

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Financial Report
December 31, 2018

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RSM US LLP

Independent Auditor's Report

To the Board of Directors
North Sonoma County Healthcare District

Report on the Financial Statements

We have audited the accompanying financial statements of the North Sonoma County Healthcare District d/b/a Healdsburg District Hospital (the Hospital) as of and for the years ended December 31, 2018 and 2017, and the related notes to the financial statements, which collectively comprise the Hospital's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit 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 Hospital'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 Hospital'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 North Sonoma County Healthcare District as of December 31, 2018 and 2017, and the changes in its financial position 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 3–10 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

RSM US LLP

Davenport, Iowa

June 27, 2019

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Management's Discussion and Analysis
Year Ended December 31, 2018**

North Sonoma County Healthcare District is a special healthcare district, a political subdivision of the State of California, which owns and operates Healdsburg District Hospital (Hospital) located in Healdsburg, County of Sonoma, State of California. In 2018, the Hospital staffed 38 beds (21 acute medical/surgical beds and 17 distinct part skilled nursing beds) and provided a continuum of medical and surgical inpatient care, as well as diagnostic, therapeutic and clinical outpatient services. The Hospital staffing was an average of 264 full-time equivalent employees (FTE's) in 2018, up from 247 in 2017.

Financial Highlights

- The Hospital experienced a decrease in net position after three straight years of profitability. Our focus continued to be on building operational sustainability through the delivery of quality patient care, optimization of operating and financial systems, and intensive cash and debt management while seeking out strategic business growth opportunities. The Hospital expects the investments made in both staffing and capital in 2018 will help deliver improved operational and financial performance in years to come.
- The Hospital drew down the remaining \$7,504,000 on its 2016 Certificates of Participation (COP), which is restricted for capital. Overall, \$4,197,000 was spent on capital in 2018, allowing the Hospital to make significant upgrades in both facilities and equipment to better serve our patients.
- In addition to the capital spending noted above, the Hospital paid down \$1,218,000 of debt in 2018, provided market basket rate and wage increases to staff, and hired an additional physician (five now employed), while still increasing the total deposits and investments by \$8,228,000. \$7,874,000 of the Hospital's cash and investments is restricted or designated, and \$7,460,000 is unrestricted and can be used at the Hospital's discretion. The year-end cash and cash equivalents at the Hospital is greater than it has been in over eight years.
- Current assets and current liabilities were consistent with 2017, with a strong current ratio of 2.21.

Financial Reporting Entity

The definition of the reporting entity is based on the principal of financial accountability. A primary government entity is financially accountable for the organizations that make up that legal entity. It is also financially responsible for legally separate corporations that have the potential to provide specific financial benefits to, or impose specific financial burdens, on the primary government entity. The financial reporting entity for this report consists of the primary government entity, the North Sonoma County Healthcare District, which is comprised of Healdsburg District Hospital and North Sonoma County Healthcare Services.

Overview of Financial Statements

Management's Discussion and Analysis is designed to assist the reader in understanding the audited financial statements and provides an overview of the Hospital's financial position and significant financial and operational issues. Please read it in conjunction with the audited financial statements.

Unless otherwise noted, all discussion and analysis pertains to the Hospital's financial condition, operating results, and cash flows, as of, and for the year ended December 31, 2018.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Management's Discussion and Analysis
Year Ended December 31, 2018**

The financial statements and related information disclosed in the Notes to the Financial Statements are presented in accordance with the pronouncements of the Governmental Accounting Standards Boards (GASB) and follow the guidelines of the American Institute of Certified Public Accountants (AICPA) for Health Care Organizations.

Hospital Financial Statements

The Financial Statements are designed to provide readers with a broad overview of the Hospital's finances. Hospital Districts are defined as "special purpose governments engaged only in business activities." Approximately 94 percent of the Hospital's operations were financed through service revenue. The Hospital also receives parcel tax revenue. Unlike some governmental entities, the Hospital's financial statements are comprehensive, reflect all financial interests and are similar to most hospitals and other business entities. The statements are prepared utilizing enterprise fund accounting on an accrual basis of accounting using the economic resources measurement focus.

The financial statements include the following:

The statement of net position, also known as a balance sheet, presents information on all of the Hospital's Assets, Deferred Outflows, Liabilities, Deferred Inflows and Net Position. The balance sheet includes information about the nature of the Hospital's assets and liabilities and classifies them as current or noncurrent. It also provides the basis for evaluation of the capital structure of the Hospital, and for assessing its liquidity and financial flexibility. Over time, increases or decreases in Net Position serve as a useful indicator of whether the financial position of the Hospital is improving or deteriorating.

