330	838,483	535	40,649	29,267
Pharmaceuticals and supplies	232,998	1	2,404	8,441	216,809	24	5,567	3,864
Physician services	341,214	-	-	-	285,926	-	-	-
Medical claims expense	-	-	619,886	971,297	-	-	608,893	921,691
Other purchased services	252,641	5,004	56,339	55,681	213,704	3,251	65,805	42,390
Depreciation and amortization	59,751	-	-	-	54,650	-	-	-
Total operating expenses	1,780,881	5,491	696,623	1,093,749	1,609,572	3,810	720,914	997,212
Operating Income (Loss)	(487,556)	(2,628)	9,327	138,615	(694,720)	1,167	25,470	(20,791)
Nonoperating Revenues (Expenses)								
Ad valorem tax revenues – net	780,713	-	-	-	767,515	-	-	-
Tobacco settlement revenues	12,924	-	-	-	13,797	-	-	-
Investment income	4,434	19,846	200	748	15,089	6,067	2,006	3,146
Interest expense	(10,920)	-	-	-	(10,866)	-	-	-
Provider Relief Fund revenue	22,134	-	-	-	-	-	-	-
Other, net	1,517	(292)	-	-	(604)	(285)	-	-
Total nonoperating revenues (expenses) – net	810,802	19,554	200	748	784,931	5,782	2,006	3,146
Changes in net position	323,246	16,926	9,527	139,363	90,211	6,949	27,476	(17,645)
Net Position – Beginning of Year	491,545	63,218	72,657	90,275	401,334	56,269	63,181	89,920
Net Position Transfer of Surplus	-	-	15,000	(15,000)	-	-	(18,000)	18,000
Net Position – End of Year	\$ 814,791	\$ 80,144	\$ 97,184	\$ 214,638	\$ 491,545	\$ 63,218	\$ 72,657	\$ 90,275

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**

Statements of Cash Flows

Years Ended February 28, 2021 and February 29, 2020
(In thousands)

	2021	2020
	Harris Health System	Harris Health System
Operating Activities		
Receipts from and on behalf of patients	\$ 642,108	\$ 593,472
Receipts from Medicaid supplemental programs	406,324	281,283
Receipts from incentive programs and grants	13,802	11,135
Receipts from other revenues	17,375	17,083
Payments to suppliers	(821,047)	(677,753)
Payments to employees and for employee benefits	(879,960)	(789,758)
Net cash used in operating activities	<u>(621,398)</u>	<u>(564,538)</u>
Noncapital Financing Activities		
Contributions and other – net	1,998	584
Ad valorem taxes – net	773,954	760,940
Receipt of Provider Relief Funds	77,905	-
Interest paid	(869)	-
Proceeds from issuance of long-term debt	29,804	-
Repayment of long-term debt	(1,517)	-
Tobacco settlement revenues	12,924	13,797
Net cash provided by noncapital financing activities	<u>894,199</u>	<u>775,321</u>
Capital and Related Financing Activities		
Receipt of property taxes for debt service	4,690	4,626
Acquisitions and construction of capital assets	(70,469)	(60,668)
Project management - cash on deposit with Harris County	-	(1,309)
Interest paid	(12,172)	(12,536)
Proceeds from issuance of long-term debt	6,196	-
Repayment of long-term debt	(9,513)	(8,545)
Net cash used in capital and related financing activities	<u>(81,268)</u>	<u>(78,432)</u>
Investing Activities		
Receipts of investment income – including realized gains and losses	5,542	11,834
Increase in cash equivalents included in assets limited as to use or restricted	9,455	38,957
Other investing activities	-	(2,190)
Purchases of investment securities	(167,611)	(737,701)
Proceeds from sale and maturities of investment securities	620,172	544,751
Net cash provided by (used in) investing activities	<u>467,558</u>	<u>(144,349)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	659,091	(11,998)
Cash and Cash Equivalents - Beginning of Year	331,524	343,522
Cash and Cash Equivalents - End of Year	<u>\$ 990,615</u>	<u>\$ 331,524</u>

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas
Statements of Cash Flows (Continued)
Years Ended February 28, 2021 and February 29, 2020
(In thousands)**

	<u>2021</u>	<u>2020</u>
	<u>Harris Health</u>	<u>Harris Health</u>
	<u>System</u>	<u>System</u>
Reconciliation of Operating Loss to Net Cash Used in Operating Activities		
Operating loss	\$ (487,556)	\$ (694,720)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization	59,751	54,650
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable	(36,964)	1,466
Increase in inventories	(3,060)	(2,305)
Increase in Medicaid supplemental program receivable	(158,107)	(8,903)
Decrease (increase) in prepaid expenses and other assets	(10,410)	4,743
Increase in estimated third-party payor settlements	(13,322)	(5,463)
Increase in accounts payable and accrued liabilities	8,628	33,418
Decrease in net pension liability	(62,804)	(54,962)
Increase in employee compensation and related benefit liabilities	8,577	13,963
Increase (decrease) in compensated absences	(86)	11,653
Increase (decrease) in Medicaid supplemental programs revenue received in advance	508	(371)
Increase (decrease) in estimated third-party payor settlements	(1,074)	3,434
Increase in postemployment health benefit liability	102,176	42,109
Increase in deferred inflows of resources - pension	59,583	30,310
Decrease (increase) in deferred outflows of resources - pension	(11,992)	34,463
(Decrease) increase in deferred inflows of resources - OPEB	(2,454)	25,003
Increase in deferred outflows of resources - OPEB	(72,792)	(53,026)
	<u>(133,842)</u>	<u>130,182</u>
Total adjustments		
Net cash used in operating activities	<u>\$ (621,398)</u>	<u>\$ (564,538)</u>
Supplemental Disclosures of Noncash Operating, Financing and Investing Activities		
Unrealized gain (loss) on investments	\$ (4,331)	\$ 2,232
Amounts related to acquisition of capital assets in accounts payable and accrued liabilities	22,830	20,602
Inkind contributions received	1,884	-

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**

**Notes to Financial Statements
February 28, 2021 and February 29, 2020**

Note 1: Organization and Mission

Harris County Hospital District, d/b/a Harris Health System, (the System), a component unit of Harris County, Texas, was created by authorization of the legislature of the State of Texas and subsequent approval by the voters of Harris County, Texas, in November 1965. The System provides patient care to the indigent population of Harris County and receives property taxes levied by Harris County for the provision of this care. The System operates two acute care hospitals and a psychiatric unit, with a total of 617 licensed beds. The System also operates 18 primary care health clinics including the nation's first free-standing HIV/AIDS treatment center; three large multi-specialty clinics; five same day clinics; five school-based clinics; a free-standing dental center; a dialysis center; a geriatric assessment center; ten homeless shelter clinics; and a mobile immunization and medical outreach program. The System is exempt from federal income taxes.

The System is a component unit of Harris County, Texas (legally separate from Harris County, Texas) since the members of the System's governing board are appointed by the Harris County Commissioners' Court. The Harris County Commissioners' Court approves the System's tax rate and annual operating and capital budget. Harris County, Texas does not provide any funding to the System, hold title to any of the System's assets or have any rights to any surpluses of the System.

The System's primary mission is to provide quality preventive, medical, hospital and emergency care to the indigent and needy of Harris County and to others with the ability to pay. All activities conducted by the System are directly associated with the furtherance of this mission and are, therefore, considered to be operating activities.

The Harris County Hospital District Foundation (the Foundation), was organized in 1993. The Foundation is a nonprofit, tax-exempt corporation organized under Section 501(c)(3) of the Internal Revenue Code whose primary purpose is to raise funds to support the operations and activities of the System. Although the System does not control the timing or amount of receipts from the Foundation, the majority of resources (or income thereon) that the Foundation holds and invests is restricted to the activities of the System by the donor. Because these restricted resources held by the Foundation can only be used by, or for the benefit of, the System, the Foundation is considered a component unit of the System and is included in the System's financial statements. The Foundation is reported as a discretely presented component unit of the System. Financial reports for the Foundation can be obtained from the Harris County Hospital District Foundation, 4800 Fournace Place, Bellaire, Texas 77401. Attention: Jeffrey Baker, Executive Director (Jeffrey.Baker@harrishealth.org).

Community Health Choice, Inc. and Community Health Choice Texas, Inc. (the HMOs) are Texas not-for-profit corporations organized under Section 501(c)(4) of the Internal Revenue Code to operate as health maintenance organizations. Community Health Choice, Inc. was incorporated on May 8, 1996, licensed by the Texas Department of Insurance on February 14, 1997, and as of December 31, 2020, offered three Medicaid insurance products as well as individual health insurance on the Health Insurance Marketplace. Community Health Choice Texas, Inc. was formed in August 2016 to allow the Health Insurance Marketplace and the Medicaid insurance

**Harris County Hospital District,
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**Notes to Financial Statements
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products to be provided and served by separate corporations. Community Health Choice, Inc. is the Health Insurance Marketplace and commercial HMO with 94,372 and 83,163 enrollees as of December 31, 2020 and 2019, respectively, and Community Health Choice Texas, Inc. is the Medicaid Managed Care HMO with 328,757 and 272,558 enrollees as of December 31, 2020 and 2019, respectively. The HMOs are reported as discretely presented component units of the System since the Board of Directors are appointed by the System's Board of Trustees and the System can impose its will on the HMOs. The differences in amounts due to the System and due from the HMOs in the accompanying statements of net position are primarily due to the presentation of the HMOs financials based on their fiscal year-end of December 31. Financial reports for the HMOs can be obtained from Community Health Choice, Inc., 2636 South Loop West, Ste. 125, Houston, Texas 77054, Attention: Mark Van Elden, Executive Vice President and Chief Financial Officer (Mark.VanElden@CommunityHealthChoice.org).

Unless otherwise noted, the following notes do not include the Foundation or the HMOs.

Note 2: Summary of Significant Accounting Policies

Basis of Accounting

The accompanying financial statements are prepared on the accrual basis of accounting.

Method of Accounting

Under the provisions of the American Institute of Certified Public Accountants' *Audit and Accounting Guide, Health Care Organizations*, the System is considered a governmental organization and is subject to the pronouncements of the Governmental Accounting Standards Board (GASB).

In accordance with GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, the System's financial statements include the statements of net position; statements of revenues, expenses and changes in net position; and statements of cash flows.

The statement of net position requires that total net position be reported in three components (a) net investment in capital assets, (b) restricted; and (c) unrestricted.

- "Net investment in capital assets" consists of capital assets, net of accumulated depreciation, reduced by the amount outstanding for any bonds, notes, or other financing liabilities that were incurred related to the acquisition, construction or improvement of the capital assets.
- "Restricted" consists of restricted assets reduced by liabilities and deferred inflows of resources related to the assets and are primarily for debt service.

**Harris County Hospital District,
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**Notes to Financial Statements
February 28, 2021 and February 29, 2020**

- "Unrestricted" is the net amount of the assets, deferred outflows of resources, liabilities and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

When an expense is incurred for purposes for which there are both restricted and unrestricted net position available, it is the System's practice to apply that expense to restricted net position to the extent such are available and then to unrestricted.

The Foundation is a private not-for-profit organization that reports under Financial Accounting Standards Board pronouncements. As such, certain revenue recognition criteria and presentation features are different from that of the GASB. The Foundation's financial statement formats were modified to make them compatible with the System's financial statement formats.

The HMOs are licensed only in the state of Texas and report under Governmental Accounting Standards Board pronouncements. The HMOs' financial statement formats were modified to make them compatible with the System's financial statement formats.

Reporting Entity

The financial statements include the accounts of the System, the Foundation and the HMOs, as described in *Note 1*. In accordance with GASB Statement No. 61, *The Financial Reporting Entity: Omnibus – An Amendment of GASB Statements Nos. 14 and 34*, the System reports the HMOs and the Foundation as discretely presented component units in its financial statements. Management of the System believes the separate presentation of the System's statements and of each discretely presented component unit to be the most reflective of the System's activities.

