Report of Independent Auditors and
Consolidated Financial Statements with
Supplemental Schedules for

Tri-City Healthcare District

June 30, 2016 and 2015

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors of
Tri-City Healthcare District

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Tri-City Healthcare District (the District), which comprise the consolidated statements of net position as of June 30, 2016 and 2015, and the related consolidated statements of revenues, expenses, changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the California Code of Regulations, Title 2, Section 1131.2, *State Controller's Minimum Audit Requirements for California Special Districts*. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Tri-City Healthcare District as of June 30, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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Other Matters

Required Supplementary Information
Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3-10 be presented to supplement the basic consolidated financial statements. Such information, although not part of the basic consolidated 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 consolidated 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.

Other Information
Our audit was conducted for the purpose of forming opinions on the consolidated financial statements that collectively comprise the District's basic financial statements. The consolidating statement of net position, June 30, 2016 and consolidating statement of revenues, expenses, and changes in net position for the year ended June 30, 2016 are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The consolidating statement of net position, June 30, 2016 and consolidating statement of revenues, expenses, and changes in net position for the year ended June 30, 2016 are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic consolidated financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America and the California Code of Regulations, Title 2, Section 1131.2, *State Controller's Minimum Audit Requirements for California Special Districts*. In our opinion, the consolidating statement of net position, June 30, 2016 and consolidating statement of revenues, expenses, and changes in net position for the year ended June 30, 2016 are fairly stated, in all material respects, in relation to the basic consolidated financial statements as a whole.

Moss Adams LLP

Irvine, California
September 19, 2016

Overview

The Tri-City Healthcare District (the "District") is a public healthcare district and is a political subdivision of the State of California (the "State") organized pursuant to Division 23 of the Health and Safety Code of the State of California. The District operates a 397-bed acute care hospital in northern San Diego County (the "County"). The "Tri-City" name represents the cities of Carlsbad, Oceanside, and Vista, the three cities which fall within its boundaries. The District was formed in 1957, and the hospital opened in 1961.

This report contains the operating results of Tri-City Medical Center and the subsidiaries in which the District owns a controlling interest. Those entities include Tri-City Medical Center Ambulatory Surgery Center Operators, LLC ("Ambulatory Surgery Center Operators"), the Tri-City Medical Center Cardiovascular Health Institute, LLC ("Cardiovascular Institute"), the Tri-City Medical Center Orthopedic Institute, LLC ("Orthopedic Institute"), the Tri-City Medical Center Neuroscience Institute, LLC ("Neuro Institute"), the Tri-City Real Estate Holding and Management Company, LLC ("Real Estate Holding and Management Company") and Tri-City Wellness, LLC ("Wellness Center").

Ambulatory Surgery Center Operators, the Cardiovascular Institute, the Orthopedic Institute, the Neuro Institute, the Real Estate Holding and Management Company and the Tri-City Wellness Center are component units that have been blended for presentation purposes. The District has determined blended presentation is appropriate for Ambulatory Surgery Center Operators as it appoints a voting majority of the governing body and its operations are an integral part of the District's mission. The District has also determined blended presentation is appropriate for the Cardiovascular Institute, the Orthopedic Institute, and the Neuro Institute as the component units provide services almost entirely to the District. The District has determined blended presentation is appropriate for the Real Estate Holding and Management Company and the Tri-City Wellness Center as management of the District has operational responsibility.

This section of the District's annual financial report presents an analysis of the District's financial performance for the years ended June 30, 2016 and 2015. All references to years refer to the fiscal year ended June 30, unless otherwise indicated. Please read this analysis in conjunction with the Report of Independent Auditors and the consolidated financial statements that follow this section.

This annual financial report includes three items:

1. Report of Independent Auditors
2. Management's Discussion and Analysis
3. Consolidated financial statements of the District, including notes that explain in more detail, some of the information in the consolidated financial statements.
4. Supplemental schedules

The District's consolidated financial statements report information using accounting methods required by the Governmental Accounting Standards Board ("GASB"). These statements contain short-term and long-term financial information about its activities.

Executive Summary

For the year ended June 30, 2016, the District reported consolidated net loss from operations of approximately $6.0 million and deficiency of revenue over expenses of approximately $1.7 million.

The 2016 deficiency of revenue over expenses by entity was as follows:

Tri-City Medical Center	$ (4,210,385)
Ambulatory Surgery Center Operators	1,709,276
Real Estate Holding and Management Company	189,295
Tri-City Wellness Center	320,475
Cardiovascular Institute	313,223
Orthopedic Institute	131,031
Neuroscience Institute	134,471
Eliminations	(280,319)
Total deficiency of revenue over expenses	$ (1,692,933)

Contributing to the 2016 results were the following significant issues:

- The District recorded revenue totaling approximately $3.5 million through the continuation of the Intergovernmental Transfer ("IGT") program. This program reimbursed the hospital for a portion of the difference between the cost of treating Medi-Cal patients and the amount reimbursed through a pre-existing Medi-Cal contract.

- The Oncology infusion practice, acquired in April 2013 by Tri-City Medical Center ("OP Infusion Center"), contributed approximately $1.6 million to excess of revenues over expenses during 2016.

- The District's strategic partnership in Ambulatory Surgery Center Operators resulted in an excess of revenues over expenses of approximately $1.7 million in fiscal 2016. Because the District owns 60% of Ambulatory Surgery Center Operators and Ambulatory Surgery Center Operators owns 52.8% of North Coast Surgery Center Ltd., the District's share of earnings was approximately $542 thousand.

- The increase in the District's revenue related to prior years' cost report settlements totaled approximately $2.8 million. Cost reports typically are finalized several years beyond the close of each fiscal year, after review by the appropriate government agency, and after all appeal rights have been exhausted. Tentative settlements occur between the end of a fiscal year and finalization of the settlement process.

- During 2016, the District recorded expenses of $6.2 million based on additional information that became known in the current year related to conditions that existed in prior periods. These items included a settlement with the Office of Inspector General for $2.2 million, legal fees associated with a trial related to a medical office building for approximately $2.6 million, and legal settlements with former employees for approximately $1.4 million. These expenses are non-recurring and the financial impact is reflected in the consolidated financial statements.

Executive Summary (continued)

The District continued or started the following initiatives which are anticipated to provide future financial benefit:

- In June 2016 the District entered into an agreement with the County of San Diego to open a Crisis Stabilization Unit ("CSU") which will provide emergency psychiatric evaluation and crisis stabilization to adults on a 24-hour, 7-day per-week basis. Crisis stabilization includes crisis intervention, medication administration, consultation with significant others and outpatient providers, and linkage and/or referral to follow-up care and community resources. Not only will the CSU provide care for patients in an appropriate setting, but will result in additional Emergency Department bed availability for those in need of emergency services. Under the new agreement, reimbursement for the care of patients in the CSU will more closely match the cost of care.

- During 2016 the District continued its efforts to finalize an exclusive affiliation agreement with University of California San Diego Health ("UC San Diego Health"). In August 2016 the agreement, designed to enhance the delivery of high quality health care to patients in North San Diego County, was executed. The agreement includes provisions for collaboration on recruiting and marketing, a dual credentialed Cardio Thoracic surgery program, and an expanded neurosurgery program under which UC San Diego Health faculty will perform neurosurgeries at TCHD. The District is taking steps to become a contracted provider under UC HealthNet Blue & Gold HMO and a provider under the Blue Shield/UC Care PPO product. See Note 15 – Subsequent Events.

- The District continued to recruit physicians to improve medical coverage for the communities it serves. The specialties recruited include family medicine, internal medicine and urology. Loans to physicians accrue interest during the draw period and during the forgiveness period. As of June 30, 2016, the physician loan balance was $5.3 million. Approximately $1.8 million was forgiven during 2016.

- In response to the need for additional obstetrics and gynecology physicians in the TCHD service area, the District opened the Radiance OB/GYN clinic in April 2016. The District owns and operates the clinic from which currently one physician and two nurse practitioners provide professional services to the community.

- In 2016 the District's Electronic Health Record ("EHR") continued to be refined in anticipation of specific application requirements for Meaningful Use Stage 3 and attestation was successfully completed for Meaningful Use Year 2, Stage 2. Special emphasis was placed on the applications for Computerized Physician Order Entry, Clinical Decision Support tools, Transition of Care Summaries, Quality Measures and the Patient Portal. A full security risk analysis was completed again this year and the public health requirements were met through TCMC's active engagement with the Immunization, Syndromic and Reportable Lab county registries.