The statement of revenue, expenses and changes in net position presents information on the results of the Hospital's operations, its tax support and any contributions during each fiscal year. All changes in revenues and expenses are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the statement for some items that will result in cash flows in future fiscal periods (for example, patient charges billed but not collected, earned but unused vacation leave), or result from past cash flows (for example, prepaid insurance, supplies issued from inventory). This statement measures the Hospital's operations and can be used to determine whether the Hospital has been able to recover all of its operating costs from patient services and other revenue sources.

The primary purpose of the statement of cash flows is to provide information about the Hospital's cash from operating, noncapital financing, capital and related financing, and investing activities. It provides answers to such questions as the Hospital's sources of cash, what was the cash used for, and what were the changes in cash balances during the reporting period.

Following the audited financial statements, please find the notes to the financial statements, which provide additional information essential for a full understanding of the information in the financial statements. The notes also present certain required information such as the Hospital's concentration of credit risk, transactions with related organizations, capital asset and long-term debt activity.

The financial statements report historic results and provide a picture of the Hospital's financial performance and position as a point in time. While they provide an indicator of financial health, the reader will need to consider at a minimum other nonfinancial factors such as changes in the Hospital's patient or physician base, economic factors such as changes in reimbursements, the impact of federal and state legislation on healthcare delivery and financing, and planned changes in the programs or services of the Hospital in order to assess the overall health of the Hospital going forward.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Management's Discussion and Analysis
Year Ended December 31, 2018**

Financial and Operating Highlights

The following discussion provides a summary explanation of the financial position of the Hospital and the results of the Hospital's operations in 2018, and the changes from 2017 shown in the following tables and the Audited Financial Statements.

Condensed Statement of Net Position

	2018	2017	2016	2017 vs 2018	
				Amount	Percent
Assets					
Current assets	\$ 16,431,352	\$ 15,839,490	\$ 13,879,680	\$ 591,862	3.7%
Noncurrent assets and deferred outflows	17,176,483	11,131,063	9,245,958	6,045,420	54.3%
Total assets	\$ 33,607,835	\$ 26,970,553	\$ 23,125,638	\$ 6,637,282	24.6%
Liabilities and Net Position					
Accounts payable, accrued expenses and estimated third-party payor settlements	\$ 6,678,779	\$ 6,535,561	\$ 6,553,230	\$ 143,218	2.2%
Notes and capital leases payable, current	746,000	1,217,980	1,005,513	(471,980)	(38.8%)
Notes and capital leases payable and workers' compensation, long-term and deferred inflows	12,928,000	5,932,032	6,426,509	6,995,968	117.9%
Net position	13,255,056	13,284,980	9,140,386	(29,924)	(0.2%)
Total liabilities and net position	\$ 33,607,835	\$ 26,970,553	\$ 23,125,638	\$ 6,637,282	24.6%

Total assets and deferred outflows, and total liabilities and net position increased 24.6 percent.

Within current assets, increases in cash of \$4,545,000 used to support operations were offset by decreases in estimated third-party payor settlements of \$4,668,000. The decrease in estimated third-party payor settlements and increase in cash was primarily the result of the receipt of a favorable settlement with a Medi-Cal managed care payor in 2018.

The increase in noncurrent assets and deferred outflows resulted primarily from the increase in noncurrent assets limited to use in the amount of \$3,843,000 as remaining funds restricted for capital from the 2016 COP exceeded the funds spent on the new MRI. There was also an increase in net capital assets of \$2,337,000 as additions to capital assets significantly exceeded depreciation. See Note 5 in the financial statements for details regarding assets limited as to use and Note 6 for details on capital assets.

Total current liabilities were consistent with 2017, just a 4.2 percent decrease. Long-term liabilities and deferred inflows increased 49.0 percent as the issuance of funds from the 2016 COP was offset by scheduled payments on the capital lease and COP of \$1,218,000. The capital lease was paid off in 2018.

Net Position (Total Assets and Deferred Outflows less Total Liabilities and Deferred Inflows) decreased by \$30,000 or 0.23 percent. The decrease in restricted net position of \$1,780,000 was partially offset by increases in unrestricted net position and net investment in capital assets of \$318,000 and \$1,432,000, respectively.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Management's Discussion and Analysis
Year Ended December 31, 2018**

Condensed Statement of Revenues, Expenses and Changes in Net Position

	2018	2017	2016	2017 vs 2018	
				Amount	Percent
Operating revenues, net	\$ 50,925,073	\$ 48,491,365	\$ 44,095,112	\$ 2,433,708	5.0%
Operating expenses	54,226,389	49,747,205	45,809,315	4,479,184	9.0%
Operating loss	(3,301,316)	(1,255,840)	(1,714,203)	(2,045,476)	162.9%
Nonoperating revenues, net	3,258,792	3,122,242	3,151,915	136,550	4.4%
Gain (loss) before capital contributions	(42,524)	1,866,402	1,437,712	(1,908,926)	(102.3%)
Capital contributions for acquisition of equipment	12,600	2,278,192	349,000	(2,265,592)	(99.4%)
Change in net position	(29,924)	4,144,594	1,786,712	(4,174,518)	(100.7%)
Net position, beginning of year	13,284,980	9,140,386	7,353,674	4,144,594	45.3%
Net position, end of year	\$ 13,255,056	\$ 13,284,980	\$ 9,140,386	\$ (29,924)	(0.2%)

The Hospital experienced the first year of a decrease in net position after three straight years of increases. Below are some of the key factors that contributed to the results.