Transactions between the System and its component units include the following:

The System provides certain administrative services to the HMOs including employment of all individuals who perform the day-to-day requirements of the business functions of the HMOs. The HMOs reimburse the System for such salaries, wages and benefits and these costs are reflected as expenses of the HMOs. An additional fee for indirect costs approximating \$3 million for fiscal years 2021 and 2020 is included as a revenue and expense in the System/HMO financial statements. The System pays a portion of the premiums for enrollees to Community Health Choice, Inc. for insurance coverage under the insurance plans that are offered as part of the HMO's mission. Premiums paid on behalf of enrollees were \$36 million and \$22 million for fiscal years 2021 and 2020, respectively, which is included as expense and revenue in the System/Community Health Choice, Inc. financial statements.

The System supports the Foundation with payments for goods and services of approximately \$544 thousand and \$574 thousand in fiscal years 2021 and 2020, respectively, which are recognized in the Foundation financial data as in-kind contributions and expenses. The Foundation provided support to the System for projects and grants of \$2 million for fiscal years 2021 and 2020. In addition, the Foundation distributed to the System contributions totaling \$2 million and \$500 thousand in 2021 and 2020, respectively, from its multi-year Capital Campaign funds.

**Harris County Hospital District,
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**Notes to Financial Statements
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Cash, Cash Equivalents and Short-term Investments

Cash and cash equivalents include cash and investments that are highly liquid with maturities of less than three months when purchased, and excludes cash and cash equivalents that are restricted or limited as to use. Short-term investments are investments with maturities in excess of three months, but less than a year, when purchased.

The System's and HMO's cash, cash equivalents and short-term investments are invested in fully collateralized time deposits, commercial paper, money market mutual funds and government securities as authorized by Chapter 281 of the *Texas Health and Safety Codes* and Chapter 116 of the *Texas Local Government Code*, except as disclosed in *Note 6*. Such total collateralization and insurance coverage is required by the Board of Trustees of the System. The Foundation's investments, however, are not subject to these laws.

Investments are reported at fair value, with realized and unrealized gains and losses included in investment income in the statements of revenues, expenses and changes in net position.

Foundation Net Position

Gifts of cash and other assets received without donor stipulations are reported as unrestricted revenue and net position. Gifts received with a donor stipulation that limits their use are reported as restricted net position. When a donor stipulated time restriction ends or purpose restriction is accomplished, restricted net position is reclassified to unrestricted net position. The majority of pledges recorded are externally imposed to the System's expansion projects. Pledges are included in other assets in the statements of net position.

Inventories

Inventories are valued at the lower of cost, using the first-in, first-out method, or market and consist principally of pharmaceuticals.

Capital Assets

Property, plant and equipment are carried at cost or acquisition value at the time of donation and include expenditures for new facilities and equipment and expenditures that substantially increase the useful life of existing capital assets. Ordinary maintenance and repairs are charged to expense when incurred. Capitalization is limited to assets with a cost of \$5,000 or greater.

Disposals are removed at carrying cost less accumulated depreciation, with any resulting gain or loss included in other nonoperating revenue and expenses. Depreciation is recorded on the straight-line method over the estimated useful lives of the assets. Estimated useful lives for buildings are up to 40 years and for equipment are 2 to 25 years. Equipment under capital leases is amortized on the straight-line method over the lesser of the useful life of the equipment or the lease term. Such amortization is included in depreciation and amortization in the accompanying statements of revenues, expenses and changes in net position.

**Harris County Hospital District,
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**Notes to Financial Statements
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Capital Asset Impairment

The System evaluates capital assets for impairment whenever events or circumstances indicate a significant, unexpected decline in the service utility of a capital asset has occurred. If a capital asset is tested for impairment and the magnitude of the decline in service utility is significant and unexpected, either accumulated depreciation is increased by the amount of the impairment loss. No material asset impairment was recognized during the years ended February 28, 2021 and February 29, 2020.

Risk Management

The System is exposed to various risks of loss from torts; theft of, damage to and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; medical malpractice; and employee health, dental and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters other than medical malpractice and employee health claims. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

The System is self-insured for a portion of its exposure to risk of loss from medical malpractice and employee health claims. Annual estimated provisions are accrued for the self-insured portion of medical malpractice and employee health claims and include an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

Compensated Absences

The System maintains a paid time-off plan. Under the paid time-off plan, the cost of all compensated absences is accrued at the time the benefits are earned. At the option of the employee, unused benefits may be liquidated at 50.0 percent or at the time of termination, unused benefits are payable at 75.0 percent. Changes in the System's liability for compensated absences in fiscal years 2021 and 2020 are as follows (in thousands).

Fiscal	Beginning of Year Liability	Current Year Claims and Change in Estimates	Claim Payments	End of Year Liability
2021	\$ 46,902	\$ 75,134	\$ 75,220	\$ 46,816
2020	35,249	78,820	67,167	46,902

Classification of Revenues and Expenses

Operating revenues include those generated from direct patient care and related support services. Nonoperating revenues consist of those revenues that are related to financing and investing types of activities and result from nonexchange transactions or investment income. Operating expenses include those related to direct patient care and related support services. Nonoperating expenses include interest expense and other expenses that are not considered operating.

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Net Patient Service Revenue and Accounts Receivable

Net patient service revenue is reported as the estimated net realized amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive revenue adjustments under reimbursement agreements with third-party payors. In recognizing net patient service revenue, estimates are used in recording allowances for contractual adjustments and uncollectible accounts. Allowances for uncollectible accounts are estimated using historical experience, current trend information, aged account balances and a collectability analysis. The System's financial assistance program for uninsured patients classified as self-pay determines expected payments based on the Medicare allowable reimbursement. Charges in excess of the expected payment are reflected as an administrative uninsured discount. The allowance for uncollectible accounts was estimated at \$49 million and \$52 million as of February 28, 2021 and February 29, 2020, respectively. The System provides services under contract to patients covered under the Medicare and Medicaid programs. Net revenues from these programs are included in patient service revenue at estimated reimbursement based on customary billing charges, predetermined rates of reimbursement, plus certain adjustments. The amounts due to or from these programs are subject to final review and settlement by the program administrative contractor. Retroactive adjustments under third-party reimbursement agreements are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. As a result, it is reasonably possible that these estimates could differ from actual settlements and thus change in the near term by material amounts.

Charity Care Policy

The System accepts all Harris County residents as patients regardless of their ability to pay. Harris County residents may qualify for partial financial assistance, on a sliding scale. The extent to which a resident will be financially responsible is determined based upon pre-established financial criteria, which utilize family income and size as it relates to the federal poverty guidelines set by the U.S. Department of Health and Human Services. Charity services are defined as those services for which no payment is anticipated. These amounts are not reported as revenue. The System maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges foregone for services and supplies furnished under the System's Financial Assistance program. The cost of charity care is estimated by applying the ratio of cost to gross charges to the gross charity care charges. The following information measures the level of charity care provided during the years ended February 28, 2021 and February 29, 2020 (in thousands):

	2021	2020
Charges foregone, based on established rates	\$ 904,580	\$ 1,240,562
Cost of foregone charges, estimated	720,268	720,390

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Premium Revenue

Premium revenue is recognized as revenue by the HMOs during the coverage period of the subscriber agreement. For the primary Medicaid business, notification is received throughout the year of any new, removed or revised members and the date of eligibility for coverage. The date of notification may be subsequent to the date of eligibility. The HMOs believe premium revenue has been appropriately recognized for the years ended December 31, 2020 and 2019.

Medical Claims Expense

The HMOs arrange for comprehensive health care services to its members primarily through fee-for-service arrangements. The HMOs compensate hospitals on either a discounted fee for service or per diem basis and compensates physicians and other providers primarily on a discounted fee for service basis.

Medical claims expense reserves represent the estimated ultimate net cost of all reported and unreported losses incurred through the end of December and are presented on a discounted basis. The reserves for unpaid medical claims expenses are actuarially estimated based on claims experience and statistical analyses. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes the reserves for medical claims expenses are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations.

Contracts are evaluated to determine if it is probable that a loss will be incurred and a premium deficiency reserve is recognized when it is probable that expected future claims, including maintenance costs, will exceed existing reserves plus anticipated future premiums and reinsurance recoveries, without consideration of anticipated investment income. For purposes of determining premium deficiency reserves, contracts are grouped in a manner consistent with the method of acquiring, servicing and measuring the profitability of such contracts. As of December 31, 2020, the HMOs recognized no premium deficiency reserve for the Health Insurance Marketplace business. As of December 31, 2019, the HMOs recognized a \$1 million premium deficiency reserve for the Health Insurance Marketplace business.

Changes in the HMO's aggregate liability for medical claims in fiscal years 2021 and 2020 are as follows (in thousands):

Fiscal Year	Beginning of Fiscal Liability	Medical Claims and Change in Estimates	Claim Payments	End of Fiscal Year Liability
2021	\$ 166,701	\$ 1,598,373	\$ 1,556,668	\$ 208,406
2020	149,949	1,536,232	1,519,480	166,701

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In fiscal year 2021, the HMOs in aggregate paid \$1,395 million in claims related to the current fiscal year and \$162 million in claims related to the prior fiscal year. In fiscal year 2020, the HMOs paid \$1,377 million in claims related to the current fiscal year and \$142 million in claims related to the prior fiscal year.

The HMOs are a party to a reinsurance agreement to limit its losses on individual claims. Under the terms of the agreement, the reinsurer reimburses the HMOs approximately 90.0 percent, subject to certain limitations as specified in the contract, of the cost of each member's annual inpatient hospital services. For the Medicaid and Children's Health Insurance Program (CHIP) business, the recovery is based on costs in excess of a \$1 million deductible, up to a limitation of \$5 million per member per agreement period. The HMOs also carry coverage for the health insurance marketplace business for which the reinsurer reimburses approximately 90.0 percent of each member's annual inpatient hospital services in excess of a \$750 thousand deductible, up to a limitation of \$5 million per member per agreement period.

Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (ACA)

The HMOs participate in the federally facilitated health insurance exchange in 10 southeast Texas counties. The exchange was created pursuant to the ACA under regulations established by the U.S. Department of Health and Human Services (HHS). Under these rules, HHS pays the HMO a portion of the policy premium, in the form of Advanced Premium Tax Credit (APTC), and part of the health care costs, in the form of Cost Sharing Reduction (CSR), for low income individual exchange members. HHS also administers certain risk management programs as detailed below.

The HMOs recognize premiums received from its exchange members and APTC received from HHS as premium revenue when earned and CSR offsets health care costs when incurred. For 2021, the HMOs recognized \$438 million and \$0 of APTC and CSR, respectively. For 2020, the HMOs recognized \$427 million and \$0 of APTC and CSR, respectively.

The risk adjustment data validation program was implemented to ensure the integrity and accuracy of risk adjustment transfer amounts. Prior year submission data is audited and adjustments to the receivable or payable transfer amounts are made. Subject to this program, the HMOs have recorded a liability of approximately \$27 million and \$16 million, at December 31, 2020 and 2019, respectively, which is included as liabilities related to the Affordable Care Act within current liabilities in the accompanying statements of net position.

The ACA established a permanent risk adjustment program which adjusts the premiums that commercial, individual and small group health insurance issuers receive based on the demographic factors and health status of each member as derived from current year medical diagnosis as reported throughout the year. This program transfers funds from lower risk plans to higher risk plans with similar plans in the same state. The risk adjustment program is applicable to commercial, individual and small group health plans (except certain exempt and grandfathered plans) operating both inside and outside of the exchange. A risk score is determined for the entire subject population for each market in each state. Plans with an average risk score below the state average will pay into a pool and health insurance issuers with an average risk score that is greater

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than the state average risk score will receive money from that pool. The HMOs issues individual plans and is therefore subject to the risk adjustment. At December 31, 2020 and 2019, the HMOs recorded a risk adjustment receivable of \$87 million and \$75 million, respectively, which is included in prepaid expenses and other current assets in the accompanying statements of net position.