Executive Summary (continued)

Required Consolidated Financial Statements

Consolidated Statement of Net Position – The consolidated statement of net position includes all of the District's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to the District's creditors (liabilities), and net position – the difference between assets and liabilities – of the District, and the changes thereto. The statement of net position also provides the basis for evaluating the capital structure of the District and assessing the liquidity and financial flexibility of the District.

Condensed Consolidated Statements of Net Position as of June 30, 2016 and 2015 (In Thousands)

	2016	2015
ASSETS		
Current assets	$ 119,253	$ 124,980
Capital assets - net	108,307	109,059
Non-current assets	21,453	21,763
Total	$ 249,013	$ 255,802
LIABILITIES AND NET POSITION		
Current liabilities	$ 117,444	$ 121,750
Long-term debt - net of current portion	29,464	28,358
Workers' compensation and comprehensive liability - net of current portion	7,672	7,966
Total liabilities	154,580	158,074
Net investment in capital assets	74,691	77,480
Unrestricted	18,310	18,545
Restricted, non-expendable	1,432	1,703
Total net position	94,433	97,728
Total	$ 249,013	$ 255,802

2016 Analysis of Changes in the Consolidated Statement of Net Position

- Current assets totaling approximately $119.3 million in 2016, represents a decrease of $5.7 million from the prior year. Included in current assets is a decrease of approximately $4.5 million in cash and cash equivalents, and a decrease in net estimated third-party payor settlements of approximately $2.0 million.

- Cash on hand and unused availability from the revolving credit facility provide liquidity to the District. Cash and cash equivalents totaled approximately $11.2 million and the unused available revolving line of credit was approximately $20.5 million at June 30, 2016.

- Net estimated third-party payor settlements decreased approximately $2.0 million primarily due to receipts pertaining to the IGT Program, Meaningful Use, and prior year cost report settlements. The majority of third-party settlements receivable at June 30, 2016 pertains to current year cost report estimates.

- Capital assets, net of accumulated depreciation, decreased approximately $752 thousand, and totaled approximately $108.3 million as of June 30, 2016. A combination of cash payments and equipment financing were utilized to acquire approximately $10.5 million in equipment, software, and other capital improvement projects during the year.

- Current liabilities, totaling approximately $117.4 million at June 30, 2016 reflects a decrease of approximately $4.3 million compared to June 30, 2015. Long-term debt totaled approximately $29.5 million at year end.

- Workers' compensation and comprehensive liability insurance reserves classified as long term liabilities decreased by $295 thousand, based on actuarial analyses of open claims and estimates of claims incurred but not yet reported ("IBNR"). Actuarial studies are commissioned twice each year to determine the potential liabilities and required reserves.

Condensed Consolidated Statements of Revenues, Expenses, and Changes in Net Position for the Years Ended June 30, 2016 and 2015 (In Thousands)

	2016	2015
Operating revenue	$ 334,596	$ 337,195
Operating expenses	340,625	336,771
(Loss) Income from operations	(6,029)	424
Non-operating revenue	4,336	4,010
(Deficiency) Excess of revenue over expenses	(1,693)	4,434
Minority interest distributions - net	(1,601)	(1,330)
Change in net position	(3,294)	3,104
Beginning net position	97,728	94,624
Ending net position	$ 94,434	$ 97,728
Average daily census	191.9	191.0
Emergency room visits	65,828	70,090

2016 Analysis of the Consolidated Statement of Revenues, Expenses and Changes in Net Position

- The District experienced a slight increase in inpatient volume in 2016. Total average daily census was 192 for the current year compared to 191 in the prior year. Total hospital outpatient visits decreased slightly by approximately 1% compared to 2015. Emergency treat and release visits decreased approximately 6.1%, while OP Specialty Unit visits increased approximately 21.2% in 2016.

- Operating revenues decreased by approximately $2.6 million in 2016 compared to 2015. This decrease is due to multiple factors including a decrease in the number of surgeries, decreased outpatient volumes and payor mix changes. Net revenue in both years was reduced by sequestration, resulting in a 2% reduction in Medicare reimbursement, approximating $2.4 million for both years ended June 30, 2016 and 2015.

2016 Analysis of the Consolidated Statement of Revenues, Expenses and Changes in Net Position (continued)

- Operating expenses, which include patient care expenses and overhead and administrative expenses, increased approximately $3.9 million. The largest single increase was experienced in salaries and related expenses. Although salaries and related expenses increased by approximately $3.0 million, salaries and related expenses as a percentage of total operating revenue remained fairly consistent at approximately 57% in 2016 compared to approximately 56% in 2015.

- Non-operating income and expense is comprised of the District's share of property tax revenue collected by the County of San Diego, interest earned on invested monies, interest expense, and other non-operating items. The resulting net non-operating revenue totaled approximately $4.3 million in 2016 compared to approximately $4.0 million in 2015.

Statement of Cash Flows – The Statement of Cash Flows reports cash receipts, cash payments, and net changes in cash resulting from operating, noncapital and capital financing, and investing activities.

	Years Ended June 30, 2016	2015
Net cash provided by (used in)		
Operating activities	$ 3,061	$ 9,586
Noncapital financing activities	6,299	6,865
Capital and related financing activities	(13,934)	(14,713)
Investing activities	40	45
Net change in cash and cash equivalents	(4,534)	1,783
Beginning cash and cash equivalents	15,711	13,928
Ending cash and cash equivalents	$ 11,177	$ 15,711

Cash flows arise from operating income adjusted for noncash expenditures such as depreciation expense and bad debt expense ("operating activities"), changes in investments and interest income received on investments ("investing activities"), purchase of new capital assets and payments of interest and principal on debt ("capital and related financing activities"), and county tax revenues ("noncapital financing activities").

2016 Analysis of the Consolidated Statement of Cash Flows

Cash and cash equivalents totaled approximately $11.2 million at fiscal 2016 year end, compared to approximately $15.7 million at fiscal 2015 year end. Net cash provided by operating activities in 2016 decreased approximately $6.5 million and cash provided by noncapital financing activities in 2016 decreased by approximately $565 thousand. The $3.3 million payment to the DOJ for settlement of the self-disclosure issue from prior years contributed to the decrease in cash. Cash used in capital and related financing activities decreased approximately $779 thousand from 2015 to 2016. The District received approximately $1.3 million from the Foundation and Auxiliary during 2016.

2016 Capital Assets

During 2016 the District invested approximately $10.5 million in new equipment and building improvements. Major acquisitions during 2016 included the renovation of an angiography lab, continued development of analytics tools to aid in data-driven decision making, wireless monitoring equipment for the neonatal intensive care unit, the purchase of patient mattresses, pharmacy carousels which provide secure automated storage for medications, several hospital remodel projects and a number of surgical equipment upgrades.

Capital lease payments were made timely. More detailed information about the District's debt is presented in Notes 7 and 8 to the consolidated financial statements.

Finance Contact

The District's consolidated financial statements are designed to present users with a general overview of the District's finances and to demonstrate the District's accountability. If you have any questions about the report or need additional financial information, please contact the Chief Financial Officer, Tri-City Healthcare District, 4002 Vista Way, Oceanside, California 92056.

ASSETS

	JUNE 30, 2016	JUNE 30, 2015
CURRENT ASSETS		
Cash and cash equivalents	$ 11,176,800	$ 15,711,112
Restricted cash and investments	51,366,000	51,418,000
Patient accounts receivable - net of estimated uncollectible accounts of $18,474,430 and $23,096,486 in 2016 and 2015, respectively	42,396,754	43,587,397
Other receivables	2,647,024	1,972,226
Supplies inventory	8,479,210	7,401,180
Prepaid expenses and other assets	2,956,557	2,691,937
Estimated third-party payor settlements	230,191	2,198,603
Total current assets	119,252,536	124,980,455
NON-CURRENT CASH AND INVESTMENTS		
Board-designated	394,050	392,638
CAPITAL ASSETS - net	108,306,915	109,058,505
OTHER ASSETS		
Notes receivable	5,343,659	5,456,244
Other	15,716,139	15,913,884
Total other assets	21,059,798	21,370,128
TOTAL	$ 249,013,299	$ 255,801,726

See accompanying notes.