The increase in total operating revenues, net was primarily due to increases in net patient service revenue of \$2,434,000. Increased supplemental funding from the Medi-Cal Hospital Quality Assurance Fee (HQAF) accounted for the increase.

Total operating expenses increased \$4,479,000, or 9.0 percent due to the following:

- The most significant expense for any Hospital relates to staffing. Salaries and wages, and employee benefits increased \$3,483,000, or 12.6 percent. In addition to an increase in FTE's of 17, we increased our payroll by the provision of market basket rate increases and wage adjustments for many positions in the organization and hired one additional physician (five employed physicians in total). We also had increases in both paid time off (PTO) and payroll taxes due to the market basket rate and wage increases provided to the staff in 2018. We also recognized an additional \$654,000 in expense in 2018 from our self-insured employee health program.
- Supplies expense increased \$1,200,000, or 23.8 percent. The increase was primarily a result of increased surgery department costs for implants in the amount of \$838,000. Outpatient surgeries increased by 1,711 in 2018, an increase in the number of procedures by 186.2 percent.
- Registry and other professional fees decreased \$392,000 due to a concerted shift from agency to employee staffing.

Nonoperating revenues consist primarily of parcel taxes in the amount of \$3,391,000 net of interest expense of \$314,000, both of which were consistent with 2017.

Other nonoperating revenues come primarily from donations. In 2017, the Hospital received \$2,273,000 of grant funds from the Foundation, which were used for the purchase of a new MRI in 2018. In 2018, the Hospital received \$220,000 in unrestricted contributions from the Foundation.

The change in net position is the sum of the operating loss plus net nonoperating revenues, plus the capital contributions. The Hospital net position decreased \$30,000 in 2018.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Management's Discussion and Analysis
Year Ended December 31, 2018**

Condensed Statement of Cash Flows

	2018	2017	2016	2017 vs 2018	
				Amount	Percent
Cash flows provided by (used in) operating activities	\$ 2,813,022	\$ (3,280,831)	\$ (1,985,376)	\$ 6,093,853	(185.7%)
Cash flows provided by noncapital financing activities	3,391,426	3,397,114	3,324,257	(5,688)	(0.2%)
Cash flows provided by (used in) capital and related financing activities	1,851,968	666,351	(2,774,638)	1,185,617	177.9%
Cash flows provided by (used in) investing activities	(3,511,619)	(3,727,655)	2,982,652	216,036	(5.8%)
Net change in cash and cash equivalents	4,544,797	(2,945,021)	1,546,895	7,489,818	(254.3%)
Cash and cash equivalents:					
Beginning of year	2,811,902	5,756,923	4,210,028	(2,945,021)	(51.2%)
End of year	<u>\$ 7,356,699</u>	<u>\$ 2,811,902</u>	<u>\$ 5,756,923</u>	<u>\$ 4,544,797</u>	<u>161.6%</u>
Reconciliation of operating loss to net cash provided by (used in) operating activities:					
Operating loss	\$ (3,301,316)	\$ (1,255,840)	\$ (1,714,203)	\$ (2,045,476)	162.9%
Adjustments to reconcile	6,114,338	(2,024,991)	(271,173)	8,139,329	(401.9%)
Net cash provided by (used in) operating activities	\$ 2,813,022	\$ (3,280,831)	\$ (1,985,376)	\$ 6,093,853	(185.7%)

Cash and cash equivalents totaled \$7,357,000 compared to \$2,812,000 in 2017. The \$2,813,000 of cash provided by operating activities was largely a product of the settlement with a Medi-Cal managed care payor in excess of increased payments to employees and vendors. Cash flows from noncapital financing activities of \$3,391,000 consist exclusively of the Hospital's parcel tax. The cash flows from capital and related financing activities of \$1,852,000 was a result of the issuance of the 2016 COP funds exceeding purchases of capital assets and principal and interest payments for debt. The cash used in investing activities was primarily from additional funds being restricted for capital from the unspent portions of the 2016 COP's exceeding the amounts that were spent in 2018 that were restricted for the MRI project.

Capital Assets

The Hospital's capital assets increased by \$2,337,000 or 31.0 percent in 2018 due to asset acquisitions of \$4,197,000 (of both equipment and facility additions) in excess of depreciation of \$1,845,000. (See Note 6 in the Audited Financial Statements for information on capital assets.)