Ad Valorem Tax Revenues – Net

Ad valorem tax revenues are recorded in the year for which the taxes are levied, net of provisions for uncollectible amounts, collection expenses and appraisal fees. Harris County Commissioners' Court levies a tax for the System as provided under state law. The taxes are collected by the Harris County Tax Assessor – Collector and are remitted to the System as received. On January 1, at the time of assessment, an enforceable lien is attached to the property for property taxes. Taxes are levied and become collectible from October 1 to January 31 of the succeeding year. Subsequent adjustments to the tax rolls, made by the County Assessor, are included in revenues in the period such adjustments are made by the County Assessor. Harris County also enters into property tax abatement agreements with local businesses under the state Property Redevelopment and *Tax Abatement Act*, Chapter 312, as well as its own guidelines and criteria, which is required under the Act.

Tobacco Settlement Revenues

In the fiscal years ended February 28, 2021 and February 29, 2020, the System received a portion of the funds from the settlement between various counties and hospital districts in Texas and the tobacco industry for tobacco-related health care costs. Under the program guidelines, the System is free to use the funds in either the immediate or future periods without restriction. The System recognizes all funds received from the settlement as nonoperating revenue in the period funds are allocated.

Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Plan and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by the Plan. For this purpose, benefits payments are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Postemployment Benefits Other Than Pensions

The System has a single-employer defined benefit other postemployment benefit (OPEB) plan. For purposes of measuring the net OPEB liability, deferred outflows and deferred inflows of resources related to OPEB, and OPEB expense have been determined on the same basis as they are reported by the OPEB plan. For this purpose, the System recognizes benefit payments when due and payable in accordance with the benefit terms.

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Use of Estimates

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

Newly Adopted Accounting Pronouncements

GASB released Statement 97, *Certain Component Unit Criteria, and Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, an amendment of GASB Statements No. 14 and 84, and a supersession of GASB Statement No. 32. Under GASB 97, Section 457 plans should be accounted for as either a pension plan or other employee benefit plan, if the plan meets the definition of a pension or an other employee benefit plan within GASB 67 or 73. Accounting and financial reporting requirements for 457 plans that meet the definition of a pension plan are defined in the Statement.

GASB 97 limits the applicability of the financial burden criterion in GASB 14 regarding contributions to postemployment benefit plans to only defined benefit pension plans and defined benefit OPEB plans that are administered through trusts meeting paragraph 3 criteria in GASB 67 or 74. The statement also changes how the absence of a governing board should be considered in determining whether a primary government is financially accountable for purposes of evaluating potential component units that are pension or OPEB plans. This supersedes certain previous guidance in Statement 84 and Implementation Guide 2019-2.

Adoption of this standard had no effect on the System's financial statements.

Pending Adoption of Recent Accounting Pronouncements

GASB Statement No. 87 - *Leases*. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It 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 requirements of this statement are effective for reporting periods beginning after June 15, 2021, with earlier application encouraged.

GASB Statement No. 91 – *Conduit Debt Obligations*. The primary objectives of this Statement are to provide a single method of reporting conduit debt obligations by issuers and eliminate diversity in practice associated with (1) commitments extended by issuers, (2) arrangements associated with conduit debt obligations, and (3) related note disclosures. This Statement achieves those objectives by clarifying the existing definition of a conduit debt obligation; establishing that a conduit debt obligation is not a liability of the issuer; establishing standards for accounting and financial reporting of additional commitments and voluntary commitments extended by issuers and arrangements associated with conduit debt obligations; and improving required note disclosures.

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The requirements of this Statement are effective for reporting periods beginning after December 15, 2021. Earlier application is encouraged.

GASB Statement No. 96 – *Subscription Based Information Technology Arrangement*. This Statement provides guidance on the accounting and financial reporting for subscription-based information technology arrangements (SBITAs) for government end users (governments). This Statement (1) defines a SBITA; (2) establishes that a SBITA results in a right-to-use subscription asset—an intangible asset—and a corresponding subscription liability; (3) provides the capitalization criteria for outlays other than subscription payments, including implementation costs of a SBITA; and (4) requires note disclosures regarding a SBITA. To the extent relevant, the standards for SBITAs are based on the standards established in Statement No. 87, *Leases*, as amended. The requirements of this Statement are effective for fiscal years beginning after June 15, 2022, and all reporting periods thereafter. Earlier application is encouraged.

Reclassifications

Certain reclassifications have been made to the 2020 financial statements to conform to the 2021 presentation. The reclassifications had no effect on the changes in financial position.

Note 3: Net Patient Service Revenue

The System has agreements with third-party payors that provide for payments to the System at amounts different from its established rates. The amounts by which the established billing rates exceed the amounts recoverable from these programs are written off and accounted for as contractual allowances. A summary of the payment arrangements with major third-party payors follows:

Medicare – Inpatient acute care services and defined capital costs related to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical diagnostic and other factors. Medicare outpatient services are reimbursed on fee schedules and on a prospective basis through ambulatory payment classifications, which are based on clinical resources used in performing the procedures. The System's Medicare cost reports have been audited by the Medicare administrative contractor through February 28, 2017.

Medicaid – Inpatient services rendered to Medicaid program beneficiaries are paid at prospectively determined rates per discharge similar to those of the Medicare inpatient program. Medicaid outpatient services are paid by fee schedules for specific services, including outpatient surgery, imaging and laboratory services. Other outpatient services are reimbursed on reasonable cost, based on a percentage from the System's most recent Medicaid cost report tentative settlement as of March 1, 2013. The System's Medicaid cost reports have been settled by the Medicaid administrative contractor through February 28, 2017.

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Cash received from the Medicare program accounted for approximately 54.6 percent and 54.3 percent of the System's total cash collections for net patient service revenue for years ended February 28, 2021 and February 29, 2020, respectively. Cash received from the Medicaid program (including managed Medicaid) accounted for approximately 17.7 percent and 26.2 percent of the System's total cash collections for net patient service revenue for the years ended February 28, 2021 and February 29, 2020, respectively.

Compliance with laws and regulations governing the Medicare and Medicaid programs can be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties and exclusion from the Medicare and Medicaid programs.

Note 4: Medicaid Supplemental Programs

The Disproportionate Share III (DSH) program was created in fiscal 1992 by the state of Texas to access additional federal matching funds. These funds are distributed to selected hospitals that provide services to low-income and uninsured patients.

The Upper Payment Limit (UPL) program was created in May 2002 with an effective date of July 2001. The UPL program used federal matching funds to raise state Medicaid reimbursement rates to 100.0 percent of equivalent Medicare rates for certain public hospital systems. In December 2011, Texas received federal approval to redirect the funding it would have received under the UPL program. The 1115 Waiver allows the state to expand Medicaid managed care, improve Medicaid services and reward performance. Federal funding that would have been received by hospitals if managed care was not expanded is to be preserved. The UPL program was replaced with two new pools of funding, the uncompensated care (UC) pool and the delivery system reform incentive payment (DSRIP) pool. The UC pool directs more funding to hospitals that serve large numbers of uninsured patients and the DSRIP pool provides incentive payments for health care providers based on improvements in quality of care. On January 15, 2021, the Centers for Medicare and Medicaid Services (CMS) approved an extension of the Waiver for an additional 10-year period through September 30, 2030. This extension ended the DSRIP pool effective September 30, 2021, made changes to other funding programs and created new funding programs to reflect CMS policy changes. On April 16, 2021, CMS rescinded the extension approval citing an improper exemption from the public notice and comment process originally granted. As of June 24, 2021, the Waiver is set to expire on September 30, 2022 and future funding from the Waiver programs described herein is uncertain. Funding for the DSRIP pool will end on September 30, 2021. The System also participates in three other Medical Supplemental Payment Programs, the Network Access Improvement Program (NAIP), the Uniform Hospital Rate Increase Program (UHRIP) and the new Graduate Medical Education (GME) program.

The System recognizes all funds received under the DSH, UC, DSRIP, NAIP, GME and UHRIP programs as operating revenues in the period applicable to the funds. Any amounts related to that year that are not received as of fiscal year-end are recorded as receivables and reflected in other current assets in the accompanying statements of net position. These receivables can be subject to adjustments that are reflected in the period they become known. The System recorded an

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unfavorable adjustment of \$6 million in fiscal year 2020 for prior years' programs. No material adjustments were recorded in fiscal year 2021 for prior years' programs. The System's financial statements reflect current liabilities for program revenue received but unearned of \$2 million and \$1 million at February 28, 2021 and February 29, 2020, respectively, and receivables of \$202 million and \$44 million at February 28, 2021 and February 29, 2020, respectively, related to the Medicaid Supplemental Programs. The rate increase for the System associated with UHRIP for the period March 1, 2019 through August 31, 2019, was 43.0 percent. The rate increase for the System for the periods from September 1, 2019 through August 31, 2020 and September 1, 2020 through February 28, 2021 was 70.0 percent.

During fiscal 2020, the System began participating in a Local Provider Participation Fund (LPPF) in Harris County. The System acts as the administrator of the LPPF by assessment and collection of mandatory payments from hospitals in Harris County. These payments are to be used to fund intergovernmental transfers representing the state's share of supplemental Medicaid funding programs. As the System acts as a conduit for these funds, the receipts and intergovernmental transfers are not recognized as revenue and expense in the statements of revenues, expenses and changes in net position. As of February 28, 2021, and February 29, 2020, the System held \$54 million and \$36 million in LPPF funds, respectively, which is reported as restricted cash in the statements of net position. At February 28, 2021, the System had \$62 million and \$36 million in intergovernmental transfer liability of which \$54 million and \$36 million related to LPPF and the residual related to intergovernmental transfers required for private providers.

Note 5: Assets Limited as to Use or Restricted

Assets limited as to use or restricted represent those assets whose use has been legally restricted related to the 2010 and 2016 refunding and revenue bond issues (50.0 percent of the greatest debt service requirement scheduled to occur); unspent bond proceeds; funds restricted by donors; or funds designated by the board for other uses. Investments in U.S. Treasury, agency and instrumentality obligations with a remaining maturity of one year or less at the time of acquisition and in non-negotiable certificates of deposit are carried at amortized cost.

The System also invests in Texas CLASS and Lone Star Investment pool (collectively, the investment pools), both of which are state investment pools that are considered investments for financial reporting. Investments must be in compliance with the *Texas Public Funds Investment Act* and include obligations of the United States or its agencies, direct obligation of the state of Texas or its agencies, certificates of deposit and repurchase agreements. The System has an undivided beneficial interest in the pool of assets held by the investment pools. The fair value of the position in these pools is the same as the value of the shares in each pool. Both investment pools are rated AAAM by Standard & Poor's. Investments in external investment pools qualifying for amortized cost under GASB Statement No. 79 - *Certain External Investment Pools and Pool Participants*, are carried at amortized cost per share.

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All other investments are recorded at fair value. The fair values of securities are based on appropriate valuation methodologies by third parties, quoted market prices and information available to management as of February 28, 2021 and February 29, 2020.

The components of assets limited as to use or restricted at fair value at February 28, 2021 and February 29, 2020, are as follows (in thousands):

Description of Assets	2021						
	Total	Restricted Debt Service	Series 2020 Capital Asset Fund	BT Level 1 Trauma	Cash on Deposit with Harris County Project Management	Restricted Cash and Cash Equivalents LPPF	Other
Money market government funds	\$ 26,158	\$ 1,816	\$ 13	\$ -	\$ -	\$ 24,278	\$ 51
U.S. Treasury notes	10,993	10,993	-	-	-	-	-
Investment pools	41,204	19,845	20,487	-	-	-	872
Cash	30,001	-	-	-	-	30,001	-
Other	10	-	-	-	10	-	-
	108,366	32,654	20,500	-	10	54,279	923
Less funds required for current liabilities	(61,329)	(7,050)	-	-	-	(54,279)	-
	\$ 47,037	\$ 25,604	\$ 20,500	\$ -	\$ 10	\$ -	\$ 923

Description of Assets	2020						
	Total	Restricted Debt Service	Series 2020 Capital Asset Fund	BT Level 1 Trauma	Cash on Deposit with Harris County Project Management	Restricted Cash and Cash Equivalents LPPF	Other
Money market government funds	\$ 44,239	\$ 3,319	\$ -	\$ 4,905	\$ -	\$ 35,894	\$ 121
U.S. Treasury notes	29,142	29,142	-	-	-	-	-
Commercial paper	3,793	-	-	2,990	-	-	803
Other	21,736	-	-	-	21,736	-	-
	98,910	32,461	-	7,895	21,736	35,894	924
Less funds required for current liabilities	(42,728)	(6,834)	-	-	-	(35,894)	-
	\$ 56,182	\$ 25,627	\$ -	\$ 7,895	\$ 21,736	\$ -	\$ 924

Through 2020, the System contracted with Harris County for the management of certain infrastructure projects. Under the agreement, the System deposits with the County estimated funds required for the completion of each project. The funds are held by the County for those project expenditures with any remaining amounts refunded upon project completion.