LIABILITIES AND NET POSITION

	JUNE 30, 2016	JUNE 30, 2015
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	$ 37,033,841	$ 40,043,691
Accrued payroll and related expenses	19,824,036	21,064,762
Current maturities of long-term debt	4,151,552	3,221,570
Short-term debt	55,479,469	56,430,432
Other current liabilities	954,752	989,459
Total current liabilities	117,443,650	121,749,914
LONG-TERM DEBT - net of current portion	29,463,883	28,357,448
WORKERS' COMPENSATION AND COMPREHENSIVE LIABILITY - net of current portion	7,671,667	7,966,244
Total liabilities	154,579,200	158,073,606
NET POSITION		
Net investment in capital assets	74,691,480	77,479,485
Unrestricted	18,310,367	18,545,334
Restricted, non-expendable	1,432,253	1,703,301
Total net position	94,434,100	97,728,120
TOTAL	$ 249,013,299	$ 255,801,726

See accompanying notes.

TRI-CITY HEALTHCARE DISTRICT
CONSOLIDATED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	YEARS ENDED JUNE 30,	
	2016	2015
REVENUE		
Net patient service revenue	$ 309,438,940	$ 311,993,429
Premium revenue	18,734,093	17,893,104
Other revenue	6,423,150	7,308,188
Total operating revenue	334,596,183	337,194,721
EXPENSES		
Salaries and related expenses	192,330,034	189,371,461
Supplies	69,565,938	71,529,950
Purchased services	17,449,771	18,147,963
Depreciation and amortization	11,157,771	11,724,273
Other operating expense	19,924,006	18,336,719
Professional and medical fees	16,655,002	14,646,849
Maintenance, rent & utilities	13,542,381	13,013,256
Total operating expenses	340,624,903	336,770,471
(LOSS) INCOME FROM OPERATIONS	(6,028,720)	424,250
NON-OPERATING REVENUE (EXPENSE)		
District tax revenue	8,957,499	8,469,927
Interest income	247,462	195,950
Interest expense	(3,604,253)	(4,229,852)
Other non-operating expense	(1,264,921)	(426,307)
Total non-operating revenue	4,335,787	4,009,718
(DEFICIENCY) EXCESS OF REVENUE OVER EXPENSES	(1,692,933)	4,433,968
MINORITY INTEREST DISTRIBUTIONS - NET	(1,601,087)	(1,329,846)
Changes in net position	(3,294,020)	3,104,122
NET POSITION - Beginning of year	97,728,120	94,623,998
NET POSITION - End of year	$ 94,434,100	$ 97,728,120

TRI-CITY HEALTHCARE DISTRICT
CONSOLIDATED STATEMENTS OF CASH FLOWS

	YEARS ENDED JUNE 30, 2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from patients, insurers, and other payors	$ 330,657,290	$ 331,219,815
Payments to vendors	(140,480,564)	(136,172,665)
Payments for salaries, wages, and related benefits	(193,570,760)	(187,062,668)
Other receipts and payments	6,454,784	1,601,656
Net cash provided by operating activities	3,060,750	9,586,138
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Minority interest distributions, net	(1,601,087)	(1,329,846)
Receipt of District taxes	8,957,499	8,469,927
Other non-operating expense	(1,057,076)	(275,377)
Net cash provided by noncapital financing activities	6,299,336	6,864,704
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition of capital assets	(5,880,765)	(6,402,951)
Proceeds from revolving line of credit	327,286,467	366,335,846
Principal repayments on revolving line of credit	(328,237,431)	(367,280,639)
Proceeds from other debt	956,352	1,050,624
Principal repayments on other debt	(4,454,385)	(4,185,936)
Interest payments on debt	(3,604,253)	(4,229,852)
Net cash used in capital and related financing activities	(13,934,015)	(14,712,908)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest on investments	39,617	45,020
Net cash provided by investing activities	39,617	45,020
NET CHANGE IN CASH AND CASH EQUIVALENTS	(4,534,312)	1,782,954
CASH AND CASH EQUIVALENTS - Beginning of year	15,711,112	13,928,158
CASH AND CASH EQUIVALENTS - End of year	$ 11,176,800	$ 15,711,112

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

	2016	2015
Capital assets acquired through long-term debt	$ 4,529,271	$ -

See accompanying notes.

RECONCILIATION OF (LOSS) INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES

	YEARS ENDED JUNE 30, 2016	YEARS ENDED JUNE 30, 2015
(Loss) income from operations	$ (6,028,720)	$ 424,250
Adjustments to reconcile (loss) income from operations to net cash provided by operating activities:		
Provision for bad debt	36,890,483	48,397,226
Depreciation and amortization	11,157,771	11,724,273
Changes in net assets and liabilities		
Patient accounts receivable	(35,699,840)	(48,898,282)
Other receivables	(674,798)	700,416
Other - net	(301,981)	(5,964,168)
Accounts payable and accrued liabilities	(3,009,850)	(240,292)
Accrued payroll and related expenses	(1,240,726)	2,308,793
Estimated third-party payor settlements	1,968,412	1,133,922
Net cash provided by operating activities	$ 3,060,750	$ 9,586,138

See accompanying notes.

Note 1 – Organization

Organization – Tri-City Healthcare District (the "District" or "TCMC") is a political subdivision of the state of California organized as a special district. The District provides comprehensive medical services at its facility located in Oceanside, California. The consolidated financial statements of the District include the accounts of the District, Tri-City Medical Center ASC Operators, LLC ("ASCO"), North Coast Surgery Center Ltd. ("NCSC"), the Cardiovascular Health Institute, LLC ("CVI"), the Orthopedic Institute, LLC ("Ortho"), the Neuroscience Institute, LLC ("Neuro"), Tri-City Real Estate Holding and Management Co, LLC ("REHM") and Tri-City Wellness, LLC ("Tri-City Wellness").

ASCO, NCSC, CVI, Ortho, Neuro, REHM and Tri-City Wellness are component units that have been blended for presentation purposes. The District owns a 60% interest in ASCO, which provides management services to NCSC. ASCO owns a 52.8% interest in NCSC. NCSC provides outpatient surgical services to the surrounding communities of Oceanside, California. The District has determined blended presentation is appropriate as it appoints a voting majority of ASCO's governing body. The District owns 61.4% of CVI, 50% of Ortho and 68% of Neuro. The Institutes were established to align the goals of independent physician practices and specialty services with the goals of the hospital. Key goals are to improve quality outcome reporting and improve financial and operational performance of the respective service lines. The District has determined blended presentation is appropriate for CVI, Ortho, and Neuro as the component units provide services almost entirely to the District. The District owns 99% of REHM. The District has determined blended presentation is appropriate for REHM as management of the District has operational responsibility for REHM. The District owns 99.9% of Tri-City Wellness. The District has determined blended presentation is appropriate for Tri-City Wellness as management of the District has operational responsibility for Tri-City Wellness. All intercompany transactions have been eliminated in the District's consolidated financial statements.

Note 2 – Summary of Significant Accounting Policies

Basis of presentation – The consolidated financial statements have been prepared in accordance with the applicable provisions of the American Institute of Certified Public Accountants' Audit and Accounting Guide, *Health Care Organizations*, and pronouncements of the Governmental Accounting Standards Board ("GASB") and the California Code of Regulations, Title 2, Section 1131, *State Controller's Minimum Audit Requirements and Reporting Guidelines for California Special Districts*. The District uses proprietary (enterprise) fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

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

Note 2 – Summary of Significant Accounting Policies (continued)

Cash equivalents – For purposes of the consolidated financial statements, the District considers highly liquid debt instruments (excluding non-current cash and investments) purchased with a maturity of three months or less to be cash equivalents.

Term loan collateral – The term loan is fully collateralized by restricted cash of $51.0 million at June 30, 2016 and 2015. See Note 7 – Short-Term Debt. The custodians of the restricted cash are the financial institutions that have provided the term loan. Term loan collateral is included within restricted cash in the consolidated statements of net position at June 30, 2016 and 2015.

Investments – Investments are reported at fair value, as determined by quoted market prices, in the statements of net position, and all investment income or losses, including changes in the fair value of investments, are reported in non-operating income (expense) in the statements of revenues, expenses, and changes in net position.

Supplies inventories – Supplies inventories are reported at the lower of cost (first-in, first-out) or market value.

Goodwill – Goodwill represents the excess of purchase price of an acquired business over the net tangible and identifiable intangible assets acquired and liabilities assumed in connection with the acquisition of the oncology infusion practice in 2013. At June 30, 2016 and 2015, goodwill associated with this transaction was approximately $4.6 million, which is included in other assets in the consolidated statements of net position. The District evaluates goodwill for impairment at least annually or whenever events or changes in circumstances require an interim impairment assessment. The District compares the fair value of each reporting unit to its carrying amount to determine if there is potential goodwill impairment. If the fair value of a reporting unit is less than its carrying value, an impairment loss is recorded to the extent that the fair value of the goodwill within the reporting unit is less than the carrying value of its goodwill. Management determined that there was no impairment of goodwill as of June 30, 2016 and 2015.