In spite of the significant investment made in 2018, continued capital investment will still be needed in the next few years to further replace aging assets, build new capacity and meet new technology needs for patient care. The Hospital implemented an electronic medical records system, which required a large capital outlay and significant retooling of operations in order to make best use of the technology. This technology has practically become a mandate (by the American Recovery & Reinvestment Act of 2009) for healthcare providers, and is an ongoing requirement the Hospital will have to address.

**North Sonoma County Healthcare District
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**Management's Discussion and Analysis
Year Ended December 31, 2018**

Debt

During 2016, the Hospital issued the 2016 COP (tax exempt bonds) in the amount of \$12,440,000 to refund the 2008 COP in the amount of \$4,936,000 and obtain additional funding for the purposes of improvement, renovation, replacement and equipping of the Hospital. In 2018, the Hospital drew down the remaining \$7,504,000 on the COP for the purposes mentioned above. The Hospital also paid off the final \$490,000 remaining on a \$1,781,000 capital lease in 2018. (See Note 7 in the Audited Financial Statements for details of the Hospital's debt.)

Operating Statistics

The table below presents the Hospital's key patient activity levels in 2016, 2017 and 2018.

	2018	2017	2016	2017 vs 2018	
				Amount	Percent
Inpatient statistics:					
Acute care admissions	478	569	615	(91)	(16.0%)
ICU admissions	169	105	111	64	61.0%
Skilled care (SWG) admissions	65	62	54	3	4.8%
Subacute care admissions	5	13	11	(8)	(61.5%)
Total admissions	717	749	791	(32)	(4.3%)
Acute care patient days	1,666	2,096	2,698	(430)	(20.5%)
ICU patient days	779	459	345	320	69.7%
Skilled care (SWG) patient days	515	297	493	218	73.4%
Subacute care patient days	5,483	4,963	5,771	520	10.5%
Total patient days	8,443	7,815	9,307	628	8.0%
Acute/skilled % of occupancy	38.62%	35.89%	46.20%	2.73%	
Acute/skilled average daily census	8.1	7.8	9.7	0.3	3.8%
Acute/skilled average length of stay (days)	4.2	4.4	4.5	(0.2)	(5.5%)
Subacute % of occupancy	88.36%	79.98%	91.20%	8.38%	
Subacute average daily census (patients)	15.0	13.6	15.8	1.4	10.5%
Outpatient statistics:					
Surgeries	2,630	919	744	1,711	186.2%
Total emergency room visits	8,576	9,104	8,956	(528)	(5.8%)
Occupational medicine	3,814	5,655	6,461	(1,841)	(32.6%)
Total laboratory visits	7,208	8,601	8,566	(1,393)	(16.2%)
Total radiology procedures	13,639	14,321	15,530	(682)	(4.8%)
Healdsburg primary care	8,706	8,063	8,801	643	8.0%
Total outpatient visits	46,494	44,689	46,384	1,805	4.0%

- Total admissions decreased 4.3 percent in 2018, the bulk of which related to acute care.
- Total patient days increased 8.0 percent, or 628 days as a decrease in acute care was offset by increases in ICU, skilled care, and Subacute.
- Surgeries increased 186.2 percent or 1,711 surgeries, primarily in the area of pain management.

**North Sonoma County Healthcare District
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**Management's Discussion and Analysis
Year Ended December 31, 2018**

- Total occupational medicine visits decreased 32.6 or 1,841 visits as some of these were taken in through Healdsburg primary care.
- Total outpatient visits increased 4.0 percent or 1,805 visits. In addition to the changes noted in the graph above, increases in specialty medical clinic visits were also offset by decreases in wound care clinic visits. The Hospital has added two additional providers at Healdsburg primary care and 3 at specialty medical to expand services and improve patient care in these service lines.

Economic Factors and Outlook

Over the next several years, the Hospital will continue to evolve to keep up with the constantly shifting landscape in the healthcare industry. Currently, the Hospital receives over 72 percent of its patient revenues from Medicare and Medicaid leaving us vulnerable to any changes in Medicare and Medicaid reimbursement, or payment system transformations such as the migration towards a value based reimbursement system focused on quality and quality improvement processes. The Hospital also receives a significant amount of funding through various supplemental reimbursement and payment programs to subsidize our Medicare and Medicaid heavy payor mix, in addition to the 3 percent of patient revenues that are received from uninsured patients. The Hospital continues to focus on ensuring we are maximizing the amount of supplemental funding we qualify for as these payments are critical to the financial health of the Hospital. Changes in the political landscape at the federal or state level could place these supplemental payment programs in jeopardy of being reduced, modified or even eliminated.

In Sonoma County, each of the past five years has seen growth in the percentage of Medicare beneficiaries enrolling in Medicare managed care programs (Medicare Advantage Plans). Currently, one provider in Sonoma County holds approximately 83 percent of the market share for these programs. These enrollees are excluded from receiving any services at the Hospital other than emergency services.

