REPORT OF INDEPENDENT AUDITORS AND
FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION AND
IN ACCORDANCE WITH THE UNIFORM GUIDANCE

TRI-CITY HEALTHCARE DISTRICT

June 30, 2019 and 2018

MOSSADAMS

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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 386-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 that 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 ("ASCO"); 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 ("REHM"); and Tri-City Wellness, LLC ("Wellness Center").

ASCO, the Cardiovascular Institute, the Orthopedic Institute, the Neuro Institute, the REHM, and the Wellness Center are component units that have been blended for presentation purposes. The District has determined blended presentation is appropriate for ASCO 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 REHM and the 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, 2019, 2018, and 2017. 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 financial statements that follow this section.

This annual financial report includes four items:

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

Overview (continued)

The District's 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. In accordance with accounting principles generally accepted in the United States of America (also known as GAAP or generally accepted accounting principles) for governmental health care providers, the District's statements of revenue, expenses, and changes in net position reflect that non-operating income (expenses) including interest expense, which for nongovernmental hospitals is typically grouped as an operating expense. While these GASB requirements make district hospitals conform to other governmental entities such as cities and counties, they may be less comparable to nongovernment hospitals because of these GASB requirements.

Executive Summary

For the year ended June 30, 2019, the District reported a reduction in net position (deficiency of revenue over expenses) of approximately $4.2 million.

The 2019 deficiency of revenue over expenses by entity was as follows:

Tri-City Medical Center	$ (5,983,506)
Ambulatory Surgery Center Operators	2,729,697
Tri-City Wellness Center	101,722
Cardiovascular Institute	354,556
Orthopedic Institute	(255,500)
Neuroscience Institute	(150,056)
Eliminations	(1,015,722)
Total deficiency of revenue over expenses	$ (4,218,809)

Contributing to the 2019 results were the following significant activities:

- The District recorded a $5.1 million non-operating charge related to an on-campus medical office building legal matter. See Note 14 - Commitments and Contingencies.

- Excluding the one-time charge noted above, the District reported Earnings Before Interest Taxes Depreciation and Amortization (EBITDA) of $16.7 million during fiscal 2019. This represents a $5.4 million favorable improvement over fiscal 2018.

- Excess of Revenue Over Earnings (EROE) also reflects a positive bottom line when the one-time non-operating expense is excluded and represents an improvement over fiscal 2018 of over $5 million.

- The District recorded revenue totaling approximately $24.1 million through the continuation of the Intergovernmental Transfer (IGT) program. This program reimbursed the District for a portion of the difference between the cost of treating Medi-Cal patients and the amount reimbursed through pre-existing Medi-Cal contracts.

Executive Summary (continued)

- The District participated in the Public Hospital Redesign and Incentives in Medi-Cal (PRIME) program in 2019. The PRIME program is a community centric population health, pay-for-performance, outcomes-based initiative. Performance baselines were established and target goals were set. The District is currently in the ongoing evaluation of quality improvement interventions phase of the program. The PRIME program contributed approximately $4.6 million to revenue in 2019.

- The District has experienced a decrease in inpatient patient volumes for the past few years. From 2014–2015 hospitals saw a spike in patient volumes. This was due to the implementation of the Affordable Care Act (ACA) that enabled more people to obtain healthcare insurance than prior to the ACA. In recent years there has been an overall shift towards outpatient care. There have been increases to outpatient surgery centers and urgent care centers. The national shift to outpatient care is also due to increases in insurance deductibles where patients shoulder a larger portion of their healthcare costs. Accordingly, there has been a decrease in emergency department visits nationwide. Additionally, the District suspended Inpatient Behavioral Health Unit (BHU) and Crisis Stabilization Unit (CSU) service lines during fiscal 2019. These factors contributed to the District experiencing a 7.4% decrease in emergency department visits and a 12.7% decrease in inpatient days.

- The District's strategic partnership in ASCO resulted in an excess of revenues over expenses of approximately $2.7 million in 2019. Because the District owns 60% of ASCO and ASCO owns 52.8% of North Coast Surgery Center Ltd., the District's share of earnings was approximately $799 thousand.

- The District's revenue related to prior years' cost report settlements totaled approximately $2.2 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.

- The District continued to recruit physicians to improve medical coverage for the communities it serves. Specialties recruited include primary care, cardiology, and surgery. Loans to physicians accrue interest during the draw period and during the forgiveness period. As of June 30, 2019, the physician loan balance was $3.0 million. Approximately $2.5 million was forgiven during 2019.

- In July 2017, the District purchased Orthopedic Specialists of North County (OSNC) clinic operations for $6.0 million. The partnership between the District and the clinic combines the strength of the two organizations to provide delivery of the most advanced, high quality orthopedic medical and surgical services, including joint replacement, spine care, sports medicine, cutting-edge non-operative therapy, and physical rehabilitation to the community. The associated transactions along with financial results are reported in the District's financial statements.

Executive Summary (continued)

During fiscal year 2019, supplies and pharmaceuticals expense decreased by $1.3 million, salaries and related expenses decreased by $9.2 million, and professional and medical fees decreased by $2.4 million. The decreases were primarily due to the lower inpatient volumes in addition to the suspension of the Inpatient Behavioral Health Unit (BHU) and Crisis Stabilization Unit (CSU) service lines.

Required Financial Statements

Statement of net position – The 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 Statements of Net Position as of June 30 (In Thousands):

	2019	2018	2017
ASSETS			
Current assets	$ 114,193	$ 114,329	$ 115,075
Capital assets - net	98,670	101,759	103,650
Non-current assets	38,721	44,710	39,869
TOTAL ASSETS	$ 251,584	$ 260,798	$ 258,594
LIABILITIES AND NET POSITION			
Current liabilities	$ 80,016	$ 79,850	$ 67,817
Long-term debt - net of current portion	80,654	83,988	88,091
Workers' compensation and comprehensive liability - net of current portion	7,955	7,938	7,755
Total liabilities	168,625	171,776	163,663
Invested in capital assets - net of related debt	16,777	12,995	13,377
Restricted assets	9,124	8,670	7,966
Unrestricted	57,058	67,357	73,588
Total net position	82,959	89,022	94,931
TOTAL LIABILITIES AND NET POSITION	$ 251,584	$ 260,798	$ 258,594

Analysis of Changes in the Statement of Net Position

Changes from fiscal year 2018 to 2019

- Current assets totaling approximately $114.2 million in 2019 remained relatively unchanged with a slight decrease of $136 thousand from the prior year. Included in current assets is an increase of approximately $4.3 million in short-term investments, cash, and cash equivalents, offset with a decrease of approximately $2.2 million in patient accounts receivable and a decrease of approximately $2.9 million in estimated third-party settlements.

- Non-current assets totaling approximately $38.7 million in 2019 represents a decrease of $6.0 million from the prior year, primarily due to recording a $5.1 million offset resulting from a court ruling related to the on-campus medical office building. See Note 14 - Commitments and Contingencies. Included in non-current assets is approximately $7.5 million deposited for mortgage reserve funds related to the HUD guaranteed loan.

- Cash on hand, short-term investments, and unused availability from the revolving credit facility provides liquidity to the District. Cash and cash equivalents totaled approximately $45.0 million, short-term investments totaled approximately $5.9 million, and the unused available revolving line of credit was approximately $3.5 million as of June 30, 2019. This resulted in total liquidity of approximately $54.5 million. This represents a $1.7 million increase in total liquidity over the prior year.

- Net estimated third-party payor settlements of approximately $3.9 million decreased by approximately $2.9 million from 2018 due to the payments received for prior year balances. The majority of the third-party settlements balance as of June 30, 2019, pertains to outstanding receivables from the PRIME program and current year cost report estimates.

- Capital assets net totaled approximately $98.7 million as of June 30, 2019. A decrease of approximately $3.1 million from 2018 was the result of $9.1 million in new equipment, software acquisitions, and other capital improvement projects, offset by depreciation and amortization expense of $12.2 million.