Capital assets – Capital assets are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful life of each class of depreciable asset (the shorter of the estimated useful life or the lease term for leasehold improvements) as follows:

Land improvements	15 years
Buildings and building improvements	10-40 years
Leasehold improvements	3-15 years

Note 2 – Summary of Significant Accounting Policies (continued)

Capital assets are evaluated for impairment when events or changes in circumstances suggest that the service utility of the capital asset may have significantly and unexpectedly declined. Capital assets are considered impaired if both the decline in service utility of the capital asset is large in magnitude and the event or change in circumstance is outside the normal life cycle of the capital asset. Such events or changes in circumstances that may be indicative of impairment include evidence of physical damage, enactment or approval of laws or regulations or other changes in environmental factors, technological changes or evidence of obsolescence, changes in the manner or duration of use of a capital asset, and construction stoppage. The determination of the impairment loss is dependent upon the event or circumstance in which the impairment occurred. Impairment losses, if any, are recorded in the statements of revenues, expenses, and changes in net position. No impairment losses are recorded in the years ended June 30, 2016 and 2015.

Net position – Net position of the District is classified in four components. "Net investment in capital assets" consists of capital assets, net of accumulated depreciation and is reduced by the balances of any outstanding borrowing used to finance the purchase or construction of those assets. "Unrestricted" net position is the remaining net position that does not meet the definition of net investment in capital assets or restricted. "Restricted" net position is non-capital net position required to be used for a particular purpose, as specified by contributors external to the District. "Restricted, nonexpendable" net position includes the net position of ASCO, CVI, Ortho, Neuro, REHM and Tri-City Wellness not owned by the District.

Grants and contributions – From time to time, the District receives grants and contributions from individuals or private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenues. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses.

Operating revenues and expenses – The District's statements of revenues, expenses, and changes in net position distinguish between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the District's principal activity. Operating expenses include all expenses incurred to directly provide health care services. Non-operating income and expenses consist of those revenues and expenses that result from non-exchange transactions, such as District taxes, financing costs, interest expense, and investment income.

Note 2 – Summary of Significant Accounting Policies (continued)

Net patient service revenue – Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payers. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined. The District estimates net collectible accounts receivable and the corresponding impact on net patient services revenue by applying historical collection realization percentages to outstanding gross accounts receivable by payor class. Normal estimation differences between subsequent cash collections on patient accounts receivable and net patient accounts receivable estimated in the prior year are reported as adjustments to net patient service revenue during the collection period. Subsequent collections through July 2016 have exceeded net patient accounts receivable reflected as of June 30, 2015 by approximately $4.9 million, and have exceeded net patient accounts receivable reflected as of June 30, 2014 by approximately $3.7 million.

Premium revenue – The District has agreements with various health maintenance organizations ("HMOs") to provide medical services to subscribing participants. Under these agreements, the District receives monthly capitation payments based on the number of each HMO's participants, regardless of services actually performed by the District. The District recognizes premium revenue in the period the District is obligated to provide services, which is generally in the month capitation payments are received. In addition, the HMOs make fee-for-service payments to the District for certain covered services based upon discounted fee schedules. Under some of these agreements, the District also participates in shared-risk pools with medical groups, through which it could receive additional reimbursement or pay additional amounts to the medical groups. In conjunction with the risk pools, the District estimates incurred but not reported ("IBNR") claims for medical services provided to patients at other facilities. See Note 13 – Commitments and Contingencies.

IBNR liabilities of approximately $1.5 million and $1.9 million are included in accounts payable and accrued liabilities in the accompanying consolidated statements of net position as of June 30, 2016 and 2015, respectively.

Property taxes – The District receives financial support from property taxes. These funds are used to support operations. Property taxes are levied annually by the County of San Diego (the "County") on behalf of the District and are intended to finance the District's activities. The County's fiscal year is from July 1 through June 30. Amounts of tax levied are based on assessed property values as of the first day of January proceeding the fiscal year for which the taxes are levied. See Note 3 – Non-operating Revenue.

Income taxes – The District is a governmental subdivision of the state of California and is exempt from federal income and state franchise taxes.

Note 2 – Summary of Significant Accounting Policies (continued)

Compensated absences – The District's benefits-eligible employees earn vacation leave at varying rates based upon qualifying-service hours. Employees may accumulate vacation leave up to a specified maximum. Accrued vacation leave is paid to the employee upon termination of employment or upon conversion to non-benefits-eligible status. The estimated amount of vacation leave payable to employees is reported as a current liability in the accompanying consolidated statements of net position of approximately $9.4 million and $8.7 million as of June 30, 2016 and 2015, respectively. Sick time is also earned at a specific rate per qualified-service hour. However, no payment is made for accrued sick time when employment is terminated.

Note 3 – Patient Service Revenue, Third-Party Reimbursement Programs and Non-Operating Revenue

The District renders services to patients under contractual arrangements with the Medicare and Medi-Cal programs and various HMOs and preferred provider organizations ("PPOs"). The Medicare program generally pays the District a prospectively determined rate per discharge for services rendered to Medicare inpatients. Additionally, Medicare reimburses the District for certain capital related costs and psychiatric services on the basis of costs incurred.

Senate Bill 853 added section 14105.28 to the Welfare and Institution Code. This section mandated the design and implementation of a new payment methodology for hospital inpatient services provided to Medi-Cal beneficiaries based upon Diagnosis Related Groups ("DRGs"). The DRG case-based reimbursement methodology replaced the previous per diem payment method for all private hospitals with admissions on or after July 1, 2013, and for non-designated public hospitals with admissions on or after January 1, 2014. A per diem reimbursement methodology is still used for rehabilitative services and behavioral health services. Revenue from the Medicare and Medi-Cal programs accounted for approximately 65% and 66% of the District's gross patient service revenue for the years ended June 30, 2016 and 2015, respectively.

The District is reimbursed for serving a disproportionate share of low income patients, reimbursable Medicare bad debt and certain other items at a tentative rate with final settlement determined after the District's submission of annual cost reports and audits thereof by State and Federal agencies and their intermediaries. Cost reports for the Medicare programs have been final settled for all years through 2013. Results of cost report settlements, as well as the District's estimates for settlements, of all fiscal years through 2016 are reflected in the accompanying consolidated financial statements.

Estimated net third-party settlements consisted of a net receivable of approximately $230 thousand and $2.2 million as of June 30, 2016 and 2015, respectively. During fiscal year 2016, the District settled various prior-year cost reports, appeal issues and adjusted prior-year settlement estimates. Prior year settlements and changes in estimates resulted in approximately $2.8 million and $2.1 million of additional net patient service revenue in the years ended June 30, 2016 and 2015, respectively, and are included in net patient service revenue in the accompanying consolidated statements of revenue, expenses, and changes in net position.

Note 3 – Patient Service Revenue, Third-Party Reimbursement Programs and Non-Operating Revenue (continued)

The District has also entered into payment agreements with certain commercial insurance carriers, HMOs, and PPOs. The basis for payment to the District under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

The District grants credit without collateral to its patients, most of who are local residents and are insured under third-party payor agreements. The mix of net receivables from patients and third-party payors as of June 30, 2016 and 2015 were as follows:

	2016	2015
HMO/PPO	35 %	34 %
Medicare plans	32	36
Medi-Cal plans	17	17
Others	16	13
Total	100 %	100 %

Non-operating revenue includes District tax revenue and other non-patient service revenue. District tax revenue totaled approximately $9.0 million and $8.5 million for the years ended June 30, 2016 and 2015, respectively. Other non-operating income includes approximately $1.3 million and $1.0 million in donations from the Foundation and Auxiliary in 2016 and 2015, respectively.

Note 4 – Cash and Cash Equivalents and Investments

The State of California Government Code (the "Code") generally authorizes the District to invest unrestricted and Board-designated assets in obligations of the U.S. Treasury and certain U.S. government agencies, obligations of the state of California and local government entities, bankers' acceptances, commercial paper, certificates of deposit, repurchase agreements, and mortgage securities. Certain investments may be purchased only in limited amounts, as defined in the Code.

The California State Treasurer's Office makes available the Local Agency Investment Fund ("LAIF") through which local governments may pool investments. Each governmental entity may invest up to $40 million in the fund. Investments in the LAIF are highly liquid, as deposits can be converted to cash within 24 hours without loss of interest. The District is a voluntary participant in the LAIF. The fair value of the District's investments in the LAIF is reported in the accompanying consolidated financial statements based on the District's pro rata share of the fair value provided by the LAIF for the entire LAIF portfolio. As of June 30, 2016 and 2015 the District held approximately $394 thousand and $393 thousand in LAIF, respectively.