Internally, the Hospital's subacute unit continues to perform very well. During 2018, the average daily census was consistently around 15 or 16 patients, with an occupancy rate between 88 percent and 94 percent. Occupancy in 2019 has been between 94 percent and 100 percent with 16 or 17 beds filled. The subacute unit provides a consistent and strong revenue stream for the Hospital.

The Hospital continues to analyze service lines to identify opportunities for growth in profitable services, look for ways to improve reimbursement and manage costs in unprofitable service lines, and evaluate opportunities for potentially new service lines. With the passage of California Assembly Bill 2024 (AB 2024), which allows Critical Access Hospitals to directly employ physicians, the Hospital has hired five physicians in the areas of general surgery, internal medicine, family medicine, cardiology, and vascular surgery (specializing in wound care).

In 2018, the Hospital made a significant investment in capital to upgrade both facilities and equipment to better serve our patients, which has continued into 2019. This was possible due to drawing down the remaining \$7,504,000 from our 2016 COP's. As of June 2019, \$4,173,000 was remaining to make further capital purchases.

In addition to the significant, routine capital improvements required to maintain facilities, equipment, electronic health records, and technology, the Hospital will be required in the next few years to address the State of California's seismic mandate. While the Hospital is not required to comply with the mandate until 2030, the sheer size, scope, and costs of complying dictate that this needs to be addressed within the next few years.

**North Sonoma County Healthcare District
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**Management's Discussion and Analysis
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Finally, in order to enhance the long-term viability of the Hospital, management and the Board of Directors continue to explore strategic partnerships that will allow us to continue our vision of enhancing the health and wellness of our community through a culture of exceptional care, collaboration, and excellence.

Financial Information Contact

This report provides a general overview of the Hospital's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Chief Financial Officer at 1375 University Ave., Healdsburg, California 95448.

Shahriar Tajbakhsh
Chief Financial Officer

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Statements of Net Position
December 31, 2018 and 2017**

	2018	2017
Assets and Deferred Outflows		
Current assets:		
Cash and cash equivalents	\$ 7,356,699	\$ 2,811,902
Assets limited as to use, current portion	695,026	812,800
Patient accounts receivable, net of allowances	5,700,970	4,771,426
Estimated third-party payor settlements	-	4,667,571
Other receivables	21,665	5,615
District tax receivables	1,585,000	1,496,910
Inventories	790,413	811,652
Prepaid expenses and other assets	281,579	461,614
Total current assets	16,431,352	15,839,490
Assets limited as to use	7,178,736	3,335,441
Capital assets:		
Nondepreciable	1,120,670	734,505
Depreciable, net	8,763,895	6,812,936
	9,884,565	7,547,441
Investments and other assets	113,182	145,565
Deferred outflows of resources, deferred charge on refunding, net	-	102,616
Total assets and deferred outflows	\$ 33,607,835	\$ 26,970,553

See notes to financial statements.

	2018	2017
Liabilities, Deferred Inflows and Net Position		
Current liabilities:		
Current maturities of long-term debt	\$ 746,000	\$ 1,217,980
Accounts payable and other accrued expenses	4,122,679	4,522,349
Accrued payroll and related liabilities	2,374,208	2,013,212
Estimated third-party payor settlements	181,892	-
Total current liabilities	7,424,779	7,753,541
Long-term debt, net of current maturities	10,438,000	3,680,122
Estimated workers' compensation liability, net of current portion	905,000	755,000
Total liabilities	18,767,779	12,188,663
Deferred inflows of resources, deferred inflows related to district tax revenues	1,585,000	1,496,910
Total liabilities and deferred inflows	20,352,779	13,685,573
Commitments and contingencies (Note 10)		
Net position:		
Net investment in capital assets	4,183,993	2,751,955
Restricted for:		
Debt service, under trust agreements	515,833	419,085
Other purposes	312,410	2,189,156
Unrestricted	8,242,820	7,924,784
Total net position	13,255,056	13,284,980
Total liabilities, deferred inflows and net position	\$ 33,607,835	\$ 26,970,553