Foundation – Assets limited as to use of \$72 million and \$52 million at February 28, 2021 and February 29, 2020, respectively, are restricted subject to donor-imposed stipulations that will be met by actions of the Foundation or the passage of time.

HMOs – Assets limited as to use aggregating \$4 million at February 28, 2021 and February 29, 2020, are restricted as to use and are pledged to satisfy insolvency and other reserves, as required by the Texas Department of Insurance.

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Note 6: Investment Risk

GASB Statement No. 40, *Deposit and Investment Risk Disclosures – an Amendment of GASB Statement No. 3*, requires disclosures related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk associated with interest-bearing investments.

Credit Risk and Concentration of Credit Risk – Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization (NRSRO).

The System, the HMOs and the Foundation each have formal investment policies adopted by their governing boards, which limit investment in securities based on an NRSRO credit rating. The System's investments are also subject to the *Public Funds Investment Act* (the Act), Texas Administrative Code Section 2256, and the investments of the HMOs are also subject to regulations enumerated in Title 28, Chapter 11 of the Texas Administrative Code and Chapter 20A of the Texas Insurance Code. The Foundation's investments are not subject to these laws.

The System's investment policy is to be reviewed and approved annually by the Board of Trustees and the Commissioners' Court. The investment policy includes a list of authorized investment instruments, a maximum allowable stated maturity by fund type and the maximum weighted average maturity of the overall portfolio. Guidelines for diversification and risk tolerance are also detailed within the policy. Additionally, the policy includes specific investment strategies for fund groups that address each group's investment options and describes the priorities for suitable investments.

The System's investment policy establishes minimum acceptable credit ratings for certain investment instruments. Securities of states, agencies, counties, cities and other political subdivisions must be rated as to investment quality by a nationally recognized investment-rating firm as A or its equivalent. Money market mutual funds and public funds investment pools must be rated AAA or its equivalent.

Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The System mitigates these risks by emphasizing the importance of a diversified portfolio. All funds must be sufficiently diversified to eliminate the risk of loss resulting from overconcentration of assets in a specific maturity, a specific issuer or a specific class of securities. In particular, no more than 25.0 percent of the overall portfolio may be invested in time deposits, including certificates of deposit, of a single issuer. Concentration by issuer for other investment instruments is not specifically addressed in the investment policy. However, the policy does specify that acceptable investment instruments must have high-quality credit ratings.

GASB Statement No. 40 also provides that securities with split ratings, or a different rating assignment between NRSROs, are disclosed using the rating indicative of the greatest degree of risk.

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The table below indicates the fair value and maturity amount of the System's cash equivalents, assets limited as to use and investments as of February 28, 2021 and February 29, 2020, summarized by security type, as well as the percentage of total portfolio, the credit rating of the investment, and the modified duration in years for each summarized security type (in thousands).

2021					
Security	Fair Value	Percentage of Portfolio	Maturity Amount	Modified Duration (Years)	Credit Rating S&P/Rating Moody's
Investment Pools					
Texas CLASS - Pool (Corporate)	\$ 423,650	37.31 %	\$ 423,650	0.003	AAAm
Texas CLASS - Pool (Government)	72,677	6.40	72,677	0.003	AAAm
Lone Star - Pool	437,791	38.56	437,791	0.003	AAAm
U.S. Treasury notes	110,962	9.77	111,000	0.567	Aaa/AA+
Money market mutual funds	90,339	7.96	90,339	0.003	BBB+/BBB-
Total cash equivalents, assets limited as to use and investments	<u>\$ 1,135,419</u>	<u>100.00 %</u>	<u>\$ 1,135,457</u>	<u>0.116</u>	
2020					
Security	Fair Value	Percentage of Portfolio	Maturity Amount	Modified Duration (Years)	Credit Rating S&P/Rating Moody's
Commercial paper:					
Toyota Motor Credit Corp (TMCC)	\$ 50,703	5.16 %	\$ 50,800	0.493	A-1+
Natixis (NATX)	265,904	27.06	267,000	0.430	A-1
BNP Paribas	199,026	20.25	200,000	0.474	A-1
Exxon Mobile Corp	32,988	3.36	33,000	0.142	A-1+
Mitsubishi UFJ Financial Group	89,191	9.08	90,000	0.621	A-1
U.S. Treasury notes	29,025	2.95	29,000	0.975	Aaa/AA+
Money market mutual funds	315,902	32.14	315,902	0.003	AAA/AAa
Total cash equivalents, assets limited as to use and investments	<u>\$ 982,739</u>	<u>100.00 %</u>	<u>\$ 985,702</u>	<u>0.448</u>	

Custodial Credit Risk – Custodial credit risk for deposits is the risk that, in the event of failure of a depository financial institution, the System will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System will not be able to recover the value of its investment or collateral securities that are in the possession of another party.

Chapter 2257 of the Texas Government Code is known as the *Public Funds Collateral Act*. This act provides guidelines for the amount of collateral that is required to secure the deposit of public funds. Federal Deposit Insurance Corporation (FDIC) insurance is available for funds deposited at any one financial institution up to a maximum of \$250 thousand each for demand deposits, time and savings deposits and deposits pursuant to indenture.

The *Public Funds Collateral Act* requires that the deposit of public funds be collateralized in an amount not less than the total deposit, reduced by the amount of FDIC insurance available. At February 28, 2021 and February 29, 2020, the balance per the bank of Community Health Choice,

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Inc. demand and time deposits was \$600 thousand and \$7 million, respectively, of which \$350 thousand and \$7 million, respectively, was uninsured and uncollateralized.

The System's deposits are not exposed to custodial credit risk since all deposits are either covered by FDIC insurance or collateralized with securities held by the System or its agent in the System's name, in accordance with the *Public Funds Collateral Act*.

Interest Rate Risk – All investments carry the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the System manages its exposure to interest rate risk is by purchasing a combination of shorter and longer-term investments and by matching cash flows from maturities so that a portion of the portfolio is maturing evenly over time as necessary to provide the cash flow and liquidity needed for operations.

According to the System's investment policy, no more than 50.0 percent of the portfolio, excluding those investments held for future capital expenditures, debt service payments, bond fund reserve accounts, and capitalized interest funds, may be invested beyond 36 months. Additionally, at least 15.0 percent of the portfolio, with the previous exceptions, is invested in overnight instruments or in marketable securities that can be sold to raise cash within one day's notice. Overall, the average maturity of the portfolio, with the previous exceptions, shall not exceed three years. As of February 28, 2021 and February 29, 2020, the System was in compliance with these guidelines.

Foreign Currency Risk – Foreign currency risk is the risk that fluctuations in the exchange rate will adversely affect the value of investments denominated in a currency other than the U.S. dollar. The System's investment policy does not list securities denominated in a foreign currency among the authorized investment instruments. Consequently, the System is not exposed to foreign currency risk.

The table below indicates the fair value and maturity amount of the cash equivalents, assets limited as to use and investments of Community Health Choice, Inc. as of December 31, 2020 and 2019 summarized by security type. Also demonstrated are the percentage of total portfolio and the modified duration in years for each summarized security type (in thousands).

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2020					
Security	Fair Value	Percentage of Portfolio	Maturity Amount	Modified Duration (Years)	Credit Rating S&P/Rating Moody's
Certificates of deposit	\$ 3,325	4.16 %	\$ 3,325	0.430	AAA
Money market mutual funds	76,528	95.84	76,528	0.003	BBB+
	<u>\$ 79,853</u>	<u>100.00 %</u>	<u>\$ 79,853</u>	<u>0.217</u>	
2019					
Security	Fair Value	Percentage of Portfolio	Maturity Amount	Modified Duration (Years)	Credit Rating S&P/Rating Moody's
Municipal bonds	\$ 25,341	33.13 %	\$ 25,203	0.153	AAA/AA/SP-1+
Certificates of deposit	3,425	4.48	3,425	0.419	AAA
Money market mutual funds	47,713	62.39	47,713	0.003	AAA
	<u>\$ 76,479</u>	<u>100.00 %</u>	<u>\$ 76,341</u>	<u>0.065</u>	

The table below indicates the fair value and maturity amount of the cash equivalents, assets limited as to use and investments of Community Health Choice Texas, Inc. as of December 31, 2020 and 2019, summarized by security type. Also demonstrated are the percentage of total portfolio and the modified duration in years for each summarized security type (in thousands).

2020					
Security	Fair Value	Percentage of Portfolio	Maturity Amount	Modified Duration (Years)	Credit Rating S&P/Rating Moody's
Municipal bonds	\$ 33,801	9.81 %	\$ 33,360	0.430	AAA/AA+/Aaa/AA/Aa1/Aa2
Certificates of deposit	600	0.17	600	0.185	AAA
Money market mutual funds	310,313	90.02	310,313	0.003	BBB+
	<u>\$ 344,714</u>	<u>100.00 %</u>	<u>\$ 344,273</u>	<u>0.206</u>	
2019					
Security	Fair Value	Percentage of Portfolio	Maturity Amount	Modified Duration (Years)	Credit Rating S&P/Rating Moody's
Municipal bonds	\$ 35,335	20.27 %	\$ 35,040	0.345	AAA/AA+/AA/Aa1/Aa2/MIGI
Certificates of deposit	600	0.34	600	0.185	AAA
Money market mutual funds	138,389	79.39	138,389	0.003	AAA
	<u>\$ 174,324</u>	<u>100.00 %</u>	<u>\$ 174,029</u>	<u>0.379</u>	

The System categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 are quoted prices in an active market for identical assets, Level 2 are significant other observable inputs and Level 3 are significant unobservable inputs.

Investments in external investment pools qualifying for amortized cost under GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*, are carried at amortized cost per share, thus, they are excluded from fair value reporting below.

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The following is a summary of the hierarchy of the fair value of cash equivalents, assets limited as to use, investments, and derivative instrument (*Note 8*) of the System as of February 28, 2021 and February 29, 2020 (in thousands).