- Current liabilities totaled approximately $80.0 million for both years ended June 30, 2019 and 2018.

- Long-term debt net of current portion totaled approximately $80.7 million as of June 30, 2019, compared to $84.0 million as of June 30, 2018. The decrease is primarily related to the payments of principal on long-term debt.

- Workers' compensation and comprehensive liability insurance reserves classified as long-term liabilities totaled approximately $8.0 million for both years ended June 30, 2019 and 2018, 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.

Analysis of Changes in the Statement of Net Position (continued)

Changes from fiscal year 2017 to 2018

- Current assets totaling approximately $114.3 million in 2018 represent a decrease of $746 thousand from the prior year. Included in current assets is a decrease of approximately $6.3 million in short-term investments, cash, and cash equivalents, and an increase of approximately $5.1 million of estimated amounts due from third-party settlements to the District for participation in the PRIME program.

- Non-current assets totaling approximately $44.7 million in 2018 represent an increase of $4.8 million from the prior year primarily due to the $4.9 million goodwill related to the purchase of OSNC Clinic operations. Included in non-current assets is approximately $7.0 million of mortgage reserve funds related to the HUD guaranteed loan and a $17.0 million deposit made to the State of California associated with a medical office building legal matter.

- Cash on hand, short-term investments, and unused availability from the revolving credit facility provides liquidity to the District. Cash and cash equivalents totaled approximately $41.2 million, short-term investments totaled approximately $5.4 million, and the unused available revolving line of credit was approximately $6.2 million as of June 30, 2018. This resulted in total liquidity of $52.8 million.

- Net estimated third-party payor settlements of approximately $6.8 million increased by approximately $5.1 million from 2017. The majority of the third-party settlements balance as of June 30, 2018, pertains to outstanding receivables from the PRIME program and current year cost report estimates.

- Capital assets net totaled approximately $101.8 million as of June 30, 2018. A decrease of approximately $1.9 million from 2017 was the result of $9.9 million in new equipment and software acquisitions and the continuation of certain capital projects, offset by depreciation and amortization expense of $11.6 million.

- Current liabilities totaling approximately $79.9 million as of June 30, 2018, reflect an increase of approximately $12.0 million compared to June 30, 2017. Current liabilities included $3.0 million in short-term debt related to the purchase of OSNC Clinic operations.

- Long-term debt net of current portion totaled approximately $84.0 million as of June 30, 2018, compared to $88.1 million as of June 30, 2017. The decrease is primarily related to the payments of principal on long-term debt.

- Workers' compensation and comprehensive liability insurance reserves classified as long-term liabilities increased by $184 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 Statements of Revenues, Expenses, and Changes in Net Position for the Years Ended June 30 (In Thousands):

	2019	2018	2017
Operating revenue	$ 356,874	$ 365,142	$ 340,112
Operating expenses	363,294	375,800	341,682
Loss from operations	(6,420)	(10,658)	(1,570)
Non-operating revenue	2,201	6,396	3,450
Change in net position before minority interest (EROE)	(4,219)	(4,262)	1,880
Minority interest distributions - net	(1,844)	(1,647)	(1,383)
Change in net position	(6,063)	(5,909)	497
Beginning net position	89,022	94,931	94,434
Ending net position	$ 82,959	$ 89,022	$ 94,931
Average daily census	153	175	180
Emergency room visits	56,437	60,935	62,555

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

Changes from fiscal year 2018 to 2019

- The District recorded a $5.1 million non-operating charge related to an on-campus medical office building legal matter during fiscal 2019. See Note 14 - Commitments and Contingencies.

- Excluding the one-time charge noted above, the District reported Earnings Before Interest Taxes Depreciation and Amortization (EBITDA) of $16.7 million during fiscal 2019. This represents a $5.4 million favorable improvement over fiscal 2018.

- Excess of Revenue Over Earnings (EROE) also reflects a positive bottom line when the one-time non-operating expense is excluded and represents an improvement over fiscal 2018 of over $5 million.

- The District experienced a decrease of 12.7% in inpatient volume in 2019. Total average daily census was 153 for the current year compared to 175 in the prior year. Total hospital outpatient visits decreased by approximately 3.9% compared to 2018. The decrease was primarily due to lower volume in general and the suspension of the BHU and CSU. Emergency Department visits decreased approximately 7.4%.

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

- Operating revenue decreased by approximately $8.3 million in 2019 compared to 2018. This decrease is primarily due to lower volume in general and the suspension of BHU and CSU.

- Operating expenses, which include patient care expenses, overhead, and administrative expenses, decreased by approximately $12.5 million. The decrease was approximately $9.2 million in salaries and related expenses partly due to suspension of BHU and CSU, $1.3 million in supplies and pharmaceuticals and $2.4 million in professional and medical fees.

- 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. Non-operating income and expenses decreased by approximately $4.2 million in 2019. There was a $5.1 million non-operating expense related to a medical office building legal matter in 2019. See Note 14 - Commitment and Contingencies.

Changes from fiscal year 2017 to 2018

- The District reported EBITDA of approximately $11.3 million during fiscal 2018.

- The District experienced a decrease of 2.8% in inpatient volume in 2018. Total average daily census was 175 for the current year compared to 180 in the prior year. Total hospital outpatient visits increased by approximately 34.4% compared to 2017 due to the addition of the new OSNC service line. Emergency Department visits decreased approximately 2.6%.

- Operating revenue increased by approximately $25.0 million in 2018 compared to 2017. This increase was primarily due to revenue from OSNC clinic operations of $15.0 million and a $6.1 million increase in receipts from the PRIME and IGT programs throughout the year, offset by a decrease in patient volume. PRIME is a community centric population health pay-for-performance, outcomes-based initiative.

- Operating expenses, which include patient care expenses, overhead, and administrative expenses, increased by approximately $34.1 million. The District experienced increases in professional and medical fees expenses, salaries, and related expenses. Although salaries and related expenses increased by approximately $9.8 million, salaries and related expenses as a percentage of the total operating revenue was slightly lower at approximately 56% compared to 57% in 2017. The professional and medical fees expenses increased approximately $11.0 million primarily due to OSNC clinic physician fees. Supplies and pharmaceuticals expenses also increased approximately $7.4 million primarily due to shortages of drugs in high demand resulting in increased prices.

- 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. Non-operating income and expenses increased by approximately $2.9 million in 2018. There was $3.4 million in closing costs related to the HUD financing included in 2017 non-operating expense.

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

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.

	2019	2018	2017
Net cash provided by (used in)			
Operating activities	$ 12,075	$ 2,190	$ 12,301
Noncapital financing activities	9,446	8,859	6,019
Capital and related financing activities	(17,716)	(17,352)	(21,121)
Investing activities	12	32,550	6,584
Net change in cash and cash equivalents	3,817	26,247	3,783
Cash and cash equivalents - Beginning of year	41,207	14,960	11,177
Cash and cash equivalents - End of year	$ 45,024	$ 41,207	$ 14,960

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").

Analysis of the Statement of Cash Flows

Cash and cash equivalents totaled approximately $45.0 million, $41.2 million, and $15.0 million, as of June 30, 2019, 2018, and 2017, respectively. Net cash provided by operating activities in 2019 was $12.1 million, an increase of approximately $9.9 million from prior year. In 2018, net cash provided by operating activities decreased approximately $10.1 million compared to 2017. Cash provided by noncapital financing activities increased approximately $587 thousand compared to 2018. Cash used in capital and related financing activities increased by approximately $364 thousand from prior year and decreased by approximately $3.8 million from 2017 to 2018 primarily due to the payment of a $12.3 million deposit to the State of California associated with a medical office building legal matter. Cash provided by investing activities decreased approximately $32.5 million in 2019 from prior year.

Capital Assets

As of June 30, 2019, 2018, and 2017, the District had $98.7 million, $101.8 million, and $103.6 million, respectively, in capital assets, net of accumulated depreciation, as detailed in Note 5 to the financial statements. The District invested in new equipment, which included information technology, surgical equipment, buildings improvements, and other minor infrastructure projects costing $9.0 million in 2019, $8.7 million in 2018, and $7.2 million in 2017.