Note 4 – Cash and Cash Equivalents and Investments (continued)

The District has $51.0 million held as collateral for a $51.0 million term loan, which is held in pledged nonnegotiable certificate of deposit accounts classified as restricted cash and investments at June 30, 2016 and 2015 in the accompanying consolidated statements of net position. The nonnegotiable certificates of deposits have redemption terms that do not consider market rates and are reported using a cost-based measure.

There are many factors that can affect the value of investments. Some, such as credit risk, custodial credit risk, and concentration of credit risk and interest rate risk, may affect both equity and fixed income securities. Equity and debt securities respond to such factors as economic conditions, individual company earnings performance, and market liquidity, while fixed income securities are particularly sensitive to credit risks and changes in interest rates.

Credit risk – Fixed income securities are subject to credit risk, which is the chance that an issuer will fail to pay interest or principal in a timely manner or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. Certain fixed income securities, including obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have credit risk. The District invests primarily in obligations of the U.S. government.

Concentration of credit risk – Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers, thereby exposing the District to greater risks resulting from adverse economic, political, regulatory, geographic, or credit developments. Investments issued or guaranteed by the U.S. government and investments in external investment pools, such as LAIF, are not considered subject to concentration of credit risk. In accordance with state law, no more than 5% of total investments may be invested in the securities of any one issuer, except obligations of the U.S. government, no more than 10% may be invested in any one mutual fund, and no more than 30% may be invested in bankers' acceptances of any one commercial bank.

Custodial credit risk – deposits – Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a policy for custodial credit risk. As of June 30, 2016 and 2015, the District's bank balances totaled approximately $62.5 million and $67.1 million, respectively, and were not exposed to custodial credit risk, as the uninsured deposits are with financial institutions which are individually required by state law to have government deposits collateralized at a rate of 110% of the deposits. Such collateral is considered to be held in the District's name.

Custodial credit risk – investments – District policy requires that all investments be insured or registered, or be held by the District's agent in the agent's nominee name, with subsidiary records listing the District as the legal owner. For these reasons, the District is not exposed to custodial credit risk for its investments.

Note 4 – Cash and Cash Equivalents and Investments (continued)

Interest rate risk – Interest rate risk is the risk that the value of fixed income securities will decline due to increasing interest rates. The terms of a debt investment may cause its fair value to be highly sensitive to interest rate changes. As a means of limiting its exposure to fair value losses arising from increasing interest rates, the District's investment policy, as per statutory requirements, limits the term of any investment to a maturity not exceeding five years.

The carrying amount of cash and investments are included in the following statements of net position captions at June 30:

	2016	2015
Cash and cash equivalents	$ 11,176,800	$ 15,711,112
Restricted cash and investments		
Nonnegotiable certificates of deposit	51,366,000	51,418,000
Board-designated	394,050	392,638
Total	$ 62,936,850	$ 67,521,750

Note 5 – Capital Assets

Capital assets as of June 30 consisted of the following:

2016	Beginning Balance June 30, 2015	Additions	Deletions	Transfers	Ending Balance June 30, 2016
Land and land improvements	$ 19,877,710	$ -	$ -	$ -	$ 19,877,710
Buildings and improvements	203,288,364	125,024	-	1,405,360	204,818,748
Equipment	151,516,634	2,969,776	(201,702)	920,022	155,204,730
	374,682,708	3,094,800	(201,702)	2,325,382	379,901,188
Assets under lease	3,907,587	4,529,271	-	-	8,436,858
Less accumulated depreciation and amortization	(271,704,580)	(11,125,576)	77,042	-	(282,753,114)
Construction in progress	2,172,790	2,874,575	-	(2,325,382)	2,721,983
Total capital assets	$ 109,058,505	$ (626,930)	$ (124,660)	$ -	$ 108,306,915

2015	Beginning Balance June 30, 2014	Additions	Deletions	Transfers	Ending Balance June 30, 2015
Land and land improvements	$ 19,877,710	$ -	$ -	$ -	$ 19,877,710
Buildings and improvements	200,915,689	187,075	-	2,185,600	203,288,364
Equipment	142,397,349	2,869,310	-	6,249,975	151,516,634
	363,190,748	3,056,385	-	8,435,575	374,682,708
Assets under lease	9,244,706	-	-	(5,337,119)	3,907,587
Less accumulated depreciation and amortization	(259,935,809)	(11,768,771)	-	-	(271,704,580)
Construction in progress	1,880,182	3,391,064	-	(3,098,456)	2,172,790
Total capital assets	$ 114,379,827	$ (5,321,322)	$ -	$ -	$ 109,058,505

Note 6 – Other Assets

Other assets consisted of the following as of June 30:

	2016	2015
Goodwill	$ 4,629,430	$ 4,629,430
Medical office building deposits	9,704,692	9,704,692
Other	1,382,017	1,579,762
Total	$ 15,716,139	$ 15,913,884

Note 6 – Other Assets (continued)

As of June 30, 2016 and 2015, approximately $9.7 million is reflected in other assets in the accompanying consolidated statements of net position with $5 million pertaining to payments to the developer of an on-campus medical office building and $4.7 million to the State of California Treasurer related to eminent domain proceedings to acquire an on-campus medical office building. Claims have been made by the developer and claims have been made by the District regarding the medical office building. In July 2014, the District commenced eminent domain proceedings to acquire the medical office building and accordingly deposited approximately $4.7 million during the year ended June 30, 2015 with the State of California Treasurer. In June 2016, a jury verdict was returned in this matter. See Note 13 – Commitments and Contingencies.

Note 7 – Short-Term Debt

Term loan – In April 2012, the District replaced its existing term loan with a new term loan with an initial maturity date of June 28, 2013. The new term loan maintained the existing principal outstanding of $51.0 million and existing collateral of $51.0 million with new lenders. The term loan agreement was amended extending the maturity date to December 31, 2016.

Line of credit – In July 2013, a new revolving line of credit was obtained from Mid Cap, LLC. The amount available under this new line of credit is up to $25.0 million, subject to a borrowing base calculation, as defined within the Credit and Security Agreement. The interest rate is the London Interbank Offered Rate ("LIBOR") plus 3.50% subject to a LIBOR floor of 1%. The initial term of this line of credit was three years. The revolving line of credit agreement was amended, extending the term maturity date to August 31, 2017. The borrowings on the credit facility are fully collateralized by certain assets of the District.

The District's revolving line of credit facility and term loan are subject to compliance with certain debt covenants, including restrictions on additional indebtedness, maximum debt to capitalization ratio, and a minimum fixed charge coverage ratio. The District is in compliance with debt covenants included in the amended revolving line of credit.

Note 7 – Short-Term Debt (continued)

A schedule of changes in the District's short-term debt as of June 30 is as follows:

2016	Beginning Balance	Additions	Payments	Ending Balance
Term loan	$ 51,000,000	$ -	$ -	$ 51,000,000
Line of credit	5,430,432	327,286,467	(328,237,431)	4,479,469
Total short-term debt	$ 56,430,432	$ 327,286,467	$ (328,237,431)	$ 55,479,469

2015	Beginning Balance	Additions	Payments	Ending Balance
Term loan	$ 51,000,000	$ -	$ -	$ 51,000,000
Line of credit	6,375,225	366,335,846	(367,280,639)	5,430,432
Total short-term debt	$ 57,375,225	$ 366,335,846	$ (367,280,639)	$ 56,430,432

Note 8 – Long-Term Debt

The terms and due dates of the District's long-term debt are as follows:

- REHM term note, interest rate of 3.25%, with principal balance outstanding of approximately $771 thousand and $821 thousand at June 30, 2016 and 2015, respectively. Principal payments of approximately $4 thousand plus interest are due monthly commencing December 2011 with the remaining aggregate unpaid amount due December 2016. The note is collateralized by certain real estate of REHM.

- REHM term note, interest rate of 3.50%, with principal balance outstanding of approximately $550 thousand and $650 thousand at June 30, 2016 and 2015, respectively. Principal payments of approximately $8 thousand plus interest are due monthly commencing January 2012 with the remaining aggregate unpaid amount due December 2016. The note is collateralized by certain real estate of REHM.

- Wellness Center Term loan, interest rate of LIBOR plus 6.0% subject to a LIBOR floor of 0.75%, with principal balance outstanding of approximately $25.2 million and $25.7 million at June 30, 2016 and 2015, respectively. Principal and interest payments of approximately $185 thousand are due monthly with the remaining aggregate unpaid amount due August 31, 2017. The note is fully collateralized by certain real estate of Tri-City Wellness, LLC.