	2021 Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
U.S. Treasury notes	\$ 110,962	\$ -	\$ -	\$ 110,962
Money market mutual funds	90,339	-	-	90,339
Total cash equivalents, assets limited as to use and investments by fair value	\$ 201,301	\$ -	\$ -	\$ 201,301
Liabilities				
Derivative financial instrument	\$ -	\$ 15,861	\$ -	\$ 15,861

	2020 Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
Commercial paper	\$ -	\$ 637,812	\$ -	\$ 637,812
U.S. Treasury notes	29,025	-	-	29,025
Money market mutual funds	315,902	-	-	315,902
Total cash equivalents, assets limited as to use and investments by fair value	\$ 344,927	\$ 637,812	\$ -	\$ 982,739
Liabilities				
Derivative financial instrument	\$ -	\$ 19,115	\$ -	\$ 19,115

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The following is a summary of the hierarchy of the fair value of investments and cash equivalents of Community Health Choice, Inc. as of December 31, 2020 and 2019 (in thousands):

2020 Fair Value Measurements Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
Money market mutual funds	\$ 76,528	\$ -	\$ -	\$ 76,528
Total investments and cash equivalents by fair value level	<u>\$ 76,528</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 76,528</u>
2019 Fair Value Measurements Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
Municipal bonds	\$ -	\$ 25,341	\$ -	\$ 25,341
Money market mutual funds	47,713	-	-	47,713
Total investments and cash equivalents by fair value level	<u>\$ 47,713</u>	<u>\$ 25,341</u>	<u>-</u>	<u>\$ 73,054</u>

The following is a summary of the hierarchy of the fair value of investments and cash equivalents of Community Health Choice Texas, Inc. as of December 31, 2020 and 2019 (in thousands):

2020 Fair Value Measurements Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets				
Municipal bonds	\$ -	\$ 33,801	\$ -	\$ 33,801
Money market mutual funds	310,313	-	-	310,313
Total investments and cash equivalents by fair value level	<u>\$ 310,313</u>	<u>\$ 33,801</u>	<u>-</u>	<u>\$ 344,114</u>

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	2019 Fair Value Measurements Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets				
Municipal bonds	\$ -	\$ 35,335	\$ -	\$ 35,335
Money market mutual funds	138,389	-	-	138,389
Total investments and cash equivalents by fair value level	\$ 138,389	\$ 35,335	-	\$ 173,724

Note 7: Capital Assets

The System's investment in capital assets as of February 28, 2021 and February 29, 2020, consists of the following (in thousands):

	2021			Ending Balance
	Beginning Balance	Additions/ Transfers	Retirements	
Land and improvements	\$ 46,180	\$ 658	\$ (9)	\$ 46,829
Buildings and fixed equipment	706,083	23,339	(6,838)	722,584
Major movable equipment	410,477	31,475	(21,764)	420,188
Total historical cost	1,162,740	55,472	(28,611)	1,189,601
Less accumulated depreciation:				
Land and improvements	(14,149)	(955)	9	(15,095)
Buildings and fixed equipment	(391,819)	(28,655)	6,742	(413,732)
Major moveable equipment	(304,244)	(30,141)	21,063	(313,322)
Total accumulated depreciation	(710,212)	(59,751)	27,814	(742,149)
Construction in progress	39,922	39,110	-	79,032
Capital assets - net	\$ 492,450	\$ 34,831	\$ (797)	\$ 526,484

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	2020			
	Beginning Balance	Additions/ Transfers	Retirements	Ending Balance
Land and improvements	\$ 45,435	\$ 804	\$ (59)	\$ 46,180
Buildings and fixed equipment	659,640	59,222	(12,779)	706,083
Major movable equipment	387,639	44,580	(21,742)	410,477
Total historical cost	<u>1,092,714</u>	<u>104,606</u>	<u>(34,580)</u>	<u>1,162,740</u>
Less accumulated depreciation:				
Land and improvements	(13,296)	(912)	59	(14,149)
Buildings and fixed equipment	(378,286)	(25,191)	11,658	(391,819)
Major moveable equipment	(296,904)	(28,547)	21,207	(304,244)
Total accumulated depreciation	<u>(688,486)</u>	<u>(54,650)</u>	<u>32,924</u>	<u>(710,212)</u>
Construction in progress	62,068	(22,146)	-	39,922
Capital assets - net	<u>\$ 466,296</u>	<u>\$ 27,810</u>	<u>\$ (1,656)</u>	<u>\$ 492,450</u>

Note 8: Long-Term Debt

Long-term debt of the System consists of various issues of Revenue Bonds and Combination Tax and Revenue Certificates of Obligation (Certificates). Revenue Bonds are payable from the pledged revenue generated by the System. Combination Tax and Revenue Certificates of Obligation are payable from the levy and collection of an ad valorem tax, levied on taxable property within the System. Although taxes are levied and collected by Harris County for the System, the Certificates are direct obligations of the System and the holders are not entitled to demand payment from any tax revenue or other revenues of Harris County.

Revenue Bonds

On October 3, 2007, the System issued two Series of Harris County Hospital District Senior Lien Refunding Revenue Bonds (the Bonds). The Series 2007A Bonds, in the amount of \$199 million, were sold to provide funding for expansion and renovation projects, to refund the System's outstanding commercial paper, to fund the Debt Service Reserve Fund, and to pay costs of issuance. The Series 2007B Bonds, in the amount of \$103 million, were used to refund the Series 2000 revenue bonds and to pay costs of issuance. The Series 2007 Bonds were insured by municipal bond insurance policies and secured by a lien on the pledged revenue of the System and certain funds established pursuant to the bond order.

In October 2016, the System refunded and refinanced the Series 2007A Bonds by issuing the \$160 million Series 2016 Senior Lien Refunding Revenue bonds at a premium of \$15 million.

The proceeds of the Series 2016 Bonds and existing debt service and debt service reserve funds covered cost of issuance and defeased the Series 2007A bonds in the principal amount \$178 million. An irrevocable deposit of sufficient funds with trustees was made to pay the principal and interest of the defeased bonds through maturity. In February 2017, the System paid the non-

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refunded principal balance due and related interest. The Series 2016 Bonds have a final maturity of February 15, 2042. The bonds were issued as serial bonds in the amount of \$106 million maturing February 15, 2036, and \$54 million in term bonds maturing February 15, 2042. The bonds maturing on or after February 15, 2027, are subject to optional redemption on or after February 15, 2026. The term bonds are additionally subject to mandatory sinking fund redemption. The refunding resulted in a net present value economic gain of \$37 million.

The Series 2007B Bonds have a final maturity date of February 1, 2042, and were initially issued as 28-day taxable auction-rate paper, convertible to tax-exempt on August 16, 2010. In April 2008, these bonds were converted from auction-rate securities and reoffered as variable rate bonds bearing interest at a term rate during a term period. The 2007B Bonds Series were hedged with a forward starting swap effective upon the tax-exempt conversion of the bonds.

In August 2010, the System refunded and refinanced the Series 2007B Bonds by issuing Series 2010 Refunding and Revenue bonds in the amount of \$104 million. The proceeds of the Series 2010 Bonds covered costs of issuance and defeased the Harris County Hospital District Senior Lien Refunding Revenue Bonds, Series 2007B, in the principal amount of \$104 million through the irrevocable deposit of sufficient funds with trustees to pay the principal and interest of such bonds through maturity. Accordingly, these trustee funds and the related defeased indebtedness are excluded from the balance sheet. The refunding resulted in a loss of \$22 million, which includes \$16 million deferred loss on refunding related to the interest rate swap, which has been deferred and is being amortized over the life of the Series 2007B Bond issue. The remaining loss on refunding of \$6 million has been deferred and is being amortized to interest expense over the life of the Series 2010 bond issue. The primary components of this loss were the write-offs of unamortized deferred financing costs and bond premiums, the net deferred amount related to the hedging derivative instrument associated with the 2007B Bonds and the difference between amounts funded for the defeasance and the principal due on the 2007B Bonds. The financial statements reflect deferred outflows-unamortized debt refunding loss of \$8 million and \$9 million at February 28, 2021 and February 29, 2020, respectively. Principal amounts of total defeased indebtedness outstanding at February 28, 2021 and February 29, 2020, are \$67 million and \$73 million, respectively. The bonds are secured by an irrevocable letter of credit issued by JPMorgan Chase Bank.

The Series 2010 Refunding and Revenue bonds in the amount of \$104 million are variable rate demand bonds maturing through February 15, 2042. The bonds are subject to purchase on the demand of the owner at a price equal to purchase price on any given business day upon irrevocable notice by electronic means to the System's tender agent and remarketing agent.

Under an irrevocable letter of credit issued by JPMorgan Chase Bank, only the tender agent is entitled to draw an amount sufficient to pay the principal amount of the bonds when due, or to pay the portion of the purchase price corresponding to the principal amount upon certain tenders. The letter of credit facility expires on August 12, 2024. Unreimbursed advances will accrue interest at the higher of (i) the Prime Rate, (ii) one-month LIBOR plus 2.5 percent, or (iii) 7.5 percent per annum. The System is also required to pay to the JPMorgan Chase Bank an annual facility fee for the letter of credit of 0.9 percent per annum of the outstanding principal amount of the bonds. No amounts were outstanding on the letter of credit as of February 28, 2021 and February 29, 2020. In

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addition, the System is required to pay the remarketing agent an annual fee of \$1.00 per \$1,000 of principal amount of the bonds actually remarketed.

Compliance

The System is in compliance with its debt covenants at February 28, 2021 and February 29, 2020.

Interest Rate Swap

Related Bonds – On September 25, 2007, the System entered into an interest rate swap agreement in connection with its \$104 million Harris County Hospital District Senior Lien Revenue and Refunding Bonds, Series 2007B with the settlement date on October 3, 2007. On August 12, 2010, when the System refunded and refinanced the Series 2007B Bonds by issuing Series 2010 Bonds, the interest rate swap was redesignated and associated with the new debt. The derivative contained an off-market element equal to the value of the swap associated with the Series 2007B Bonds on August 12, 2010. In accordance with GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, this off-market element is recorded as a borrowing payable and is amortized as an adjustment to interest expense over the life of the swap agreement.

Objective of the Swap – The intention of the swap was to effectively reduce the impact of the System's variable interest rate exposure on the Related Bonds to a synthetic fixed rate of 4.2 percent.

Swap terms:

Trade date	September 12, 2007
Effective date	August 16, 2010
Termination date	February 15, 2042
Initial notional amount	\$103,500,000
District pays fixed	4.218%
Counterparty pays floating	SIFMA Municipal Swap Index
Payment dates	Monthly on the 15th calendar day of every month

As further defined in the confirmation to the swap agreement, the System is subject to an "Annual Counterparty Ceiling" which limits the maximum payment, inclusive of collateral, made by the System in any fiscal year to \$40 million. Subject to cash settlement, the System has the right to terminate the agreement, in whole or in part, on the Effective Date, August 16, 2010, and on any Business Day (as observed by New York and London financial markets) thereafter.

The effectiveness of the interest rate swap has been measured using the regression analysis method. The System has concluded that the transactions are effective.

Fair Value – The redesignated swap that is associated with the new debt had a zero fair value at its inception date and a fair value of \$(16) million and \$(19) million at February 28, 2021 and February 29, 2020, respectively, and is reported as a derivative liability in the statements of net position. The fair value of the swap was determined by calculating the present value of the

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anticipated future cash flows for both the floating portion and the stated fixed rate portion using discount factors derived from the London Interbank Offered Rate (LIBOR) swap curve.

Interest Rate Risk – The System is exposed to interest rate risk in that as the variable rates on the swap agreements decrease the System's net payment in the swap agreement could increase.

Basis Risk – The System is exposed to basis risk when the variable interest rate paid to the holders of its variable rate demand obligations is not equivalent to the variable interest rate received from its counterparties on the related swap agreements. When exposed to basis risk, the net interest expense incurred on the combination of the swap agreement and the associated variable rate debt may be higher or lower than anticipated.

Collateral Posting Risk – The risk that the System will be required to secure its obligations under the swap agreement. Any securities posted as collateral would not be available for the System's expenditure or reserve needs, which could adversely impact credit ratings and overall liquidity and budgetary efforts. The System was not exposed to collateral posting risk as of and for the years ended February 28, 2021 and February 29, 2020.

Credit Risk – The risk of a change in the credit quality or credit rating of the System and/or its counterparty. At both February 28, 2021 and February 29, 2020, the swap counterparty was rated BBB+ by Standard & Poor's, A3 by Moody's Investor Services, and BBB+ by Fitch. At both February 28, 2021 and February 29, 2020, the System was rated AA- by Standard & Poor's, Aa1 by Moody's Investor Services and AA by Fitch.

Rollover Risk – The System is exposed to rollover risk only on swaps that mature or may be terminated at the counterparty's option prior to the maturity of the associated debt. As of February 28, 2021 and February 29, 2020, the System was not exposed to rollover risk.