Capital Assets (continued)

Capital lease payments were made timely. More detailed information about the District's debt is presented in Notes 8 and 9 to the financial statements.

Economic Factors

Over the next five years, the District will continue to face challenges in the evolving landscape of the healthcare industry. The industry is moving towards value-based care. As the industry migrates to a value-based system and new entrants force market innovation, the hospital-focused inpatient utilization rates continue to decline in many areas of the country. Other drivers of lower hospital utilization include focus on decreasing readmission rates, transitioning patients to observation status, and increased use of care management teams.

Government payers have slowed on spending growth. On top of the 2% sequestration cuts that were put in place in 2013, Medicare is looking for additional ways to cut costs by focusing on quality-based reimbursement models that reward healthcare providers for their contributions to producing improved health and penalizing providers who are not able to improve quality outcomes and reduce readmission rates. The Medicare value-based purchasing program includes measuring process-of-care measures, patient experience measures, patient outcome measures, and efficiency measures. The District is working diligently to continue improving these quality metrics, which in turn will reduce the risk of reimbursement cuts.

On the State level, the Affordable Care Act (ACA) has significantly increased the coverage for the Medi-Cal population, which in turn has reduced the amount of uncompensated/self-pay care for hospitals across the state including the District. Greater use of Medi-Cal managed care is likely to continue with the goals of improved quality and increased savings through reduced use of hospital services.

Despite some of the challenges the hospital is facing from government payers, the District has been actively negotiating its insurance contracts to ensure that it maintains competitive reimbursement rates over the coming years. Furthermore, the District is actively engaged in performance-based programs such as PRIME along with service line analysis to identify opportunities for growth in profitable services, as well as evaluating unprofitable services for cost and efficiency improvements while maintaining the highest quality of care and clinical outcomes.

Finance Contact

The District's 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.

Report of Independent Auditors

The Board of Directors
Tri-City Healthcare District

Report on the Financial Statements

We have audited the accompanying financial statements of Tri-City Healthcare District (the "District") which comprise the statements of net position as of June 30, 2019 and 2018, and the related statements of revenues, expenses and 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 financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; 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 financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Tri-City Healthcare District as of June 30, 2019 and 2018, 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.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 1 to 10 be presented to supplement the basic financial statements. Such information, although not 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.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The schedule of expenditures of federal awards on page 49, as required by Title 2 *U.S. Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*; the U.S. Department of Housing and Urban Development (HUD) Required Financial Information on page 44, as required by District's Regulatory Agreement with HUD; the schedule of net position, June 30, 2019 on pages 41 and 42; and schedule of revenues, expenses, and changes in net position for the year ended June 30, 2019 on page 43, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedule of expenditures of federal awards, HUD Required Financial Information, schedule of net position, June 30, 2019, and schedule of revenues, expenses, and changes in net position for the year ended June 30, 2019, are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic 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 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. In our opinion, the schedule of expenditures of federal awards, HUD Required Financial Information, schedule of net position, June 30, 2019 and schedule of revenues, expenses, and changes in net position for the year ended June 30, 2019, are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Information – Compliance with Contractual Agreements

In connection with our audit, nothing came to our attention that caused us to believe that Tri-City Healthcare District failed to comply with the terms, covenants, provisions, or conditions of sections 1 to 49, inclusive, of the HUD Regulatory Agreement dated March 1, 2017, insofar as they relate to accounting matters. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding Tri-City Healthcare District's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the HUD Regulatory Agreement, insofar as they relate to accounting matters.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 18, 2019 on our consideration of Tri-City Healthcare District'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 Tri-City Healthcare District'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 Tri-City Healthcare District's internal control over financial reporting and compliance.

Restricted Use Relating to the Other Matter – Compliance with Contractual Agreements

The communication related to compliance with the aforementioned HUD Regulatory Agreement described in the *Other Matters* paragraph is intended solely for the information and use of the board of directors and management of Tri-City Healthcare District and HUD and is not intended to be, and should not be, used by anyone other than these specified parties.

Moss Adams LLP

Irvine, California
September 18, 2019

Tri-City Healthcare District
Statements of Net Position

ASSETS

	June 30, 2019	June 30, 2018
CURRENT ASSETS		
Cash and cash equivalents	$ 45,023,745	$ 41,207,227
Short-term investments	5,930,724	5,414,483
Restricted cash and investments	298,000	317,000
Patient accounts receivable	44,012,687	46,195,877
Other receivables	2,019,202	2,446,519
Supplies inventory	9,421,046	9,013,015
Prepaid expenses and other assets	3,636,938	2,978,734
Estimated third-party payor settlements	3,850,532	6,755,695
Total current assets	114,192,874	114,328,550
NON-CURRENT INVESTMENTS		
Board-designated	407,795	401,227
CAPITAL ASSETS - net	98,670,226	101,758,785
OTHER ASSETS		
Notes receivable	3,015,138	4,387,497
Restricted mortgage reserve fund	7,530,972	7,039,024
Goodwill	9,529,430	9,529,430
Other	18,237,261	23,353,409
Total other assets	38,312,801	44,309,360
Total assets	$ 251,583,696	$ 260,797,922

See accompanying notes.

LIABILITIES AND NET POSITION

	June 30, 2019	June 30, 2018
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	$ 44,643,030	$ 44,130,100
Accrued payroll and related expenses	19,805,596	19,232,710
Current maturities of long-term debt	3,381,447	3,827,098
Short-term debt	10,075,123	10,442,249
Other current liabilities	2,110,349	2,217,445
Total current liabilities	80,015,545	79,849,602
LONG-TERM DEBT - net of current portion	80,653,772	83,987,851
WORKERS' COMPENSATION AND COMPREHENSIVE LIABILITY - net of current portion	7,955,184	7,938,447
Total liabilities	168,624,501	171,775,900
NET POSITION		
Invested in capital assets - net of related debt	16,776,513	12,994,959
Restricted assets	9,124,319	8,669,677
Unrestricted	57,058,363	67,357,386
Total net position	82,959,195	89,022,022
Total liabilities and net position	$ 251,583,696	$ 260,797,922

See accompanying notes.

Tri-City Healthcare District
Statements of Revenues, Expenses, and Changes in Net Position

	Years Ended June 30, 2019	2018
OPERATING REVENUE		
Net patient service revenue	$ 329,873,288	$ 340,128,328
Premium revenue	18,934,440	18,033,694
Other revenue	8,066,194	6,979,912
Total operating revenue	356,873,922	365,141,934
OPERATING EXPENSES		
Salaries and related expenses	194,907,096	204,066,033
Supplies	74,085,888	75,411,889
Purchased services	20,807,688	20,407,603
Depreciation and amortization	12,103,066	11,577,114
Other operating expense	21,187,961	22,677,794
Professional and medical fees	22,487,086	24,876,541
Maintenance, rent, and utilities	17,714,924	16,783,117
Total operating expenses	363,293,709	375,800,091
LOSS FROM OPERATIONS	(6,419,787)	(10,658,157)
NON-OPERATING REVENUE (EXPENSE)		
District tax revenue	10,927,012	10,245,197
Interest income	764,984	576,581
Interest expense	(4,554,654)	(4,554,127)
Other non-operating (expense) income	(4,936,364)	128,200
Total non-operating revenue, net	2,200,978	6,395,851
CHANGE IN NET POSITION BEFORE MINORITY INTEREST (DEFICIENCY OF REVENUE OVER EXPENSES)	(4,218,809)	(4,262,306)
MINORITY INTEREST DISTRIBUTIONS - NET	(1,844,018)	(1,646,988)
Change in net position	(6,062,827)	(5,909,294)
NET POSITION - Beginning of year	89,022,022	94,931,316
NET POSITION - End of year	$ 82,959,195	$ 89,022,022

See accompanying notes.