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2018 and 2017**

	2018	2017
Operating revenues:		
Net patient service revenue, before provision for bad debt	\$ 52,244,138	\$ 49,785,158
Provision for bad debt	<u>(2,192,211)</u>	<u>(1,984,906)</u>
Net patient service revenue	50,051,927	47,800,252
Other operating revenue	<u>873,146</u>	<u>691,113</u>
Total operating revenues	<u>50,925,073</u>	<u>48,491,365</u>
Operating expenses:		
Salaries and wages	22,170,397	19,254,150
Employee benefits	8,927,555	8,360,912
Registry and other professional fees	1,954,512	2,346,895
Medical professional fees	6,313,871	6,460,919
Supplies	6,214,585	5,020,415
Purchased services	2,921,738	2,451,694
Repairs and maintenance	605,933	663,828
Utilities	481,592	437,528
Building and equipment rent	1,218,137	1,163,318
Insurance	335,410	302,708
Depreciation	1,845,223	1,717,912
Other operating expenses	<u>1,237,436</u>	<u>1,566,926</u>
Total operating expenses	<u>54,226,389</u>	<u>49,747,205</u>
Operating loss	<u>(3,301,316)</u>	<u>(1,255,840)</u>
Nonoperating revenues (expenses):		
District tax revenues	3,391,426	3,397,114
Investment gain (loss), net	(38,632)	18,493
Interest expense	(314,153)	(294,039)
Grants and contributions	<u>220,151</u>	<u>674</u>
Total nonoperating revenues, net	<u>3,258,792</u>	<u>3,122,242</u>
Gain (loss) before capital contributions	<u>(42,524)</u>	<u>1,866,402</u>
Capital contributions for acquisition of equipment	<u>12,600</u>	<u>2,278,192</u>
Change in net position	<u>(29,924)</u>	<u>4,144,594</u>
Net position:		
Beginning of year	<u>13,284,980</u>	<u>9,140,386</u>
End of year	<u>\$ 13,255,056</u>	<u>\$ 13,284,980</u>

See notes to financial statements.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Statements of Cash Flows
Years Ended December 31, 2018 and 2017**

	2018	2017
Cash flows from operating activities:		
Receipts from patients and other third-party payors	\$ 53,971,846	\$ 42,605,824
Payments to suppliers	(21,412,056)	(20,226,588)
Payments to employees	(30,586,956)	(26,888,699)
Other receipts	840,188	1,228,632
Net cash provided by (used in) operating activities	2,813,022	(3,280,831)
Cash flows provided by noncapital financing activities, district tax revenues		
	3,391,426	3,397,114
Cash flows from capital and related financing activities:		
Purchase of capital assets	(4,196,936)	(502,222)
Issuance of long-term debt	7,503,878	-
Contributions received for capital asset acquisitions	12,600	2,278,192
Principal payments on long-term debt	(1,217,980)	(1,005,513)
Interest payments on long-term debt	(249,594)	(104,106)
Net cash provided by capital and related financing activities	1,851,968	666,351
Cash flows from investing activities:		
Net change in assets limited as to use	(3,725,521)	(3,732,997)
Investment gain (loss)	(6,249)	4,668
Grants and contributions	220,151	674
Net cash used in investing activities	(3,511,619)	(3,727,655)
Net increase (decrease) in cash and cash equivalents	4,544,797	(2,945,021)
Cash and cash equivalents:		
Beginning of year	2,811,902	5,756,923
End of year	\$ 7,356,699	\$ 2,811,902

(Continued)

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

**Statements of Cash Flows (Continued)
Years Ended December 31, 2018 and 2017**

	2018	2017
Reconciliation of operating loss to net cash provided by (used in) operating activities:		
Operating loss	\$ (3,301,316)	\$ (1,255,840)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities:		
Depreciation	1,845,223	1,717,912
Loss on disposal of capital assets	14,589	-
Changes in operating assets and liabilities:		
Patient accounts receivables and other receivables	(945,594)	159,591
Other current assets	180,035	27,296
Inventories	21,239	38,507
Estimated third-party payor settlements	4,849,463	(4,816,500)
Accounts payable and accrued expenses	(617)	(4,797)
Estimated workers' compensation liability	150,000	853,000
	\$ 2,813,022	\$ (3,280,831)

See notes to financial statements.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies

Nature of business: North Sonoma County Healthcare District (d/b/a Healdsburg District Hospital), heretofore referred to as the Hospital, is a public entity organized under Local Hospital District Law as set forth in the Health and Safety Code of the State of California. The Hospital is a political subdivision of the State of California and is generally not subject to federal or state income taxes. The Hospital is governed by a five-member Board of Directors, elected from within the district to specified terms of office. The Hospital is located in Healdsburg, California. It operates a 21-bed acute care facility with intensive care, a 17-bed hospital-based sub-acute nursing facility and swing bed services. The Hospital provides health care services primarily to individuals who reside in the local geographic area.

Significant accounting policies:

Accrual basis of accounting: The accrual basis of accounting is used by the Hospital. Under the accrual basis of accounting, revenue is recognized when earned and expenses are recognized when the liability has been incurred.

Basis of accounting: The financial statements of the Hospital are prepared in accordance with generally accepted accounting principles (GAAP) as applied to governmental units. The Government Accounting Standards Board (GASB) is the standard-setting body for governmental accounting and financial reporting. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards, which, along with subsequent GASB pronouncements (Statements and Interpretations), constitutes GAAP for governmental units.