Termination Risk – The System's swap agreements do not contain any out-of-the-ordinary termination events that would expose it to significant termination risk. In keeping with market standards, the System or the counterparty may terminate each swap if the other party fails to perform under the terms of the contract. In addition, the swap documents allow either party to terminate in the event of a significant loss of creditworthiness. If at the time of the termination a swap has a negative value, the System would be liable to the counterparty for a payment equal to the fair value of such swap. As of February 28, 2021 and February 29, 2020, termination of the original swap agreement would create a liability of \$27 million and \$31 million, respectively, and would result in a reversal of the derivative liability related to the redesignated swap, the borrowing payable amount and the unamortized loss on refunding. Any resulting net change would be recorded through nonoperating expenses.

Swap Payments – Using interest rates as of February 28, 2021, debt service requirements of the System's outstanding fixed and variable-rate debt and net swap payments on the variable-rate debt were as follows (in thousands). As rates vary, variable rate interest rate payments on the bonds and net swap payments will change.

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2021				
Years Ending February	Debt Principal	Debt Interest	Swaps, Net	Total
2022	\$ 6,765	\$ 9,491	\$ (2,461)	\$ 13,795
2023	7,080	9,173	(2,385)	13,868
2024	7,400	8,840	(2,306)	13,934
2025	7,755	8,491	(2,224)	14,022
2026	8,125	8,126	(2,138)	14,113
2027-2031	46,690	34,515	(9,272)	71,933
2032-2036	57,320	23,685	(6,531)	74,474
2037-2041	69,410	11,642	(3,187)	77,865
2042	15,575	622	(171)	16,026
Total	<u>\$ 226,120</u>	<u>\$ 114,585</u>	<u>\$ (30,675)</u>	<u>\$ 310,030</u>

Hybrid Instrument Borrowings – The System's interest rate swap includes fixed rates that were off market at the execution of the interest rate swap. For financial reporting purposes, the interest rate swap is considered a hybrid instrument and is bifurcated between borrowings, with an aggregate original amount of \$18 million reflecting the fair value of the instrument at its execution, and an interest rate swap with a fixed rate that was considered at the market at execution.

Activity for the hybrid instrument borrowings for the years ended February 28, 2021 and February 29, 2020, was as follows (in thousands).

	2021	2020
Beginning balance	\$ 9,612	\$ 10,366
Reductions	<u>(733)</u>	<u>(754)</u>
Ending balance	<u>\$ 8,879</u>	<u>\$ 9,612</u>

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The following table sets forth as of February 28, 2021, the amortization of the hybrid instrument borrowings for the next five years and thereafter (in thousands).

Years ending February:		
2022	\$	712
2023		690
2024		667
2025		644
2026		619
2027-2031		2,684
2032-2036		1,891
2037-2041		922
2042		<u>50</u>
Total	\$	<u><u>8,879</u></u>

Certificates of Obligation, Series 2016

In August 2016, the System issued Combination Tax and Revenue Certificates of Obligation, Series 2016 in the principal amount of \$63 million. The funds are being used to expand the operative suites and supporting services at Ben Taub Hospital necessary to maintain the facility's Level 1 Trauma status. The bonds mature in February 2036. The System's financial statements reflect \$53 million and \$55 million in outstanding principal and \$5 million and \$6 million in unamortized premium related to this debt at February 28, 2021 and February 29, 2020, respectively. Principal and interest paid, as well as corresponding tax revenue applicable to debt service, was \$5 million for both 2021 and 2020.

Certificates of Obligation, Series 2020

In April 2020, the System issued the combination tax and revenue Certificates of Obligation, Series 2020 (the 2020 certificates of obligation) in the amount of \$31 million. The 2020 certificates of obligation mature in various amounts annually starting February 15, 2021 through February 15, 2030, with a stated coupon rate of 5.0%. The 2020 Certificates are collateralized by a levy of ad valorem tax revenue and lien on and pledge of surplus revenues. Proceeds from the 2020 Certificates are being used to fund the construction and equipping of certain facilities at Ben Taub Hospital and the purchase and installation of certain medical equipment in Harris County's jail facilities as well as the purchase and installation of an upgraded electronic medical record system, among other facility improvements. The System's financial statements reflect \$29 million in outstanding principal and \$5 million in unamortized premium related to this debt at February 28, 2021. Principal and interest paid, as well as corresponding tax revenue applicable to debt service, was \$3 million for 2021.

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Annual debt service requirements to maturity as of February 28, 2021 are as follows (in thousands).

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Years ending February:			
2022	\$ 5,155	\$ 3,606	\$ 8,761
2023	5,415	3,349	8,764
2024	5,685	3,078	8,763
2025	5,970	2,794	8,764
2026	6,240	2,524	8,764
2027-2031	31,960	7,787	39,747
2032-2036	21,115	2,339	23,454
	<u>81,540</u>	<u>25,477</u>	<u>107,017</u>
Total	<u>\$ 81,540</u>	<u>\$ 25,477</u>	<u>\$ 107,017</u>

Other Obligations

Other long-term obligations at February 28, 2021, are as follows (in thousands):

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Years ending February:			
2022	\$ 38	\$ 1	\$ 39
2023	10	-	10
	<u>48</u>	<u>1</u>	<u>49</u>
Total	<u>\$ 48</u>	<u>\$ 1</u>	<u>\$ 49</u>

Note 9: Employee Benefit Plans

The System currently maintains two benefit plans allowing employees to plan and save for retirement: a defined contribution plan and a defined benefit plan. In October 2006, the Harris County Hospital District Board of Trustees amended the defined benefit pension plan to close enrollment. The amended plan offers employees hired prior to January 1, 2007, a choice to either (1) continue with their current pension plan or (2) elect to participate in the System's enhanced 401(k) retirement savings plan with a match, effective July 2007, of up to 5.0 percent of participant's compensation provided by the System. All new hires and rehires after December 31, 2006, are only eligible for the System's 401(k) retirement savings plan with a match of up to 5.0 percent. The change was designed to safeguard individuals approaching retirement, who had accumulated a large pension benefit in the current plan, while providing employees who planned to work many more years an option for better flexibility and portability in the System's enhanced 401(k) plan.

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The System administers the Harris County Hospital District Pension Plan and the Harris County Hospital District 401(k) Plan. The System issues publicly available financial reports that include financial statements and required supplementary information. The financial reports may be obtained by writing to Harris Health System, Human Resources Department, 4800 Fournace Place, Bellaire, Texas 77401.

Defined Contribution Plan

The System has a defined contribution 401(k) plan (which qualifies as a tax-exempt employee benefit plan under Section 401(a) of the Internal Revenue Code) (401(k) Plan) open to all full-time and part-time employees of the System who meet the plan's requirements. It is a single-employer, self-administered, trustee plan to which contributions are made by participants on a bi-weekly basis not to exceed the statutory maximum of \$20 thousand and \$19 thousand during calendar years 2020 and 2019, respectively, for all participants. Contributions to the plan cannot exceed the statutory maximum of \$26 thousand and \$25 thousand during calendar years 2020 and 2019, respectively, for participants age 50 and older. Effective July 2007, the System enhanced the 401(k) Plan with an employer match up to 5.0 percent of the participant's compensation for eligible employees, which is 100.0 percent vested with three or more years of service. The 401(k) Plan is a governmental plan and, as such, is specifically exempt from the reporting and disclosure requirements of Title I of the *Employee Retirement Income Security Act of 1974* (ERISA). Total participant contributions were \$40 million and \$37 million in fiscal years 2021 and 2020, respectively. Total System contributions were \$18 million and \$15 million in fiscal years 2021 and 2020, respectively.

Forfeitures under the 401(k) Plan for a plan year will be applied to reduce the System's obligation to make future matching contributions or to pay 401(k) Plan administrative expenses for the 401(k) Plan year. During each of the years ended February 28, 2021 and February 29, 2020, System contributions were reduced by approximately \$1 million from forfeited non-vested accounts.

Pension Plan

The System has a noncontributory, defined benefit pension plan (the Plan). It is a single-employer, self-administered, trustee plan in which a separate stand-alone financial report is issued. The Plan is administered by an Administrative Committee appointed by the Board of Trustees of the System, which is responsible for administering the Plan under the terms that are established. The Board of Trustees approves amendments to the Plan. State Street Bank & Trust Co. serves as the trustee and custodian for the Plan. As a unit of local government, the Plan is not covered by ERISA. The Plan is funded through actuarially determined contributions by the System. The entry age normal method is used to determine both the funding and the pension benefit obligation.

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Each participant shall have a monthly benefit payable for life equal to the greater of (a) the number of years of service multiplied by 1.5 percent of average monthly compensation (average base compensation received in five highest consecutive calendar years out of the 10 complete calendar years prior to retirement) or (b) the accrued monthly retirement benefit determined as of January 1, 1989, plus the number of years of future service earned after January 1, 1989, multiplied by 1.5 percent of average monthly compensation, subject to a minimum equal to the benefit earned under the Plan prior to the adoption of the 6th Amendment as of September 30, 1991 (applies to non-highly compensated employees only). Monthly benefit payments are subject to a minimum based on the number of years of service multiplied by \$6 and a maximum provision permitted to be paid under Section 415 of the Internal Revenue Code. Participants may also elect to receive their benefits in other optional forms approved by the Administrative Committee.

As of January 1, 2020 and 2019, the following employees were covered by the benefit terms:

	2020	2019
Inactive employee or beneficiaries currently receiving benefits	3,210	3,108
Inactive employees entitled to but not yet receiving benefits	1,345	1,349
Active employees	2,175	2,335
	6,730	6,792

The Harris Health System Board of Trustees establishes the contribution requirements of the System based on an actuarially determined rate recommended by an independent actuary. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. For the year ended February 28, 2021, the System contributed \$54 million or 34.0 percent of covered payroll. For the year ended February 29, 2020, the System contributed \$34 million or 21.0 percent of covered payroll.

Net Pension Liability

The System's net pension liability was measured as of December 31, 2020 and 2019, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of those dates.

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Actuarial assumptions and methods used in the actuarial valuations are as follows.

	2020	2019
Valuation date	January 1, 2020	January 1, 2019
Measurement date	December 31, 2020	December 31, 2019
Actuarial cost method	Entry age normal	Entry age normal
Equivalent single amortization period	20 years, closed	20 years, closed
Asset valuation method	Market value	Market value
Actuarial assumptions:		
Inflation	2.5%	2.5%
Investment rate of return (net of expenses)	6.25	6.75
Projected salary increases (ultimate rate):		
Initial rate	5.1	5.1
Ultimate rate	3.0	3.0
Mortality rates:		
Healthy	Pri-2012 Total Dataset Mortality Table, with generational mortality improvement projected after year 2012 using Scale MP-2020	Pri-2012 Total Dataset Mortality Table, with generational mortality improvement projected after year 2012 using Scale MP-2019
Disabled	Pri-2012 Disability Mortality Table, with generational mortality improvement projected after year 2012 using Scale MP-2020	Pri-2012 Disability Mortality Table, with generational mortality improvement projected after year 2012 using Scale MP-2019

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return as of December 31, 2020, for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Real estate funds	5 %	6.83 %
Domestic equity-large cap	26	7.74
Domestic equity-small/mid cap	4	8.42
International equity	25	8.28
Fixed income	35	4.60
Hedge funds	5	6.71
	<u>100 %</u>	

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The discount rate used to measure the total pension liability was 6.3 percent and 6.8 percent, net of expenses, as of December 31, 2020 and 2019, respectively. The projection of cash flows used to determine the discount rate assumed that System contributions would be made at rates equal to the actuarial determined contribution and the Plan's fiduciary net position is projected to cover benefit payments and administrative expenses.