	Years Ended June 30,	
	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from patients, insurers, and other payors	$ 354,323,398	$ 353,216,681
Payments to vendors	(156,836,852)	(156,569,411)
Payments for salaries, wages, and related benefits	(194,334,210)	(202,912,635)
Other receipts and payments, net	8,922,288	8,455,526
Net cash provided by operating activities	12,074,624	2,190,161
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Minority interest distributions, net	(1,844,018)	(1,646,988)
Receipt of District taxes	10,927,012	10,245,197
Other non-operating income	363,056	261,251
Net cash provided by noncapital financing activities	9,446,050	8,859,460
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	(9,014,507)	(8,686,308)
Proceeds from revolving line of credit	404,138,227	405,520,641
Principal repayments on revolving line of credit	(401,505,353)	(400,600,468)
Principal repayments on debt	(6,779,730)	(9,031,815)
Interest payments on debt	(4,554,654)	(4,554,127)
Net cash used in capital and related financing activities	(17,716,017)	(17,352,077)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of short-term investments	(60,019,000)	(21,404,752)
Proceeds from sales of short-term investments	60,000,000	54,000,000
Payments to mortgage reserve fund	(491,948)	(488,910)
Interest on investments	522,809	443,530
Net cash provided by investing activities	11,861	32,549,868
Net change in cash and cash equivalents	3,816,518	26,247,412
CASH AND CASH EQUIVALENTS - Beginning of year	41,207,227	14,959,815
CASH AND CASH EQUIVALENTS - End of year	$ 45,023,745	$ 41,207,227
NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES		
Non-operating legal damages and related fees (See Note 14)	$ 5,057,245	$ -
Capital assets and supplies inventory assumed related to acquisition of OSNC clinic	$ -	$ 1,100,000
Promissory note related to acquisition of OSNC clinic	$ -	$ 6,000,000

See accompanying notes.

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

	Years Ended June 30, 2019	Years Ended June 30, 2018
Loss from operations	$ (6,419,787)	$ (10,658,157)
Adjustments to reconcile loss from operations to net cash provided by operating activities:		
Provision for bad debt	37,829,703	46,418,835
Depreciation and amortization	12,103,066	11,577,114
Changes in assets and liabilities		
Patient accounts receivable	(35,646,513)	(48,598,072)
Other receivables	427,317	2,330,600
Estimated third-party payor settlements	2,905,163	(5,096,705)
Other - net	(210,141)	2,513,629
Accounts payable and accrued liabilities	512,930	2,549,519
Accrued payroll and related expenses	572,886	1,153,398
Net cash provided by operating activities	$ 12,074,624	$ 2,190,161

See accompanying notes.

Note 1 – Organization

Organization – Tri-City Healthcare District (the "District") 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 financial statements of the District include the accounts of the District, Tri-City Medical Center Ambulatory Surgery Center Operators, LLC ("ASCO"); North Coast Surgery Center Ltd. ("NCSC"); the Cardiovascular Health Institute, LLC (the "Cardiovascular Institute"); the Orthopedic Institute, LLC (the "Orthopedic Institute"); the Neuroscience Institute, LLC (the "Neuro Institute"); Tri-City Real Estate Holding and Management Co, LLC ("REHM"); and Tri-City Wellness, LLC (the "Wellness Center"). The Cardiovascular Institute, the Orthopedic Institute, and the Neuro Institute are hereafter collectively referred to as "The Institutes."

ASCO, NCSC, the Cardiovascular Institute, the Orthopedic Institute, the Neuro Institute, REHM, and the Wellness Center 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 the Cardiovascular Institute, 50% of the Orthopedic Institute and 68% of the Neuro Institute. These 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 the Cardiovascular Institute, the Orthopedic Institute, and the Neuro Institute as the component units provide services almost entirely to the District. The District owned 99% of REHM and dissolved REHM during fiscal year 2019. The District has determined blended presentation is appropriate for REHM as management of the District had operational responsibility for REHM. The District owns 99.9% of the Wellness Center. The District has determined blended presentation is appropriate for the Wellness Center as management of the District has operational responsibility for the Wellness Center. All intercompany transactions have been eliminated in the District's financial statements.

Note 1 – Organization (continued)

Condensed component information for each of the District's blended component units is as follows:

	ASCO	REHM & Wellness Center	The Institutes
ASSETS			
Current assets	$ 2,201,944	$ 289,698	$ 603,466
Capital assets - net	708,757	-	-
Non-current assets	-	-	166,153
TOTAL ASSETS	$ 2,910,701	$ 289,698	$ 769,619
LIABILITIES AND NET POSITION			
Current liabilities	$ 926,623	$ 7,500	$ 163,901
Total liabilities	926,623	7,500	163,901
Invested in capital assets - net of related debt	708,757	-	-
Restricted assets	1,355,522	282	237,543
Unrestricted	(80,201)	281,916	368,175
Total net position	1,984,078	282,198	605,718
TOTAL LIABILITIES AND NET POSITION	$ 2,910,701	$ 289,698	$ 769,619

Note 1 – Organization (continued)

Condensed Statement of Net Position
As of June 30, 2018

	ASCO	REHM & Wellness Center	The Institutes
ASSETS			
Current assets	$ 1,847,060	$ 229,363	$ 998,624
Capital assets - net	619,793	2,264,931	-
Non-current assets	-	-	175,087
Total assets	$ 2,466,853	$ 2,494,294	$ 1,173,711
LIABILITIES AND NET POSITION			
Current liabilities	$ 717,439	$ 7,500	$ 163,902
Total liabilities	717,439	7,500	163,902
Invested in capital assets - net of related debt	619,793	2,264,931	-
Restricted assets	1,195,200	23,243	412,210
Unrestricted	(65,579)	198,620	597,599
Total net position	1,749,414	2,486,794	1,009,809
Total liabilities and net position	$ 2,466,853	$ 2,494,294	$ 1,173,711

Note 1 – Organization (continued)

Condensed Statements of Revenues, Expenses, and Changes in Net Position
For the Year Ended June 30, 2019

	ASCO	REHM & Wellness Center	The Institutes
OPERATING REVENUE	$ 11,180,776	$ 108,835	$ 58,197
OPERATING EXPENSES	8,450,083	7,113	109,197
Gain (loss) from operations	2,730,693	101,722	(51,000)
NON-OPERATING EXPENSES, net	(996)	-	-
Change in net position before minority interest	2,729,697	101,722	(51,000)
MINORITY INTEREST DISTRIBUTIONS - NET	(2,495,033)	(2,306,318)	(353,091)
Change in net position	234,664	(2,204,596)	(404,091)
NET POSITION - Beginning of year	1,749,414	2,486,794	1,009,809
NET POSITION - End of year	$ 1,984,078	$ 282,198	$ 605,718

Condensed Statements of Revenues, Expenses, and Changes in Net Position
For the Year Ended June 30, 2018

	ASCO	REHM & Wellness Center	The Institutes
OPERATING REVENUE	$ 10,811,452	$ 106,041	$ 944,939
OPERATING EXPENSES	8,557,509	8,621	187,035
Gain from operations	2,253,943	97,420	757,904
NON-OPERATING REVENUE, net	2,742	-	-
Change in net position before minority interest	2,256,685	97,420	757,904
MINORITY INTEREST DISTRIBUTIONS - NET	(2,065,601)	(1,800,000)	(555,054)
Change in net position	191,084	(1,702,580)	202,850
NET POSITION - Beginning of year	1,558,330	4,189,374	806,959
NET POSITION - End of year	$ 1,749,414	$ 2,486,794	$ 1,009,809

Note 1 – Organization (continued)

Condensed Statement of Cash Flows
For the Year Ended June 30, 2019

	ASCO	REHM & Wellness Center	The Institutes
NET CASH PROVIDED BY (USED IN)			
Operating activities	$ 2,946,310	$ 108,578	$ 322,647
Noncapital financing activities	(2,495,033)	(41,387)	(353,089)
Capital and related financing activities	(99,001)	-	-
Investing activities	9,041	-	-
Net change in cash and cash equivalents	361,317	67,191	(30,442)
CASH AND CASH EQUIVALENTS - Beginning of year	502,653	215,446	207,348
CASH AND CASH EQUIVALENTS - End of year	$ 863,970	$ 282,637	$ 176,906

Condensed Statement of Cash Flows
For the Year Ended June 30, 2018

	ASCO	REHM & Wellness Center	The Institutes
NET CASH PROVIDED BY (USED IN)			
Operating activities	$ 2,482,015	$ 104,075	$ 528,781
Noncapital financing activities	(2,301,123)	(1,800,000)	(555,054)
Capital and related financing activities	15,662	-	-
Investing activities	2,950	-	-
Net change in cash and cash equivalents	199,504	(1,695,925)	(26,273)
CASH AND CASH EQUIVALENTS - Beginning of year	303,149	1,911,371	233,621
CASH AND CASH EQUIVALENTS - End of year	$ 502,653	$ 215,446	$ 207,348

Note 2 – Summary of Significant Accounting Policies

Basis of presentation – The 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.