Deferred inflows of resources: In addition to liabilities, the statements of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow or resources (revenue) until that time. Property taxes are shown as a deferred inflow of resources under the full accrual basis of accounting and will become an inflow in the year for which they are levied and intended for the Hospital's use.

Management estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents, and investments: For purposes of the statements of cash flows, cash and cash equivalents include deposits on account in banking institutions and certain investments in highly liquid debt instruments, when present, with an original maturity of a short-term nature or subject to withdrawal upon request, excluding cash and cash equivalents included in assets limited as to use. Exceptions are for those investments, which are intended to be continuously invested. Investments in securities are reported at fair value.

Interest, dividends and both unrealized and realized gains and losses on investments are included as investment gain (loss) in nonoperating revenues when earned.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Patient accounts receivable: Patient accounts receivable consist of amounts owed by various governmental agencies, insurance companies and private patients. The Hospital manages its receivables by regularly reviewing the accounts, inquiring with respective payors as to collectability and providing for allowances for estimated contractual adjustments and uncollectible accounts. Significant concentrations of patient accounts receivable are discussed in Note 4.

Patient accounts receivable, where a third-party payor is responsible for paying the amount, are carried at a net amount determined by the original charge for the services provided, less an estimate made for contractual adjustments or discounts provided to third-party payors.

Patient accounts receivable due directly from the patients are carried at the original charge for the services provided less amounts covered by third-party payors and less an estimated allowance for doubtful receivables based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by identifying troubled accounts, by using historical experience applied to an aging of accounts, and by considering a patient's financial and credit history, and current economic conditions. Patient accounts receivable are written off when deemed uncollectible. Recoveries of receivables previously written off are recorded as a reduction of bad-debt expense when received.

Inventories: Inventories, which consist primarily of medical supplies and pharmaceutical drugs, are valued at the lower of cost (first-in, first-out method) or market.

Assets limited as to use: Assets limited as to use include contributor restricted funds, amounts designated by the Board of Directors for replacement or purchases of capital assets, and other specific purposes, and amounts held by trustees under specified agreements. Assets limited as to use consist primarily of deposits on hand with local banking and investment institutions, and bond trustees.

Capital assets: Capital assets consist of property and equipment and are reported on the basis of cost, or in the case of donated items, on the basis of fair value at the date of donation. Routine maintenance and repairs are charged to expense as incurred. Expenditures, which increase values, change capacities, or extend useful lives are capitalized. Depreciation of property and equipment and amortization of property under capital leases are computed by the straight-line method over the estimated useful lives of the assets, which range from 10 to 40 years for buildings and improvements, and 3 to 10 years for equipment. Effective January 1, 2018, the Hospital adopted GASB Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*, as a result no interest costs were capitalized in the current fiscal year.

Capital assets are evaluated for impairment when events or changes in circumstances suggest that there has been a significant unexpected decline in the utility of a capital asset. 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 amount of impairment, if any, is determined by comparing the historical carrying value of the asset to the valuation method that most appropriately reflects the decline in service utility of the capital asset. During the years ended December 31, 2018 and 2017, there were no impairment losses recognized.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

Compensated absences: The Hospital's employees earn paid time off (PTO) benefits at varying rates depending on years of service. Accumulated PTO benefits are paid to an employee upon either termination or retirement, or upon request of an employee at any time. Amounts representing the cost of earned but unused compensated absences are recorded as current liabilities. These liabilities have been computed based on rates of pay in effect at December 31, 2018 and 2017, and were approximately \$1,287,000 and \$974,000, respectively, as of those dates.

Risk management: The Hospital 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 medical malpractice. Commercial insurance coverage is purchased for claims arising from such matters.

Net position: Net position is classified in three categories. The first category is "net investment in capital assets." This category of net position consists of capital assets (both restricted and unrestricted), net of accumulated depreciation and reduced by the outstanding principal balances of any debt borrowings that were attributable to the acquisition, construction, or improvement of those capital assets.

The second category is "restricted" net position. This category consists of externally designated constraints placed on those net assets by creditors (such as through debt covenants), grantors, contributors, law or regulations of other governments or government agencies, or law or constitutional provisions or enabling legislation. The third category is "unrestricted" net position. This category consists of net position that does not meet the definition or criteria of the previous two categories.

Net patient service revenue: Patient service revenue is recorded at the Hospital's established rates when services are provided, with contractual adjustments, provisions for bad debts, and charity care allowances deducted to arrive at net patient service revenue as the net realizable amount.

The Hospital has agreements with third-party payors that provide for reimbursement to the Hospital at amounts different from its established rates. The primary payors are Medicare and Medicaid.

Retroactive adjustments with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity care: The Hospital accepts all patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain established policies of the Hospital. Essentially, these policies define charity services as those services for which no payment is anticipated. Because the Hospital does not pursue collection of amounts determined to qualify as charity care, they are not reported as net patient service revenue. Services provided are recorded as gross patient service revenue and then written off entirely as an adjustment to net patient service revenue.