Changes in the net pension liability are as follows (in thousands):

	Increase (Decrease)		
	Total Pension Liability (a)	Plan Fiduciary Net Position (b)	Net Pension Liability (a)-(b)
Balances at December 31, 2019	\$ 962,260	\$ 737,322	\$ 224,938
Changes for the year:			
Service cost	8,036	-	8,036
Interest	64,307	-	64,307
Differences between expected and actual experience	3,807	-	3,807
Changes of assumptions	50,545	-	50,545
Contributions - employer	-	53,778	(53,778)
Net investment income	-	138,087	(138,087)
Benefit payments	(50,184)	(50,184)	-
Administrative expense	-	(2,366)	2,366
Net changes	<u>76,511</u>	<u>139,315</u>	<u>(62,804)</u>
Balance at December 31, 2020	<u>\$ 1,038,771</u>	<u>\$ 876,637</u>	<u>\$ 162,134</u>

	Increase (Decrease)		
	Total Pension Liability (a)	Plan Fiduciary Net Position (b)	Net Pension Liability (a)-(b)
Balances at December 31, 2018	\$ 914,616	\$ 634,716	\$ 279,900
Changes for the year:			
Service cost	8,057	-	8,057
Interest	63,183	-	63,183
Differences between expected and actual experience	243	-	243
Changes of assumptions	23,528	-	23,528
Contributions - employer	-	33,621	(33,621)
Net investment income	-	119,362	(119,362)
Benefit payments	(47,367)	(47,367)	-
Administrative expense	-	(3,010)	3,010
Net changes	<u>47,644</u>	<u>102,606</u>	<u>(54,962)</u>
Balance at December 31, 2019	<u>\$ 962,260</u>	<u>\$ 737,322</u>	<u>\$ 224,938</u>

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Sensitivity of the net pension liability to changes in the discount rate – the following presents the net pension liability of the System, calculated using the discount rate of 6.3 percent, as well as what the System's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (5.3 percent) or 1.0 percentage point higher (7.3 percent) than the current rate (in thousands):

	1% Decrease	Current Discount	1% Increase
System's net pension liability	\$ 284,507	\$ 162,134	\$ 59,139

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the fiscal years ended February 28, 2021 and February 29, 2020, the System recognized pension expense of \$39 million and \$52 million, respectively. At February 28, 2021 and February 29, 2020, the System reported deferred outflows and deferred inflows of resources related to pension from the following sources (in thousands).

	2021	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Changes of assumptions	\$ 26,830	\$ -
Differences between expected and actual experience	1,895	-
Net difference between projected and actual earnings on pension plan investments	-	89,893
Employer contributions remitted subsequent to the measurement date	8,926	-
Total	\$ 37,651	\$ 89,893

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	2020	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Changes of assumptions	\$ 15,250	\$ -
Differences between expected and actual experience	1,409	-
Net difference between projected and actual earnings on pension plan investments	-	30,310
Employer contributions remitted subsequent to the measurement date	9,000	-
Total	\$ 25,659	\$ 30,310

At both February 28, 2021 and February 29, 2020, the System reported \$9 million as deferred outflows of resources related to pensions resulting from System contributions made subsequent to the measurement date that will be recognized as a reduction of the net pension liability at February 28, 2022 and February 28, 2021.

Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows (in thousands):

Year ended the last day of February:	
2022	\$ 1,996
2023	(14,511)
2024	(31,579)
2025	(17,074)
	\$ (61,168)

Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in the separately issued Plan financial report.

Deferred Compensation

The System has a deferred compensation plan for the benefit of its eligible employees under Section 457 of the Internal Revenue Code of 1954. The assets in the Deferred Compensation Plan, which is not recorded in the accompanying statements of net position, are not subject to creditors. The Deferred Compensation Plan assets at February 28, 2021 and February 29, 2020, were approximately \$144 million and \$118 million, respectively.

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Note 10: Other Postemployment Benefits (OPEB) Health Care Plan

Plan Description and Benefits Provided

The OPEB is sponsored by the System which provides certain health care benefits for retired employees. The System's employees may become eligible for those benefits upon completing 10 years of service. Retiree medical plan participants are provided benefits under the System's self-insured medical plan. The contribution requirements of plan members and the System are established by and may be amended by the System's Board of Trustees. The System funds these benefits on a pay-as-you-go basis, meaning that the System will pay benefits as they come due. For fiscal years 2021 and 2020, the System contributed \$21 million and \$20 million, respectively, to the Plan for current premiums and administrative costs. Plan members receiving benefits during both fiscal years 2021 and 2020 contributed \$4 million, or approximately 21.0 percent of the total premiums, through their required contribution. Plan members that are ages 65 and younger were required to contribute \$75.83 and \$96.75 per month for retiree-only coverage and \$477.42 and \$593.42 for retiree and spouse coverage in 2021 and 2020, respectively. Plan members that are ages 65 and older were required to contribute \$107.83 and \$126.08 per month for retiree-only coverage and \$565.00 and \$680.33 for retiree and spouse coverage in 2021 and 2020, respectively. The OPEB does not issue a separate report that includes financial statements. No assets are accumulated in a trust that meets the criteria in paragraph 4 of GASB Statement 75. In an amendment approved by the board on January 25, 2018, employees hired after June 1, 2018 are no longer eligible to participate in the OPEB.

At February 28, 2021 and February 29, 2020, the following employees were covered by the benefit terms.

	2021	2020
Inactive employee or beneficiaries currently receiving benefits	2,113	2,086
Active employees	6,578	7,858
	8,691	9,944

Total OPEB Liability

The System's total OPEB liability of \$589 million and \$486 million and expense of \$44 million and \$30 million as of February 28, 2021 and February 29, 2020, respectively, and was determined by an actuarial valuation as of March 1, 2020 and 2019, respectively, and rolled forward to the measurement date.

The total OPEB liability in the actuarial valuation report was determined using the following actuarial assumptions and the entry age normal actuarial cost method, applied to all periods included in the measurement, unless otherwise specified:

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	2021	2020
Salary increases	2.5%	2.5%
Discount rate	1.21%	2.50%
Health care cost trend rates	6.50% for 2021, decreasing to 5.75% over 3 years and following the Getzen model thereafter	7.50% for 2020, decreasing to 6.75% over 3 years and following the Getzen model thereafter

The discount rate used to measure the total OPEB liability was 1.2 percent which is based on the S&P Municipal Bond 20 Year High Grade Rate Index as of February 28, 2021.

For 2021, mortality rates for healthy pre-commencement and post-participants were based on Pri-2012 bottom quartile mortality tables with generational projected after year 2006 using scale MP-2020. Rates for disabled participants were based on Pri-2012 mortality tables for disabled retirees, adjusted to 2006, with generational mortality improvement projected after year 2016 using Scale MP-2020.

For 2020, mortality rates for healthy pre-commencement and post-participants were based on Pri-2012 bottom quartile mortality tables with generational projected after year 2006 using scale MP-2019. Rates for disabled participants were based on Pri-2012 mortality tables for disabled retirees, adjusted to 2006, with generational mortality improvement projected after year 2016 using Scale MP-2019.

No formal actuarial experience studies have been performed.

Changes in the Total OPEB Liability (In Thousands)

	2021	2020
Total OPEB liability, beginning of year	\$ 486,430	\$ 444,321
Changes for the year:		
Service cost	9,895	9,424
Interest	11,990	15,195
Experience gains	(3,056)	(30,004)
Change of assumptions	100,078	63,631
Benefit payments	(16,731)	(16,137)
Net changes	102,176	42,109
Total OPEB liability, end of year	\$ 588,606	\$ 486,430

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Sensitivity of the System's Total OPEB Liability to Changes in the Discount Rate and Health Care Cost Trend Rates

The total OPEB liability has been calculated using a discount rate of 1.2 percent. The following table presents the total OPEB liability of the System using a discount rate 1.0 percent higher and 1.0 percent lower than the current discount rate (in thousands):

	1% Decrease	Current Discount Rate	1% Increase
Total OPEB Liability	\$ 695,014	\$ 588,606	\$ 504,701

The following presents the total System's OPEB liability, as well as what the System's OPEB liability would be if it were calculated using health care cost trend rates that are 1.0 percent higher and 1.0 percent lower than the current health care cost trend rates (in thousands):

	1% Decrease	Healthcare Cost Trend Rates (6.50% decreasing to 5.75%)	1% Increase
Total OPEB Liability	\$ 496,405	\$ 588,606	\$ 707,214

OPEB Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

At February 28, 2021, and February 29, 2020, the System reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources (in thousands):

	2021	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Changes of assumptions	\$ 125,818	\$ -
Differences between expected and actual experience	-	22,549
Total	<u>\$ 125,818</u>	<u>\$ 22,549</u>

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	2020	
	Deferred Outflows of Resources	Deferred Inflows of Resources
Changes of assumptions	\$ 53,026	\$ -
Differences between expected and actual experience	-	25,003
Total	\$ 53,026	\$ 25,003

Amounts reported as deferred outflows of resources and deferred inflows of resources at February 28, 2021, related to OPEB will be recognized in OPEB expense as follows (in thousands):

Year ended the last day of February:

2022	\$ 21,775
2023	21,775
2024	21,775
2025	21,775
2026	16,169
	\$ 103,269

Note 11: Concentrations of Credit Risk

The System provides services to its patients, most of whom are local residents and may be insured under third-party payor agreements, in accordance with its charity care policy (see *Note 2*). Patient service revenues (see *Note 3*) and the related accounts receivable are reflected in the System's financial statements net of charges for charity care provided. The mix of net receivables from self-pay patients and third-party payors at February 28, 2021 and February 29, 2020, is as follows:

	2021	2020
Medicaid	11%	15%
Medicare	39%	49%
Commercial	10%	6%
Self-pay patient	40%	30%
	100%	100%

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Note 12: Commitments and Contingencies

At February 28, 2021 and February 29, 2020, the System was a defendant in certain pending civil litigation and has notice of certain claims that have been asserted against it. The System is covered under the *Texas Tort Claims Act* (the Act). Under the Act, any claims and recoveries from pending or possible litigation due to personal injuries are limited to \$100 thousand per person and \$300 thousand per single occurrence of bodily injury or death. Professional liability claims have been asserted by various claimants. The claims are in various stages of processing, and some may ultimately be brought to trial. There are also other known and unknown incidents that have occurred through February 28, 2021, that may result in the assertion of additional claims.

The System covers its exposure for asserted and unasserted claims through a program of self-insurance and has accrued its best estimate of these contingent losses. In the opinion of the System's management, the outcomes of these actions will not have a material adverse effect on the financial statements of the System.

The System has self-insurance programs for the payment of hospital professional and general liability claims, workers' compensation, and employee health claims. Liabilities related to these programs are accrued utilizing actuarial analyses based on historical claims experience and are undiscounted. Changes in these self-insurance programs for the years ended February 28, 2021, and February 29, 2020, are as follows (in thousands).

	Beginning- of-year Liability	Current-year Claims and Changes In Estimates	Claim Payments	End-of-year Liability
Hospital professional and general liability:				
2021	\$ 2,615	\$ 2,674	\$ 2,261	\$ 3,028
2020	2,588	2,181	2,154	2,615
Workers' compensation liability:				
2021	\$ 2,299	\$ 711	\$ 1,102	\$ 1,908
2020	2,376	842	919	2,299
Employee healthcare benefits liability:				
2021	\$ 10,368	\$ 114,526	\$ 115,130	\$ 9,764
2020	9,779	112,337	111,748	10,368

The reserve for hospital professional and general liability, including malpractice, and the reserve for workers' compensation claims are included in accounts payable and accrued liabilities in the accompanying statements of net position. The reserve for incurred but unreported employee health claims is included in employee compensation and related benefit liabilities in the accompanying statements of net position.

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The System is also exposed to various risks of loss related to theft of, damage to, and destruction of assets, errors and omissions, and natural disasters. It is the System's policy to purchase commercial insurance for the risks of these losses. Settled claims have not exceeded this commercial coverage in any of the past three fiscal years.

At February 28, 2021, the System had commitments outstanding in the amount of approximately \$52 million related to improvements at existing facilities and \$5 million related to information technology projects.

At February 29, 2020, the System had commitments outstanding in the amount of approximately \$11 million related to improvements at existing facilities and \$8 million related to information technology projects.

The System had rental expenses related to its operating leases of approximately \$16 million and \$13 million during the years ended February 28, 2021 and February 29, 2020, respectively.