Note 2 – Summary of Significant Accounting Policies (continued)

Accounting estimates – The preparation of 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 as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Cash equivalents – For purposes of the 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.

Investments – Investments are primarily held in Local Agency Investment Fund (LAIF), a highly liquid fund. Deposits and withdrawals can be made daily upon demand without penalty. Investment income is reported in non-operating income (expense) in the statements of revenues, expenses, and changes in net position.

Supplies inventory – Supplies inventory is 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. 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, 2019 and 2018.

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, 2019 and 2018.

Mortgage reserve fund – A mortgage reserve fund (MRF) related to the $85.8 million mortgage is required under the Hospital Regulatory Agreement between the District and the United States Department of Housing and Urban Development (HUD). The District makes deposits into the MRF trust account in accordance with the Mortgage Reserve Fund Agreement.

Net position – Net position of the District is classified into three components. “Invested in capital assets – net of related debt” 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. “Restricted assets” net position represents the net position of ASCO, the Cardiovascular Institute, the Orthopedic Institute, the Neuro Institute, REHM, and the Wellness Center not owned by the District in the amount of approximately $1.6 million for both years ended June 30, 2019 and 2018, as well as mortgage reserve fund deposits required under the Hospital Regulatory Agreement between the District and HUD of approximately $7.5 million and $7.0 million as of June 30, 2019 and 2018, respectively. “Unrestricted” net position is the remaining net position that does not meet the definition of invested in capital assets – net of related debt or restricted assets.

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 healthcare services – the District’s principal activity. Operating expenses include all expenses incurred to directly provide healthcare 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 payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. 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.

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 14 – Commitments and Contingencies.

IBNR liabilities of approximately $1.5 million for both years ended June 30, 2019 and 2018, are included in accounts payable and accrued liabilities in the accompanying statements of net position.

Property taxes – The District receives financial support from property taxes and the 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. Taxes 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.

Risk management – The District 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; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. The District is self-insured for a portion of its exposure to risk of loss from workers' compensation and malpractice claims. Annual estimated provisions are accrued based on actuarially determined amounts and includes an estimate of the ultimate costs for both reported claims and claims incurred but not yet reported.

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 of approximately $9.1 million and $9.5 million as of June 30, 2019 and 2018, respectively, is reported as a current liability within accrued payroll and related expenses in the accompanying statements of net position. 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.

The District is reimbursed for hospital inpatient services provided to Medi-Cal beneficiaries based upon Diagnosis Related Groups (DRGs), excluding rehabilitative services and behavioral health services. Rehabilitative services and behavioral health services are reimbursed on a per diem basis. Revenue from the Medicare and Medi-Cal programs accounted for approximately 65% and 64% of the District's gross patient service revenue for the years ended June 30, 2019 and 2018, respectively.

The District participates in the Intergovernmental Transfer (IGT) program, which reimburses the District for a portion of the difference between the cost of treating Medi-Cal patients and the amount reimbursed through pre-existing Medi-Cal contracts. The District recognizes revenue from the IGT program when certainty of receiving the funds is assured.

The District participates in PRIME, a pay-for-performance Medi-Cal program in which California's public health care systems and district and municipal hospitals are using evidence-based quality improvement methods to achieve performance targets and improve health outcomes for patients. All funding for this program is contingent on meeting these targets and demonstrating continued improvement. The District recognizes revenue from the PRIME program when certainty of receiving the funds is assured.

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 2015. Results of cost report settlements, as well as the District's estimates for settlements, of all fiscal years through 2019 are reflected in the accompanying financial statements.

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

Estimated net third-party settlements consisted of a net receivable of approximately $3.9 million and $6.8 million as of June 30, 2019 and 2018, respectively. During the years ending June 30, 2019 and 2018, 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 $2.2 million and $3.6 million of additional net patient service revenue in the years ended June 30, 2019 and 2018, respectively, and are included in net patient service revenue in the accompanying statements of revenue, expenses, and changes in net position.

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 whom 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:

	2019	2018
HMO/PPO	23%	29%
Medicare plans	32%	27%
Medi-Cal plans	15%	18%
Others	30%	26%
Total	100%	100%

Non-operating revenue includes District tax revenue and other non-patient service revenue. District tax revenue totaled approximately $10.9 million and $10.2 million for the years ended June 30, 2019 and 2018, respectively. Other non-operating income (expense) includes approximately $656 and $403 thousand in donations from the Foundation and Auxiliary for the years ended June 30, 2019 and 2018, respectively. Approximately $5.1 million related to an on-campus medical office building legal matter is included in non-operating expense in fiscal year 2019.

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.

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

Short-term investments – 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 $65.0 million in the fund. Investments in the LAIF are highly liquid, as deposits can be converted to cash daily without penalty. The District is a voluntary participant in the LAIF. As of June 30, 2019 and 2018, the District held approximately $6.3 million and $5.8 million in LAIF, respectively.

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. The District's investment in LAIF is not rated by a nationally recognized statistical rating organization since amounts invested in LAIF are protected by certain statutes.

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, 2019 and 2018, the District's bank balances totaled approximately $45.3 million and $41.5 million, respectively, and were not exposed to custodial credit risk, as the uninsured deposits are with financial institutions that 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)

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

	2019	2018
Cash and cash equivalents	$ 45,023,745	$ 41,207,227
Short-term investments	5,930,724	5,414,483
Restricted cash and investments –		
Non-negotiable certificates of deposit	298,000	317,000
Board-designated	407,795	401,227
Total	$ 51,660,264	$ 47,339,937

Note 5 – Capital Assets

Capital assets consisted of the following as of June 30:

	2019				
	Beginning Balance	Additions	Deletions	Transfers	Ending Balance
Land and land improvements	$ 19,930,612	$ -	$ -	$ 4,755,405	$ 24,686,017
Buildings and improvements	205,014,551	249,834	-	(372,913)	204,891,472
Equipment	162,343,531	4,887,558	(243,510)	2,206,825	169,194,404
Assets under lease	7,320,305	-	-	(858,183)	6,462,122
Construction in progress	5,577,832	3,963,473	-	(5,731,134)	3,810,171
	400,186,831	9,100,865	(243,510)	-	409,044,186
Less accumulated depreciation and amortization	(298,428,046)	(11,952,631)	6,717	-	(310,373,960)
Capital assets - net	$ 101,758,785	$ (2,851,766)	$ (236,793)	$ -	$ 98,670,226

	2018				
	Beginning Balance	Additions	Deletions	Transfers	Ending Balance
Land and land improvements	$ 19,840,144	$ 6,614	$ -	$ 83,854	$ 19,930,612
Buildings and improvements	203,063,469	209,755	-	1,741,327	205,014,551
Equipment	160,294,398	4,233,501	(2,767,495)	583,127	162,343,531
Assets under lease	7,327,323	-	(7,018)	-	7,320,305
Construction in progress	2,567,733	5,418,407	-	(2,408,308)	5,577,832
	393,093,067	9,868,277	(2,774,513)	-	400,186,831
Less accumulated depreciation and amortization	(289,443,476)	(11,563,253)	2,578,683	-	(298,428,046)
Capital assets - net	$ 103,649,591	$ (1,694,976)	$ (195,830)	$ -	$ 101,758,785

Note 6 – Goodwill

On July 1, 2017, the District acquired 100% of the ownership of Orthopedic Specialists of North County ("OSNC") financed through the issuance of a promissory note of $6.0 million. The transaction was accounted for as a business combination. As of the acquisition date, OSNC had a fair value of tangible assets of $1.1 million with no liabilities. The excess of purchase price less tangible assets acquired totaling $4.9 million was recorded as goodwill. Total goodwill was approximately $9.5 million for both years ended June 30, 2019 and 2018.