Note 8 – Long-Term Debt (continued)

- Bank of the West note payable, interest rate of 2.89%, with principal balance outstanding of approximately $225 thousand and $444 thousand at June 30, 2016 and 2015, respectively. Principal and interest payments of approximately $19 thousand are due monthly commencing June 2012 with the remaining aggregate unpaid amount due June 2017. The note is collateralized by certain capital assets of the District.

- Bank of the West note payable, interest rate of 2.91%, with principal balance outstanding of approximately $294 thousand and $483 thousand at June 30, 2016 and 2015, respectively. Principal and interest payments of approximately $17 thousand are due monthly commencing January 2013 with the remaining aggregate unpaid amount due December 2017. The note is collateralized by certain capital assets of the District.

- Bank of the West note payable, interest rate of 2.95%, with principal balance outstanding of approximately $682 thousand and $1.0 million at June 30, 2016 and 2015, respectively. Principal and interest payments of approximately $30 thousand are due monthly commencing June 2015 with the remaining aggregate unpaid amount due June 2019. The note is collateralized by certain capital assets of the District.

- Bank of the West note payable, interest rate of 3.12%, with principal balance outstanding of approximately $1.4 million at June 30, 2016. Principal and interest payments of approximately $39 thousand are due monthly commencing July 2016 with the remaining aggregate unpaid amount due June 2019. The note is collateralized by certain capital assets of the District.

- Various capital equipment leases with interest rates varying between 2.31% and 6.40%. Principal and interest payments due monthly commencing various dates and expiring on various dates ranging from August 2016 through April 2021. Principal balances due totaled approximately $4.5 million and $1.4 million as of June 30, 2016 and 2015, respectively.

Note 8 – Long-Term Debt (continued)

A schedule of changes in the District's long-term debt (including current portion) as of June 30 is as follows:

2016	Beginning Balance	Additions	Payments	Ending Balance	Due Within 1 Year
REHM notes payable	$ 1,470,833	$ -	$ (150,000)	$ 1,320,833	$ 1,320,833
Wellness Center term loan	25,705,441	-	(476,545)	25,228,896	511,960
Bank of the West notes payable	1,950,189	1,349,638	(748,808)	2,551,019	1,206,924
Promissory note payable (infusion)	1,027,775	-	(1,027,775)	-	-
Total long-term debt	30,154,237	1,349,638	(2,403,128)	29,100,747	3,039,717
Capital lease obligations	1,424,780	4,132,130	(1,042,222)	4,514,688	1,111,835
Total long-term debt	$ 31,579,017	$ 5,481,768	$ (3,445,350)	$ 33,615,435	$ 4,151,552

2015	Beginning Balance	Additions	Payments	Ending Balance	Due Within 1 Year
REHM notes payable	$ 1,620,833	$ -	$ (150,000)	$ 1,470,833	$ 150,000
Wellness Center term loan	26,150,965	-	(445,524)	25,705,441	420,580
Bank of the West notes payable	1,323,894	1,050,625	(424,330)	1,950,189	748,808
Promissory note payable (infusion)	2,208,691	-	(1,180,916)	1,027,775	1,027,775
Other	3,813	-	(3,813)	-	-
Total long-term debt	31,308,196	1,050,625	(2,204,583)	30,154,238	2,347,163
Capital lease obligations	3,406,134	-	(1,981,353)	1,424,780	874,408
Total long-term debt	$ 34,714,330	$ 1,050,625	$ (4,185,936)	$ 31,579,018	$ 3,221,570

A schedule, by year, of future minimum payments under long-term debt and capital lease obligations as of June 30, 2016, is as follows:

Years Ending June 30,	Principal	Interest	Total
2017	$ 4,151,552	$ 1,905,181	$ 6,056,733
2018	26,556,787	402,351	26,959,138
2019	1,411,416	76,796	1,488,212
2020	865,083	38,234	903,317
2021	630,597	9,079	639,676
Total	$ 33,615,435	$ 2,431,641	$ 36,047,076

Note 8 – Long-Term Debt (continued)

Assets acquired through capital leases as of June 30are as follows:

	2016	2015
Equipment under capital lease	$ 8,436,860	$ 3,907,588
Accumulated amortization	(3,560,836)	(2,492,988)
Total	$ 4,876,024	$ 1,414,600

Note 9 – Retirement Plans

The District has a contributory money accumulation pension plan ("MAPP") covering substantially all employees, under which benefits are limited to amounts accumulated from total contributions. As of June 30, 2016, there were a total of 1,292 plan members, including retirees. Active plan members are required to contribute 2% of covered salary. The District is required to contribute 6% of annual covered payroll. Plan provisions and contribution requirements are established and may be amended by the Board. The District's contribution expense related to the MAPP totaled approximately $6.0 million and $6.1 million for the years ended June 30, 2016 and 2015, respectively.

Employees are immediately vested in their own contributions and earnings and become vested in the Employer contributions and earnings according to a five year vesting schedule. Non-vested employer contributions are forfeited upon termination of employment. The forfeitures are used to reduce employer contributions under the Plan. For the years ended June 30, 2016 and 2015, forfeitures reduced the District's expenses and contributions under the Plan by approximately $96 thousand and $224 thousand, respectively.

Since 1983, the District has sponsored a retirement plan, the Tri-City Healthcare District National Security Retirement Program ("NSRP"), an alternative to the U.S. Social Security system. NSRP is administered by an insurance company and provides retirement and survivorship benefits. As a condition of participation, each employee makes contributions to NSRP. The District contributed 4.5% of each participating employee's annual compensation up to approximately $79 thousand both years ended June 30, 2016 and 2015.

The District's contributions to NSRP totaled approximately $2.6 million and $2.7 million for the years ended June 30, 2016 and 2015, respectively. Effective January 1, 1992, the District provided its employees with the option of remaining in the NSRP program or transferring to the U.S. Social Security system. Statutes authorize NSRP to invest in group or individual insurance or annuity contracts or other funding vehicles as approved by the District's Board. Contributions to NSRP are deposited in one or more investment options as elected by the individual participant or in the qualified default investment alternative if no election is made.

Note 9 – Retirement Plans (continued)

The District also offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. Employees who elect to participate in the plan make contributions through a reduction in salary. All employee contributions are invested by a funding agency selected by the District. The investments of the NSRP retirement plan and the Section 457 deferred compensation plan and earnings thereon are held by fiduciaries in trust for the benefit of the employees. The NSRP and the Section 457 deferred compensation plan assets are not subject to the claims of the District's general creditors. Accordingly, the plans' assets and the related liabilities are excluded from the accompanying consolidated statements of net position as of June 30, 2016.

The District maintains a tax-deferred capital accumulation account for certain management personnel under which the District has contributed funds to mutual fund investments as directed by the participants. The contributions vest over a period of no less than two years. As of June 30, 2016 and 2015, the balance of capital accumulation funds was approximately $226 thousand and $194 thousand, respectively, which is included in other long-term assets on the accompanying consolidated statements of net position. The corresponding compensation liabilities of approximately $226 thousand and $154 thousand as of June 30, 2016 and 2015, respectively, are included in accrued payroll and related expenses on the accompanying consolidated statements of net position. The plan assets remain the property of the District until paid or made available to participants, subject only to claims of the District's general creditors.

Note 10 – Operating Leases

The District leases certain building space and equipment under non-cancelable operating leases expiring between July 2016 and October 2028. Operating lease expense for all operating leases totaled approximately $3.2 million and $2.4 million for the years ended June 30, 2016 and 2015, respectively. As of June 30, 2016, future minimum lease payments under non-cancelable operating leases are as follows:

Years Ending June 30,	
2017	$ 3,394,466
2018	3,089,737
2019	1,858,596
2020	1,122,943
2021	544,127
Thereafter	398,896
Total	$ 10,408,765

Note 11 – Related Organizations

Tri-City Hospital Foundation (the "Foundation") and Tri-City Hospital Auxiliary (the "Auxiliary") are California nonprofit corporations organized to benefit the District. Both the Foundation and the Auxiliary have bylaws that govern their separate activities, and the members and officers of each of the two organizations are selected solely by the members themselves.

Donations to the District by the Foundation totaled approximately $1.2 million and $1.0 million in the years ended June 30, 2016 and 2015, respectively. The Auxiliary donated $36 thousand and $39 thousand in the years ended June 30, 2016 and 2015, respectively.