The System receives financial awards from federal and state agencies in the form of grants. Expenditures of funds under those programs require compliance with the grant agreements and are subject to audit. Any disallowed expenditures resulting from such audits become a liability of the System. In the opinion of management, such adjustments, if any, are not expected to materially affect the financial condition or operations of the System.

Note 13: Harris Collaborative Program

The Harris Collaborative Program is a collaborative established to improve the level of health care provided to the indigent population of Harris County by strategically allocating the available community health care resources and the burden of providing services. This collaborative wound down during the year ended February 29, 2020. Prior to dissolving, the parties to the collaborative included Harris Health System and the Affiliated Hospitals – Gulf Coast Division Inc., Memorial Hermann Hospital System, the Methodist Hospital System, Texas Children's Hospital, Tomball Regional Medical Center, Park Plaza Hospital, Houston Northwest Medical Center, Cypress Fairbanks Medical Center, Pearland Medical Center and St. Luke's Episcopal Health System. An affiliation agreement among the parties allowed the parties to improve access to health care for indigent persons residing in the Houston community through participation in one of the state's Medicaid supplemental payment programs for privately owned safety-net hospitals. The System provided funding for the nonfederal share of the Medicaid Supplemental Payment Program by using ad valorem tax revenues.

As part of the Harris collaboration, the Affiliated Hospitals formed a Certified Non-Profit Health Organization, Harris County Clinical Services Inc. (HCCS), to provide physician services to the indigent in the Harris County community. HCCS has an agreement with Affiliated Medical Services (AMS), a contracting entity for Baylor College of Medicine (Baylor) and the University of Texas Health Science Center (UT), which provides for Baylor and UT to supervise and direct services of patients of the System. With the creation of the collaborative, the agreement between AMS and HCCS was created in order to provide the physician services to indigent patients who

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seek treatment. In addition, HCCS also entered into agreements with other health care service providers to extend services available. Through its agreements with AMS and other providers, HCCS provided approximately \$147 million of physician and other clinical services annually to the indigent in the Harris County community during the year ended February 29, 2020, respectively. Under a management agreement between HCCS and the System, the System managed the services provided by AMS and provides facilities for indigent patients to receive services.

During the fiscal year ended February 29, 2020, the System utilized \$62 million of tax revenues as the nonfederal share of the Harris Collaborative program. The System recorded expenses of \$62 million in 2020 under the Harris Collaborative program and provider affiliation agreements. These expenses are reflected as physician services in the statements of revenues, expenses and changes in net position.

Note 14: COVID-19 Pandemic & CARES Act Funding

On March 11, 2020, the World Health Organization designated the SARS-CoV-2 virus and the incidence of COVID-19 (COVID-19) as a global pandemic. Patient volumes and the related revenues were significantly affected by COVID-19 as various policies were implemented by federal, state, and local governments in response to the pandemic that led many people to remain at home and forced the closure of or limitations on certain businesses, as well as suspended elective procedures by health care facilities.

Beginning in mid-March 2020, the System deferred all nonessential medical and surgical procedures and suspended elective procedures, which resumed prior to February 28, 2021.

During the year ended February 28, 2021, the System received \$78 million of distributions from the *Coronavirus Aid, Relief, and Economic Security* (“CARES”) Act Provider Relief Fund. These distributions from the Provider Relief Fund are not subject to repayment, provided the System is able to attest to and comply with the terms and conditions of the funding, including demonstrating that the distributions received have been used for qualifying expenses or lost revenue attributable to COVID-19, as defined by HHS.

The System is accounting for such payments as conditional contributions. Payments are recognized as non-operating revenue once the applicable terms and conditions required to retain the funds have been met. Based on an analysis of the compliance and reporting requirements of the Provider Relief Fund and the effect of the pandemic on the System’s operating revenues and expenses through February 28, 2021, the System recognized \$22 million, related to the Provider Relief Fund, and these payments are recorded as Provider Relief Fund revenue in the statement of revenues, expenses and changes in net position. The unrecognized amount of Provider Relief Fund distributions is recorded as Provider Relief Funds received in advance in the accompanying statements of net position.

The System will continue to monitor compliance with the terms and conditions of the Provider Relief Fund and the effect of the pandemic on the Hospital’s revenues and expenses. The terms and conditions governing the Provider Relief Funds are complex and subject to interpretation and

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change. If the System is unable to attest to or comply with current or future terms and conditions the System's ability to retain some or all of the distributions received may be affected. Additionally, the amounts recorded in the financial statements compared to the System's Provider Relief Fund reporting could differ. Provider Relief Fund payments are subject to government oversight, including potential audits.

Note 15: Fiscal Year End Change

On January 26, 2021, the Harris County Commissioners' Court approved a change in the fiscal year end from February 28 to September 30. This change is to be effective with the fiscal year beginning October 1, 2022. The County requested that the System evaluate the same change in its fiscal year, which is expected to occur in the second half of calendar 2021.

Required Supplementary Information

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**Schedule of Changes in the System's Net Pension Liability and Related Ratios
(Dollar amounts in thousands)**

	Plan Year Ended December 31,						
	2020	2019	2018	2017	2016	2015	2014
Total pension liability:							
Service cost	\$ 8,036	\$ 8,057	\$ 8,280	\$ 6,803	\$ 7,232	\$ 7,795	\$ 8,642
Interest	64,307	63,183	60,495	61,427	59,397	57,482	52,342
Difference between expected and actual experience	3,807	243	8,000	1,718	(4,063)	4,637	(1,909)
Changes of assumptions	50,545	23,528	15,748	10,709	-	-	40,689
Benefit payments	(50,184)	(47,367)	(44,712)	(42,563)	(40,178)	(44,023)	(34,444)
Net change in total pension liability	76,511	47,644	47,811	38,094	22,388	25,891	65,320
Total pension liability – beginning	962,260	914,616	866,805	828,711	806,323	780,432	715,112
Total pension liability – ending (a)	1,038,771	962,260	914,616	866,805	828,711	806,323	780,432
Plan fiduciary net position:							
Contributions – employer	53,778	33,621	30,984	29,433	32,693	31,759	31,292
Net investment income	138,087	119,362	(35,426)	107,519	37,401	(4,891)	37,069
Benefit payments	(50,184)	(47,367)	(44,712)	(42,563)	(40,178)	(44,023)	(34,444)
Administrative expense	(2,366)	(3,010)	(2,442)	(2,478)	(232)	(2,389)	(2,302)
Net change in plan fiduciary net position	139,315	102,606	(51,596)	91,911	29,684	(19,544)	31,615
Plan fiduciary net position – beginning	737,322	634,716	686,312	594,401	564,717	584,261	552,646
Plan fiduciary net position – ending (b)	876,637	737,322	634,716	686,312	594,401	564,717	584,261
System's net pension liability – ending (a) – (b)	\$ 162,134	\$ 224,938	\$ 279,900	\$ 180,493	\$ 234,310	\$ 241,606	\$ 196,171
Plan fiduciary net position as a percentage of the total pension liability	84.39%	76.62%	69.40%	79.18%	71.73%	70.04%	74.86%
Covered payroll	\$ 156,479	\$ 163,835	\$ 169,885	\$ 173,272	\$ 182,060	\$ 197,360	\$ 210,728
System's net pension liability as a percentage of covered payroll	103.61%	137.30%	164.76%	104.17%	128.70%	122.42%	93.09%

Notes to Schedule:

Changes of assumptions – In 2014, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the RP-2014 bottom quartile mortality tables with generational mortality improvement projected after 2014 with 50% of Scale MP-2014 for purposes of developing mortality rates.

Changes of assumptions – In 2017, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the MP-2017 scale and rate of return on investments from 7.5% to 7.0%.

Changes of assumptions – In 2018, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the RP-2014 total dataset mortality tables with generational mortality improvement projected after 2006 using Scale MP-2018 for purposes of developing mortality rates and change in inflation rate from 3.0% to 2.5%.

Changes of assumptions – In 2019, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the Pri-2012 total dataset mortality tables with generational mortality improvement projected after 2015 using Scale MP-2019 for purposes of developing mortality rates and change in investment return rate from 7.0% to 6.75%.

Changes of assumptions – In 2020, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the Pri-2012 total dataset mortality tables with generational mortality improvement projected after 2015 using Scale MP-2020 for purposes of developing mortality rates and change in investment return rate from 6.75% to 6.25%.

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Schedule of System Pension Contributions
January 1, 2021**

	Plan Year Ended December 31,						
	2020	2019	2018	2017	2016	2015	2014
Actuarially determined contribution	\$ 36,056	\$ 33,621	\$ 30,984	\$ 29,433	\$ 32,693	\$ 31,759	\$ 31,292
Contributions in relation to the actuarially determined contribution	53,778	33,621	30,984	29,433	32,693	31,759	31,292
Contribution deficiency (excess)	(17,722)	-	-	-	-	-	-
Covered payroll	\$ 156,479	\$ 163,835	\$ 169,885	\$ 173,272	\$ 182,060	\$ 197,360	\$ 210,728
Contributions as a percentage of covered payroll	34.37%	20.52%	18.24%	16.99%	17.96%	16.09%	14.85%

Notes to Schedule:

Valuation date:

Actuarially determined contribution rates are calculated as of January 1, one year prior to the end of the fiscal year in which contributions are reported.

Methods and assumptions used to determine contribution rates:

Actuarial cost method	Entry age normal
Amortization method	Layered over a closed 20-year period
Asset valuation method	Market value, 5-year smoothing
Inflation	2.5%
Salary increases	5.1% initial rate 3.0% ultimate rate
Investment rate of return	6.25%, net of pension plan investment expense, including inflation
Retirement age	Various – Expected retirement ages are adjusted to more closely reflect actual experience
Mortality	Pri-2012 Disability Mortality Table, with generational mortality improvement projected after year 2012 using Scale MP-2020

**Harris County Hospital District,
d/b/a Harris Health System,
A Component Unit of Harris County, Texas**

**Schedule of Changes in the System's Total OPEB Liability and Related Ratios
(Dollar amounts in thousands)**

	<u>2021</u>	<u>2020</u>	<u>2019</u>
Total OPEB liability:			
Service cost	\$ 9,895	\$ 9,424	\$ 9,746
Interest	11,990	15,195	13,820
Experience gains	(3,056)	(30,004)	-
Changes of assumptions	100,078	63,631	-
Benefit payments	<u>(16,731)</u>	<u>(16,137)</u>	<u>(20,173)</u>
Net change in total OPEB liability	102,176	42,109	3,393
Total OPEB liability – beginning	<u>486,430</u>	<u>444,321</u>	<u>440,928</u>
Total OPEB liability – ending	<u>\$ 588,606</u>	<u>\$ 486,430</u>	<u>\$ 444,321</u>
Covered employee payroll	\$ 449,724	\$ 514,871	\$ 491,810
System's total OPEB liability as a percentage of covered payroll	130.88%	94.48%	90.34%

Notes to Schedule:

This schedule is presented as of the measurement date which is as of the fiscal year-end.

In an amendment approved by the board on January 25, 2018, employees hired after June 1, 2018 are no longer eligible to participate in the OPEB.

Changes of assumptions – Change in discount rate from 4% in 2018 to 3.21% in 2019.

Changes of assumptions – In 2019, amounts reported as changes of assumptions resulted primarily from adjustments to assumed life expectancies as a result of adopting the Pri-2012 total dataset mortality table projected with Improvement Scale MP-2019 as of February 29, 2020.

Additionally, the discount rate was changed to 2.50% and the medical trend assumption was updated from 6.50% grading uniformly to 4.75% over 7 years to 7.50% grading uniformly to 6.75% over 3 years and following the Getzen model thereafter.

Changes of assumptions – In 2021, amounts reported as changes of assumptions resulted primarily from changing the mortality improvement assumption to the Improvement Scale MP-2020.

Additionally, the discount rate was changed to 1.21% and the medical trend assumption was updated from 7.50% grading uniformly to 6.75% over 3 years to 6.50% grading uniformly to 5.75% over 3 years and following the Getzen model thereafter.