Note 7 – Other Assets

Other assets consisted of the following as of June 30:

	2019	2018
Medical office building deposits	$ 16,908,114	$ 21,965,359
Other	1,329,147	1,388,050
Total	$ 18,237,261	$ 23,353,409

Medical office building deposits of approximately $16.9 million and $22.0 million as of June 30, 2019 and 2018, are reflected in other assets in the accompanying statements of net position. Included in medical office building deposits as of June 30, 2018, are payments of approximately $5.0 million to the developer of an on-campus medical office building and $17.0 million to the State of California Treasurer. In fiscal year 2019 a $5.1 million offset was recorded as a result of a Court of Appeals decision. See Note 14 – Commitments and Contingencies.

Note 8 – Short-Term Debt

Line of credit –The District has a revolving line of credit with Mid Cap, LLC with interest at the London Interbank Offered Rate ("LIBOR") plus 3.50% subject to a LIBOR floor of 1%. The maturity date of the revolving line of credit was August 31, 2019. The amount available under this revolving line of credit as of June 30, 2019, was $13.6 million and is fully collateralized by certain assets of the District. The revolving line of credit was amended subsequent to June 30, 2019. See Note 15 – Subsequent Events.

The District's revolving line of credit facility is subject to compliance with certain debt covenants, including restrictions on additional indebtedness and a minimum fixed charge coverage ratio.

Note 8 – Short-Term Debt (continued)

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

	2019			
	Beginning Balance	Additions	Payments	Ending Balance
Line of credit	$ 7,442,249	$ 404,138,227	$ (401,505,353)	$ 10,075,123
Promissory note	3,000,000	-	(3,000,000)	-
Total short-term debt	$ 10,442,249	$ 404,138,227	$ (404,505,353)	$ 10,075,123

	2018			
	Beginning Balance	Additions	Payments	Ending Balance
Line of credit	$ 2,522,076	$ 405,520,641	$ (400,600,468)	$ 7,442,249
Insurance financing	-	1,609,351	(1,609,351)	-
Promissory note	-	6,000,000	(3,000,000)	3,000,000
Total short-term debt	$ 2,522,076	$ 413,129,992	$ (405,209,819)	$ 10,442,249

Note 9 – Long-Term Debt

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

- Lancaster Pollard Mortgage Company, HUD insured loan, interest rate of 4.32%, with principal balance outstanding of approximately $81.5 million and $83.5 million as of June 30, 2019 and 2018, respectively. Principal and interest payments of approximately $468 thousand are due monthly with the remaining aggregate unpaid amount due April 2042. A mortgage reserve fund (MRF) is required under the Hospital Regulatory Agreement between the District and HUD. The District makes deposits into the MRF trust account in accordance with the MRF agreement.

- Bank of the West note payable, interest rate of 3.12%, with principal balance outstanding of approximately $39 thousand and $502 thousand as of June 30, 2019 and 2018, respectively. Principal and interest payments of approximately $39 thousand are due monthly commencing July 2016 with the remaining aggregate unpaid amount due July 2019. The note is collateralized by certain capital assets of the District.

Note 9 – Long-Term Debt (continued)

- Various capital equipment leases with interest rates varying between 2.73% and 4.83%. Principal and interest payments due monthly commencing and expiring on various dates ranging from October 2020 through June 2022. Principal balances due totaled approximately $2.5 million and $3.8 million as of June 30, 2019 and 2018, respectively.

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

	2019				
	Beginning Balance	Additions	Payments	Ending Balance	Due Within 1 Year
Lancaster (HUD) mortgage debt	$ 83,541,179	$ -	$ (2,051,123)	$ 81,490,056	$ 2,141,507
Bank of the West notes payable	501,982	-	(462,765)	39,217	39,217
Total long-term debt	84,043,161	-	(2,513,888)	81,529,273	2,180,724
Capital lease obligations	3,771,788	-	(1,265,842)	2,505,946	1,200,723
Total long-term debt	$ 87,814,949	$ -	$ (3,779,730)	$ 84,035,219	$ 3,381,447

	2018				
	Beginning Balance	Additions	Payments	Ending Balance	Due Within 1 Year
Lancaster (HUD) mortgage debt	$ 85,505,732	$ -	$ (1,964,553)	$ 83,541,179	$ 2,051,123
Bank of the West notes payable	1,380,944	-	(878,962)	501,982	501,982
Total long-term debt	86,886,676	-	(2,843,515)	84,043,161	2,553,105
Capital lease obligations	5,350,737	-	(1,578,949)	3,771,788	1,273,993
Total long-term debt	$ 92,237,413	$ -	$ (4,422,464)	$ 87,814,949	$ 3,827,098

Note 9 – Long-Term Debt (continued)

A schedule, by year, of future minimum payments under long-term debt and capital lease obligations as of June 30, 2019, is as follows:

Years Ending June 30,	Principal	Interest	Total
2020	$ 3,381,447	$ 3,542,341	$ 6,923,788
2021	3,214,020	3,408,483	6,622,503
2022	2,661,476	3,290,333	5,951,809
2023	2,437,266	3,182,539	5,619,805
2024	2,544,666	3,075,140	5,619,806
Thereafter	69,796,344	30,423,523	100,219,867
Total	$ 84,035,219	$ 46,922,359	$ 130,957,578

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

	2019	2018
Equipment under capital lease	$ 6,462,122	$ 7,320,305
Accumulated amortization	(4,037,198)	(3,411,181)
Total	$ 2,424,924	$ 3,909,124

Note 10 – 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, 2019, there were a total of 1,235 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 $5.7 million and $6.0 million for years ended June 30, 2019 and 2018, 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, 2019 and 2018, forfeitures reduced the District's expenses and contributions under the Plan by approximately $96 thousand and $106 thousand, respectively.

Note 10 – Retirement Plans (continued)

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 $89 thousand and $85 thousand for years ended June 30, 2019 and 2018, respectively.

The District's contributions to NSRP totaled approximately $2.1 million and $2.3 million for the years ended June 30, 2019 and 2018, 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.

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 statements of net position as of June 30, 2019 and 2018.

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, 2019 and 2018, the balance of capital accumulation funds was approximately $348 thousand and $292 thousand, respectively, which is included in prepaid expenses and other assets on the accompanying statements of net position. The corresponding compensation liabilities of approximately $445 thousand and $395 thousand as of June 30, 2019 and 2018, respectively, are included in accrued payroll and related expenses on the accompanying 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 11 – Operating Leases

The District leases certain building space and equipment under non-cancelable operating leases expiring between October 2018 and June 2027. Operating lease expense for all operating leases totaled approximately $4.0 million and $4.1 million for the years ended June 30, 2019 and 2018, respectively.

Note 11 – Operating Leases (continued)

As of June 30, 2019, future minimum lease payments under non-cancelable operating leases are as follows:

Years Ending June 30,	
2020	$ 3,215,954
2021	2,528,834
2022	1,528,558
2023	679,853
2024	607,379
Thereafter	1,909,596
Total	$ 10,470,174

Note 12 – 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 Board members and officers of each of the two organizations are selected solely by the members themselves.

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 $619 thousand and $752 thousand in the years ended June 30, 2019 and 2018, respectively.