The District pays salaries and related costs for employees of the Foundation, provides facilities for the Auxiliary gift shop, and provides administrative office space to both organizations free of charge. Such costs totaled approximately $726 thousand and $580 thousand in the years ended June 30, 2016 and 2015, respectively.

A summary of the organizations' assets, liabilities and net assets (unaudited) as of June 30 is as follows:

	2016	2015
Tri-City Hospital Foundation		
Assets	$ 4,042,264	$ 3,770,627
Liabilities	$ 211,650	$ 25,569
Net Assets	$ 3,830,614	$ 3,745,058
Tri-City Hospital Auxiliary		
Assets	$ 568,585	$ 1,446,824
Liabilities	$ 3,659	$ 776,113
Net Assets	$ 564,926	$ 670,711

Note 12 – Partnerships

During the year ended June 30, 2010, the District entered into a general partnership with Surgical Care Affiliates of Oceanside to form Tri-City Medical Center ASCO, LLC. The partnership acquired controlling interest in NCSC, a partnership between ASCO, and several limited partners, primarily physicians. The primary purpose of the District's involvement in the venture is to relocate lower acuity out-patient surgeries to the surgery center in order to free up surgical suite time for surgeries requiring hospital surgical services. The financial results of ASCO have been consolidated into the District's consolidated financial statements.

Note 12 – Partnerships (continued)

Also during the year ended June 30, 2010, the District formed CVI, LLC. The purpose of CVI is to further the District's mission and commitment to promote cardiovascular health and provide quality heart and vascular services for the residents of the District. The District and CVI entered into a co-management agreement under which CVI provides certain services to meet this mission.

During the year ended June 30, 2011, the District formed Ortho, LLC. The purpose of Ortho is to further the District's mission and commitment to promote orthopedic health and provide quality surgical, non-invasive and rehabilitation services for the residents of the District. The District and Ortho entered into a co-management agreement under which Ortho provides certain services to meet this mission.

During the year ended June 30, 2012, the District formed Tri-City REHM, LLC . The purpose of the REHM is to facilitate the acquisition and use of real estate properties to promote the District's mission.

During the year ended June 30, 2015, the District formed Tri-City Wellness, LLC, a California Limited Liability Company to purchase the Wellness Center which the District had previously operated under a capital lease. During July 2013, Tri-City Wellness, LLC procured a loan from Mid Cap Funding RE Holdings, LLC for $26.5 million and the District contributed the remaining capital to purchase the Wellness Center.

During the year ended June 30, 2015, the District formed the Tri-City Medical Center Neuroscience Institute, LLC ("Neuro"), a California Limited Liability Company. The purpose of the Neuro Institute is to further the District's mission and commitment to promote neuroscience health and provide quality neurological, neurosurgical and non-invasive services for the residents of the District. The District and the Neuro Institute, entered into a co-management agreement under which the Neuro Institute provides certain services to meet this mission.

The portion of consolidated excess of revenues over expenses attributable to minority interests in these entities for both years ended June 30, 2016 and 2015 is approximately $1.4 million.

Note 13 – Commitments and Contingencies

Legal actions – The District is involved in various legal matters arising from time to time in the ordinary course of business. The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; natural disasters; and employee health and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters.

Note 13 – Commitments and Contingencies (continued)

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medi-Cal programs, can be subject to government review and interpretation, as well as regulatory actions unknown and unasserted at this time. Federal government activity has increased with respect to investigations and allegations concerning possible violations by health care providers of regulations, which could result in the imposition of significant fines and penalties, as well as significant repayments of previously billed and collected revenues from patient services. During July 2013, the District made an offer for settlement to the Office of Inspector General ("OIG") and Department of Justice ("DOJ") related to a self-disclosure program to resolve a previously self-disclosed matter. Pursuant to ongoing discussions with the OIG and DOJ, during July 2015 the District increased its offer for settlement. In January 2016 the District paid the OIG $3.3 million as a final settlement.

In April 2014, the District commenced eminent domain proceedings against the developer of an on campus medical office building seeking to maintain a condemnation action under which it took possession of the medical office building. In June 2016, the jury returned a verdict against the District awarding approximately $2.9 million in damages for breach of good faith and dealing under a related lease agreement. In addition, under the condemnation action, the jury determined the value of the ground lease to be $16.8 million. As the district has already deposited $4.7 million the net amount due under the jury verdict is $12.1 million. The District has filed motions which seek to reduce or eliminate both verdicts. The ultimate outcome and potential financial impact are unknown. The District has not recognized a liability related to this matter as of June 30, 2016.

Seismic compliance – California Senate Bill 1953 ("SB 1953") originally required hospital acute care buildings to meet stringent seismic guidelines by 2013. The California Office of Statewide Health Planning and Development ("OSHPD") has revised its SB 1953 compliance standards by considering the HAZUS zones (FEMA Hazards – U.S.) in which each hospital is located. Under these revised HAZUS standards, it is expected that many acute care facilities throughout the state may be required to perform less seismic retrofit than originally expected, or none at all.

Based on a waiver granted to the District by OSHPD during 2009, the District's buildings are considered in compliance with all SB 1953 requirements to the year 2030.

Self-insurance programs – The District is self-insured for unemployment benefits and dental PPO benefits.

Note 13 – Commitments and Contingencies (continued)

Prior to January 1, 1999, the District was also self-insured for workers' compensation, with stop-loss insurance coverage for individual claims of more than $250 thousand. For policy years 1999 through 2001, the District has reached maximum premium levels on its policies and has no further liability exposure on claims from those years. For policy year 2002, the District has a retrospective premium workers' compensation insurance coverage with a maximum premium. The maximum premium level has not been reached for the 2002 policy year and further liability exposure is possible. For policy years 2003 and 2004, the District had a large-deductible workers' compensation plan, with stop-loss insurance coverage for individual claims of more than $350 thousand. Under this insurance arrangement, as of June 30, 2016, the District maintains nonnegotiable certificates of deposit totaling $50 thousand for calendar year 2003 and $316 thousand for calendar year 2004. Beginning January 1, 2005, the District began a self-insured workers' compensation program. The District has fully reserved for estimated claims based on actuarial analyses of policy years prior to 1999, and 2002 through 2015. Such reserves were approximately $8.3 million and $8.6 million as of June 30, 2016 and 2015, respectively.

Comprehensive liability insurance coverage – The District is insured for comprehensive liability (professional liability, general liability, personal injury and advertising liability, and employee benefits administration) under an occurrence general liability policy and professional claims-made policy, which covers asserted claims and incidents reported to the insurance carrier, and has a per-claim retention of $1 million effective July 1, 2009. The District has reserved for estimated IBNR claims through June 30, 2016. Such reserves were approximately $3.1 million and $3.0 million as of June 30, 2016 and 2015, respectively.

The following is a summary of the changes in the self-insured and claims-made plan liabilities for the years ended June 30, 2016 and 2015:

Balance as of June 30, 2014	$ 11,541,481
Additions	3,286,658
Payments	(3,219,265)
Balance as of June 30, 2015	11,608,874
Additions	3,978,546
Payments	(4,248,137)
Balance as of June 30, 2016	$ 11,339,283

Note 13 – Commitments and Contingencies (continued)

Medical services IBNR – The following is a summary of the changes in the medical services IBNR claims for the years ended June 30, 2016 and 2015:

Balance as of June 30, 2014	$ 1,693,233
Additions	7,677,929
Payments	(7,495,735)
Balance as of June 30, 2015	1,875,427
Additions	6,470,756
Payments	(6,847,994)
Balance as of June 30, 2016	$ 1,498,189

Physician loan agreements – Physician Recruitment Agreements are those under which the District has elected to loan practicing physicians up to a specified amount per month for a period of two or three years (the "loan distribution period"). At the end of the loan distribution period, each physician is obligated by a signed loan agreement to repay the outstanding loan balance. The loan can be repaid in cash or in-kind services. For repayment in-kind, the District forgives the loans monthly over the period defined in the loan agreement (up to 3 years), as long as the physician continues to practice in the defined service area. Loans to physicians accrue interest during the draw period and during the forgiveness period. The loan balances outstanding totaled approximately $5.3 million and $5.5 million as of June 30, 2016 and 2015, respectively. The balance is included in other long-term assets in the accompanying consolidated statements of net position.

Note 14 – Intergovernmental Transfer Program

The Non-designated Public Intergovernmental Transfer Program ("IGT") was established under AB 113 in 2011 to allow non-designated public hospitals to access additional federal funds. There are two supplemental payment methodologies under the IGT program: a fee-for-service methodology and a managed care plan methodology. Under this legislation, net intergovernmental transfers of approximately $3.5 million and $8.6 million were recorded by the District during the years ended June 30, 2016 and 2015, respectively. IGT income is reflected in net patient service revenue in the accompanying consolidated financial statements.