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

	2019	2018
Tri-City Hospital Foundation		
Assets	$ 5,454,930	$ 4,151,660
Liabilities	$ 158,792	$ 114,449
Net Assets	$ 5,296,138	$ 4,037,211
Tri-City Hospital Auxiliary		
Assets	$ 498,616	$ 516,220
Liabilities	$ 3,408	$ 2,792
Net Assets	$ 495,208	$ 513,428

Note 13 – Partnerships

During the year ended June 30, 2010, the District entered into a general partnership with Surgical Care Affiliates of Oceanside to form ASCO. 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 outpatient surgeries to the surgery center in order to free up surgical suite time for surgeries requiring hospital surgical services. As described in Note 1, ASCO is considered to be a blended component unit of the District. As a result, the financial results of ASCO have been included in the District's financial statements.

Also during the year ended June 30, 2010, the District formed the Cardiovascular Institute. The purpose of the Cardiovascular Institute 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 the Cardiovascular Institute entered into a co-management agreement under which the Cardiovascular Institute provides certain services to meet this mission.

During the year ended June 30, 2011, the District formed the Orthopedic Institute. The purpose of the Orthopedic Institute 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 the Orthopedic Institute entered into a co-management agreement under which the Orthopedic Institute provides certain services to meet this mission.

During the year ended June 30, 2012, the District formed REHM. The purpose of the REHM was to facilitate the acquisition and use of real estate properties. During the year ended June 30, 2019, the District dissolved REHM and the assets were transferred to the District.

During the year ended June 30, 2015, the District formed Tri-City Wellness Center, LLC, a California Limited Liability Company, to purchase the Wellness Center, which the District had previously operated under a capital lease.

During the year ended June 30, 2015, the District formed the Tri-City Medical Center Neuroscience Institute, LLC ("Neuro Institute"), 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 the change in net position attributable to minority interests in these entities totaled approximately $1.6 million for both years ended June 30, 2019 and 2018.

Note 14 – 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 14 – Commitments and Contingencies (continued)

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 an on-campus medical office building. The developer filed a complaint against the District and the District filed a cross complaint. 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. The District deposited $4.7 million in 2015 and an additional $12.3 million in 2017 related to the verdict. The District filed a notice of abandonment of its eminent domain claim subsequent to the verdict. The trial court set aside (nullified) the abandonment. The District appealed from the judgement and from the order setting aside the abandonment. During fiscal 2019, the Court of Appeal affirmed the award of damages but reversed the trial court's order setting aside the District's abandonment of the eminent domain claim and remanded the case to the superior court to effectuate the District's abandonment of the eminent domain proceeding. The District recorded a $5.1 million non-operating charge in 2019 related to the damages and related fees portion of the judgement and is seeking recovery of deposits made prior to the Court of Appeal's decision. The $5.1 million charge is reflected as an offset to deposits as of June 30, 2019. See Note 7 – Other Assets. Disputes remain between the Developer and the District based on the District's now lawfully abandoned condemnation action and both contend entitlement to damages.

Seismic compliance – 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.

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.

Workers' compensation – 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 unlikely. 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, 2019, the District maintains nonnegotiable certificates of deposit totaling $15 thousand for calendar year 2003 and $302 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 2019. Such reserves were approximately $8.1 million and $8.5 million as of June 30, 2019 and 2018, respectively.

Note 14 – Commitments and Contingencies (continued)

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 $1.0 million effective July 1, 2009. The District has reserved for estimated IBNR claims through June 30, 2019. Such reserves were approximately $3.2 million and $2.9 million as of June 30, 2019 and 2018, respectively.

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

Balance as of June 30, 2017	$ 11,212,133
Additions	3,384,926
Payments	(3,174,556)
Balance as of June 30, 2018	11,422,503
Additions	2,575,257
Payments	(2,663,415)
Balance as of June 30, 2019	$ 11,334,345

Medical services IBNR – The following is a summary of the changes in the medical services IBNR claims, included in accounts payable and accrued liabilities in the accompanying statement of net position for the years ended June 30:

Balance as of June 30, 2017	$ 4,219,453
Additions	8,060,212
Payments	(10,770,462)
Balance as of June 30, 2018	1,509,203
Additions	6,396,496
Payments	(6,437,924)
Balance as of June 30, 2019	$ 1,467,775

Note 14 – Commitments and Contingencies (continued)

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 $3.0 million and $4.4 million as of June 30, 2019 and 2018, respectively. The balance is included in other long-term assets in the accompanying statements of net position.

Note 15 – Subsequent Events

Effective August 30, 2019, the District amended the MidCap Credit and Security Agreement increasing the revolving line of credit to $15.4 million, decreasing the interest rate to LIBOR plus 3%, and extending the maturity date to August 30, 2022.

Supplementary Information

Tri-City Healthcare District
Schedule of Net Position
June 30, 2019

	Tri-City Medical Center	ASCO	REHM	Wellness Center	Cardiovascular Institute	Orthopedic Institute	Neuro Institute	Eliminations	TOTAL
ASSETS									
CURRENT ASSETS									
Cash and cash equivalents	$ 43,700,232	$ 863,970	$ -	$ 282,637	$ 95,836	$ 68,053	$ 13,017	$ -	$ 45,023,745
Short-term investments	5,930,724	-	-	-	-	-	-	-	5,930,724
Restricted cash and investments	298,000	-	-	-	-	-	-	-	298,000
Patient accounts receivable, net	42,866,462	1,146,225	-	-	-	-	-	-	44,012,687
Other receivables	1,843,933	-	-	-	397,450	6,414	22,696	(251,291)	2,019,202
Supplies inventory	9,419,777	1,269	-	-	-	-	-	-	9,421,046
Prepaid expenses and other assets	3,439,397	190,480	-	7,061	-	-	-	-	3,636,938
Estimated third-party payor settlements	3,850,532	-	-	-	-	-	-	-	3,850,532
Total current assets	111,349,057	2,201,944	-	289,698	493,286	74,467	35,713	(251,291)	114,192,874
NON-CURRENT INVESTMENTS									
Board-designated	407,795	-	-	-	-	-	-	-	407,795
CAPITAL ASSETS - net	97,961,469	708,757	-	-	-	-	-	-	98,670,226
OTHER ASSETS									
Notes receivable	3,015,138	-	-	-	-	-	-	-	3,015,138
Restricted mortgage reserve fund	7,530,972	-	-	-	-	-	-	-	7,530,972
Goodwill	9,529,430	-	-	-	-	-	-	-	9,529,430
Other	18,071,108	-	-	-	83,665	36,221	46,267	-	18,237,261
Total other assets	38,146,648	-	-	-	83,665	36,221	46,267	-	38,312,801
Total Assets	$ 247,864,969	$ 2,910,701	$ -	$ 289,698	$ 576,951	$ 110,688	$ 81,980	$ (251,291)	$ 251,583,696

See accompanying report of independent auditors.

Tri-City Healthcare District
Schedule of Net Position (Continued)
June 30, 2019

	Tri-City Medical Center	ASCO	REHM	Wellness Center	Cardiovascular Institute	Orthopedic Institute	Neuro Institute	Eliminations	TOTAL
LIABILITIES AND NET POSITION									
CURRENT LIABILITIES									
Accounts payable and accrued liabilities	$ 44,504,095	$ 218,825	$ -	$ 7,500	$ 131,874	$ 32,027	$ -	$ (251,291)	$ 44,643,030
Accrued payroll and related expenses	19,548,801	256,795	-	-	-	-	-	-	19,805,596
Current maturities of long-term debt	3,381,447	-	-	-	-	-	-	-	3,381,447
Short-term debt	10,075,123	-	-	-	-	-	-	-	10,075,123
Other current liabilities	1,659,346	451,003	-	-	-	-	-	-	2,110,349
Total current liabilities	79,168,812	926,623	-	7,500	131,874	32,027	-	(251,291)	80,015,545
LONG-TERM DEBT - net of current position	80,653,772	-	-	-	-	-	-	-	80,653,772
WORKERS' COMPENSATION AND COMPREHENSIVE LIABILITY - net of current portion	7,955,184	-	-	-	-	-	-	-	7,955,184
Total liabilities	167,777,768	926,623	-	7,500	131,874	32,027	-	(251,291)	168,624,501
NET POSITION									
Invested in capital assets - net of related debt	16,067,756	708,757	-	-	-	-	-	-	16,776,513
Restricted assets	7,530,972	1,355,522	-	282	171,978	39,331	26,234	-	9,124,319
Unrestricted	56,488,473	(80,201)	-	281,916	273,099	39,330	55,746	-	57,058,363
Total net position	80,087,201	1,984,078	-	282,198	445,077	78,661	81,980	-	82,959,195
Total liabilities and net position	$247,864,969	$ 2,910,701	$ -	$ 289,698	$ 576,951	$ 110,688	$ 81,980	$ (251,291)	$251,583,696

Tri-City Healthcare District
Schedule of Revenues, Expenses, and Changes in Net Position
For the Year Ended June 30, 2019

	Tri-City Medical Center	ASCO	REHM	Wellness Center	Cardiovascular Institute	Orthopedic Institute	Neuro Institute	Eliminations	Total
OPERATING REVENUE									
Net patient service revenue	$ 318,694,722	$ 11,178,566	$ -	$ -	$ -	$ -	$ -	$ -	$ 329,873,288
Premium revenue	18,934,440	-	-	-	-	-	-	-	18,934,440
Other revenue	8,970,873	2,210	-	108,835	463,697	(255,500)	(150,000)	(1,073,921)	8,066,194
Total operating revenue	346,600,035	11,180,776	-	108,835	463,697	(255,500)	(150,000)	(1,073,921)	356,873,922
OPERATING EXPENSES									
Salaries and related expenses	191,971,410	2,935,686	-	-	-	-	-	-	194,907,096
Supplies	71,139,271	2,946,617	-	-	-	-	-	-	74,085,888
Purchased services	20,034,772	831,115	-	-	-	-	-	(58,199)	20,807,688
Depreciation and amortization	11,834,213	259,920	-	-	8,933	-	-	-	12,103,066
Other operating expense	20,590,707	586,308	-	7,113	3,777	-	56	-	21,187,961
Professional and medical fees	22,334,467	56,188	-	-	96,431	-	-	-	22,487,086
Maintenance, rent & utilities	16,880,675	834,249	-	-	-	-	-	-	17,714,924
Total operating expenses	354,785,515	8,450,083	-	7,113	109,141	-	56	(58,199)	363,293,709
(LOSS) INCOME FROM OPERATIONS	(8,185,480)	2,730,693	-	101,722	354,556	(255,500)	(150,056)	(1,015,722)	(6,419,787)
NON-OPERATING REVENUE (EXPENSE)									
District tax revenue	10,927,012	-	-	-	-	-	-	-	10,927,012
Interest income	755,943	9,041	-	-	-	-	-	-	764,984
Interest expense	(4,544,617)	(10,037)	-	-	-	-	-	-	(4,554,654)
Other non-operating income (expense)	(4,936,364)	-	-	-	-	-	-	-	(4,936,364)
Total non-operating revenue (expense)	2,201,974	(996)	-	-	-	-	-	-	2,200,978
CHANGE IN NET POSITION BEFORE MINORITY INTEREST (EROE)	(5,983,506)	2,729,697	-	101,722	354,556	(255,500)	(150,056)	(1,015,722)	(4,218,809)
Minority interest distributions - net		(1,696,269)	(11,618)	-	(128,081)	-	(8,050)	-	(1,844,018)
Distributions between related entities	1,069,700	(798,764)	(2,294,700)	-	(216,960)	-	-	2,240,724	-
CHANGE IN NET POSITION	(4,913,806)	234,664	(2,306,318)	101,722	9,515	(255,500)	(158,106)	1,225,002	(6,062,827)
NET POSITION - Beginning of year	85,001,007	1,749,414	2,306,318	180,476	435,562	334,161	240,086	(1,225,002)	89,022,022
NET POSITION - End of year	$ 80,087,201	$ 1,984,078	$ -	$ 282,198	$ 445,077	$ 78,661	$ 81,980	$ -	$ 82,959,195

See accompanying report of independent auditors.

MORTGAGE RESERVE FUND	
Amount required in the mortgage reserve fund at June 30, 2019	$ 7,512,062
Balance of the mortgage reserve fund at June 30, 2019	7,530,972
Excess Fund Balance	$ (18,910)

Single Audit Reports and Related Schedules

MOSSADAMS

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

The Board of Directors
Tri-City Healthcare District

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Tri-City Healthcare District (the "District"), which comprise the statement of net position as of June 30, 2019, and the related statements of revenues, expenses, and change in net position and cash flows for the year then ended, and the related notes to the financial statements and have issued our report thereon dated September 18, 2019.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of this Report

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

Moss Adams LLP

Irvine, California
September 18, 2019

MOSSADAMS

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

The Board of Directors
Tri-City Healthcare District

Report on Compliance for the Major Federal Program

We have audited Tri-City Healthcare District's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on Tri-City Healthcare District's major federal program for the year ended June 30, 2019. Tri-City Healthcare District's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

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

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

Opinion on the Major Federal Program

In our opinion, Tri-City Healthcare District complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2019.

Report on Internal Control Over Compliance

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

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

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

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

Moss Adams LLP

Irvine, California
September 18, 2019

Tri-City Healthcare District
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2019

Federal Grantor/Pass Through Grantor/ Program or Cluster Title	CFDA Number	Pass Through Entity Identifying Number	Federal Expenditures	Passed through to Subrecipients
U.S. Department of Housing and Urban Development				
Direct:				
Mortgage Insurance_Hospitals	14.128	N/A	$ 83,541,179	$ -
Total U.S. Department of Housing and Urban Development			83,541,179	-
Total Expenditures of Federal Awards			$ 83,541,179	$ -

See accompanying notes to the Schedule of Expenditures of Federal Awards.

Note 1 – Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of Tri-City Healthcare District (the "District") under programs of the federal government for the year ended June 30, 2019. The information in this schedule is presented in accordance with the requirements of the Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the schedule presents only a selected portion of the operations of the District, it is not intended to and does not present the financial position, results of operations, or cash flow of the District.

The District's reporting entity is defined in Note 1 of the financial statements. All federal awards from federal agencies are included in the Schedule.

Note 2 – Summary of Significant Accounting Policies

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

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

Note 3 – Loan Balance

Loans outstanding at the beginning of the year plus the new value of new loans received during the year are included in the federal expenditures presented in the schedule of expenditures of federal awards. The balance of the loans outstanding as of June 30, 2019, consists of:

Program name	Section 242 - Mortgage Insurance for Hospitals
CFDA number	14.128
Loans outstanding as of June 30, 2018	$ 83,541,179
Loans awarded during the year ended June 30, 2019	-
Less: principal repaid	(2,051,123)
Loan outstanding as of June 30, 2019	$ 81,490,056

Section I – Summary of Auditor's Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP:	*Unmodified*
Internal control over financial reporting:	
• Material weakness(es) identified?	☐ Yes ☒ No
• Significant deficiency(ies) identified?	☐ Yes ☒ None reported
Noncompliance material to financial statements noted?	☐ Yes ☒ No

Federal Awards

Internal control over major federal programs:	
• Material weakness(es) identified?	☐ Yes ☒ No
• Significant deficiency(ies) identified?	☐ Yes ☒ None reported
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	☐ Yes ☒ No

Identification of major federal programs and type of auditor's report issued on compliance for major federal programs:

CFDA Number(s)	*Name of Federal Program or Cluster*	*Type of Auditor's Report Issued on Compliance for Major Federal Programs*
14.128	Mortgage Insurance_Hospitals	Unmodified

Dollar threshold used to distinguish between Type A and Type B programs:	$ 750,000
Auditee qualified as low-risk auditee?	☒ Yes ☐ No

Section II – Financial Statement Findings

None reported.

Section III – Federal Award Findings and Questioned Costs

None reported.