Note 15 – Subsequent Events

UC San Diego Affiliation – In August 2016 the District and UC San Diego Health officially entered into an exclusive affiliation agreement designed to enhance the delivery of high quality health care to patients in North San Diego County. Under the terms of a master agreement, UC San Diego Health and the District are collaborating to recruit primary care and specialty care physicians to the District's service area to supplement the needs of the existing medical staff, develop and market certain health care services and clear a pathway to clinical integration for interested physicians and specialists. Additionally, services for neurosurgical, cardiac, and other service care areas will be significantly enhanced.

SUPPLEMENTAL SCHEDULES

TRI-CITY HEALTHCARE DISTRICT
CONSOLIDATING STATEMENT OF NET POSITION
JUNE 30, 2016

	TCMC	ASCO	REHM	WC	CVI	Ortho	Neuro	Eliminations	Consolidated
ASSETS									
CURRENT ASSETS									
Cash and cash equivalents	$ 9,791,779	$ 430,234	$ 218,985	$ 507,482	$ 125,444	$ 68,252	$ 34,624	$ -	$ 11,176,800
Restricted cash and investments	51,366,000	-	-	-	-	-	-	-	51,366,000
Patient accounts receivable - net of estimated	-	-	-	-	-	-	-	-	-
uncollectible accounts of $18,474,430 and	-	-	-	-	-	-	-	-	-
$23,096,486 in 2016 and 2015, respectively	41,549,449	847,305	-	-	-	-	-	-	42,396,754
Other receivables	2,073,065	-	-	253,186	294,240	157,940	164,820	(296,227)	2,647,024
Supplies inventory	8,477,353	1,857	-	-	-	-	-	-	8,479,210
Prepaid expenses and other assets	2,158,817	122,857	-	674,883	-	-	-	-	2,956,557
Estimated third-party payor settlements	230,191	-	-	-	-	-	-	-	230,191
Total current assets	115,646,654	1,402,253	218,985	1,435,551	419,684	226,192	199,444	(296,227)	119,252,536
NON-CURRENT INVESTMENTS									
Board-designated	394,050	-	-	-	-	-	-	-	394,050
CAPITAL ASSETS - net	67,922,336	657,905	3,697,475	36,029,199	-	-	-	-	108,306,915
OTHER ASSETS									
Notes receivable	5,343,659	-	-	-	-	-	-	-	5,343,659
Other	28,989,929	-	-	-	109,720	47,057	46,267	(13,476,834)	15,716,139
Total other assets	34,333,588	-	-	-	109,720	47,057	46,267	(13,476,834)	21,059,798
TOTAL	$ 218,296,628	$ 2,060,158	$ 3,916,460	$ 37,464,750	$ 529,404	$ 273,249	$ 245,711	$ (13,773,061)	$ 249,013,299

TRI-CITY HEALTHCARE DISTRICT
CONSOLIDATING STATEMENT OF NET POSITION (CONTINUED)
JUNE 30, 2016

	TCMC	ASCO	REHM	WC	CVI	Ortho	Neuro	Eliminations	Consolidated
LIABILITIES AND NET POSITION									
CURRENT LIABILITIES									
Accounts payable and accrued liabilities	$ 36,898,228	$ 273,275	$ -	$ 458,535	$ 144,026	$ 44,976	$ 12,061	$ (797,259)	$ 37,033,841
Accrued payroll and related expenses	19,646,095	177,941	-	-	-	-	-	-	19,824,036
Current maturities of long-term debt	2,318,759	-	1,320,833	511,960	-	-	-	-	4,151,552
Short-term debt	55,479,469	-	-	-	-	-	-	-	55,479,469
Other current liabilities	750,804	62,035	-	141,913	-	-	-	-	954,752
Total current liabilities	115,093,355	513,251	1,320,833	1,112,408	144,026	44,976	12,061	(797,259)	117,443,650
LONG-TERM DEBT - net of current position	4,746,949	-	-	24,716,934	-	-	-	-	29,463,883
WORKERS' COMPENSATION AND									
COMPREHENSIVE LIABILITY - net of current portion	7,671,667	-	-	-	-	-	-	-	7,671,667
Total liabilities	127,511,971	513,251	1,320,833	25,829,342	144,026	44,976	12,061	(797,259)	154,579,200
NET POSITION									
Net investment in capital assets	60,856,630	657,905	2,376,641	10,800,303	-	-	-	-	74,691,480
Unrestricted	29,928,028	(167,845)	193,029	823,470	236,468	114,137	158,882	(12,975,802)	18,310,367
Restricted, non-expendable	-	1,056,847	25,957	11,635	148,910	114,137	74,768	-	1,432,253
Total net position	90,784,658	1,546,907	2,595,627	11,635,408	385,378	228,273	233,650	(12,975,802)	94,434,100
TOTAL	$ 218,296,628	$ 2,060,158	$ 3,916,460	$ 37,464,750	$ 529,404	$ 273,249	$ 245,711	$ (13,773,061)	$ 249,013,299

TRI-CITY HEALTHCARE DISTRICT
CONSOLIDATING STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2016

	TCMC	ASCO	REHM	WC	CVI	Ortho	Neuro	Eliminations	Consolidated
REVENUE									
Net patient service revenue	$ 300,547,205	$ 8,891,735	$ -	$ -	$ -	$ -	$ -	$ -	$ 309,438,940
Premium revenue	18,734,093	-	-	-	-	-	-	-	18,734,093
Other revenue	6,676,674	2,004	247,346	2,898,252	471,197	247,635	242,005	(4,361,963)	6,423,150
Total operating revenue	325,957,972	8,893,739	247,346	2,898,252	471,197	247,635	242,005	(4,361,963)	334,596,183
EXPENSES									
Salaries and related expenses	189,623,324	2,588,981	-	-	38,201	41,329	38,201	-	192,330,034
Supplies	67,289,828	2,276,110	-	-	-	-	-	-	69,565,938
Purchased services	17,789,758	620,859	-	-	3,057	3,306	3,056	(970,265)	17,449,771
Depreciation and amortization	10,007,785	323,324	-	810,885	8,933	6,844	-	-	11,157,771
Other operating expense	19,281,545	590,180	10,174	20,285	7,277	7,229	7,316	-	19,924,006
Professional and medical fees	16,397,282	40,357	-	-	100,506	57,896	58,961	-	16,655,002
Maintenance, rent & utilities	15,176,307	742,854	-	-	-	-	-	(2,376,780)	13,542,381
Total operating expenses	335,565,829	7,182,665	10,174	831,170	157,974	116,604	107,534	(3,347,045)	340,624,903
(LOSS) INCOME FROM OPERATIONS	(9,607,857)	1,711,075	237,172	2,067,082	313,223	131,031	134,471	(1,014,918)	(6,028,720)
NON-OPERATING REVENUE (EXPENSE)									
District tax revenue	8,957,499	-	-	-	-	-	-	-	8,957,499
Interest income	247,471	(9)	-	-	-	-	-	-	247,462
Interest expense	(1,807,978)	(1,790)	(47,877)	(1,746,608)	-	-	-	-	(3,604,253)
Other non-operating (expense) revenue	(1,999,520)	-	-	-	-	-	-	734,599	(1,264,921)
Total non-operating revenue (expense)	5,397,472	(1,799)	(47,877)	(1,746,608)	-	-	-	734,599	4,335,787
(DEFICIENCY) EXCESS OF REVENUE OVER EXPENSES	(4,210,385)	1,709,276	189,295	320,475	313,223	131,031	134,471	(280,319)	(1,692,933)
Minority interest distributions - net	-	(1,587,390)	-	(10)	(13,741)	42,298	(42,242)	-	(1,601,087)
Contributions (distributions) between consolidating entities	-	(667,115)	-	(1,010,361)	(213,466)	(41,633)	(88,587)	2,021,162	-
Changes in net position	(4,210,385)	(545,230)	189,295	(689,896)	86,016	131,696	3,642	1,740,843	(3,294,020)
NET POSITION - Beginning of year	94,995,041	2,092,166	2,406,332	12,325,306	299,363	96,578	230,009	(14,716,674)	97,728,120
NET POSITION - End of year	$ 90,784,657	$ 1,546,937	$ 2,595,627	$ 11,635,410	$ 385,379	$ 228,274	$ 233,651	$ (12,975,831)	$ 94,434,100