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy, the estimated cost of those services and supplies, and equivalent service statistics. The cost estimates are based upon the Hospital's cost-to-charge ratio and are on the accrual basis of accounting, thereby including the impact of changes in charity care allowances. Charity care does not include the unreimbursed costs of Medi-Cal. Charges forgone based on established rates during 2018, as well as 2017, and estimated costs and expenses to provide those services were deemed immaterial.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 1. Nature of Business and Significant Accounting Policies (Continued)

District tax revenues: Property taxes are levied by the County on the Hospital's behalf on July 1, and are intended to help finance the Hospital's activities during the year ending the following June 30. The County has established certain dates to levy, lien, mail bills and receive payments from property owners during the year. Amounts levied on behalf of the Hospital are a direct charge of \$150 per parcel. Property taxes are considered delinquent on the day following each payment due date. The Hospital received approximately \$3,391,000 and \$3,397,000 of its financial support from property taxes for the years ended December 31, 2018 and 2017, respectively. These funds are used to support operations and meet required debt service agreements. They are classified as nonoperating revenue as the revenue is not directly linked to patient care and recorded by the Hospital when levied and during the period of their intended use. Management determined that levied amounts not yet received and which are intended for the Hospital's future use should be recorded as deferred inflows, which totaled approximately \$1,585,000 and \$1,497,000 as of December 31, 2018 and 2017, respectively.

Grants and contributions: From time to time, the Hospital receives grants from various governmental agencies and private organizations. The Hospital also receives contributions from foundation and auxiliary organizations, as well as from individuals and other private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or capital acquisitions. These amounts, when recognized upon meeting all requirements, are reported as either nonoperating revenue or capital contributions for acquisition of equipment.

340B program: The Hospital participates in the 340B drug discount program, which enables qualifying health care providers to purchase drugs from pharmaceutical suppliers at a substantial discount. The 340B program is managed by the Health Resources and Services Administration (HRSA) Office of Pharmacy Affairs. The Hospital benefits under this program by purchasing pharmaceuticals at a reduced cost. As one of the conditions for participating in the 340B program, the Hospital is subject to audit. During 2018, HRSA conducted an audit of the Hospital's 340B drug discount program. While the final results of their audit have not been received, the Hospital believes there will not be a material financial impact to the financial statements as a result of the audit.

Operating revenues and expenses: The Hospital's statements of revenues, expenses and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services, which is the Hospital's principal activity. Operating expenses are all expenses incurred to provide health care services, other than financing costs. Nonoperating revenues and expenses are those transactions not considered directly linked to providing health care services.

Subsequent events: The Hospital has evaluated subsequent events through June 27, 2019, the date on which the financial statements were issued.

Reclassifications: Certain items on the statement of net position and statement of revenues, expenses and changes in net position as of and for the year ended December 31, 2017 have been reclassified to be consistent with classifications adopted as of December 31, 2018. The reclassifications had no effect on total net position and the change in net position.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 2. Deposits and Investments

The fair value of deposits and investments at December 31 are as follows:

	2018	2017
Deposits:		
Deposits with financial institutions	\$ 14,713,039	\$ 6,539,577
Cash on hand	1,589	1,481
	<u>14,714,628</u>	<u>6,541,058</u>
Investments:		
Money market mutual fund	515,833	419,085
Corporate stock	103,240	145,565
Other	9,942	-
	<u>629,015</u>	<u>564,650</u>
	<u>\$ 15,343,643</u>	<u>\$ 7,105,708</u>
Reported as follows in the statement of net position:		
Cash and equivalents	\$ 7,356,699	\$ 2,811,902
Assets limited to use, current portion	695,026	812,800
Assets limited to use, noncurrent portion	7,178,736	3,335,441
Investments and other assets	113,182	145,565
Total	<u>\$ 15,343,643</u>	<u>\$ 7,105,708</u>

Custodial credit risk—deposits: At December 31, 2018 and 2017, the Hospital's cash deposits with financial institutions totaled approximately \$15,119,000 and \$7,482,000, respectively. Funds held in deposits are collateralized in accordance with the California Government Code (CGC), except for \$250,000 per account that is federally insured by the Federal Deposit Insurance Corporation. Under the provisions of the CGC, California banks and savings and loan associations are required to secure the Hospital's deposits by pledging government securities as collateral. The market value of pledged securities must equal at least 110 percent of the Hospital's deposits. California law also allows financial institutions to secure Hospital deposits by pledging first trust deed mortgage notes having a value of 150 percent of the Hospital's total deposits. The pledged securities are held by the pledging financial institution's trust department in the name of the Hospital.

Custodial credit risk—investments: For investments, custodial credit risk is the risk that, in the event of failure of the counterparty, the Hospital will not be able to recover the value of the investments or collateral securities that are in the possession of an outside party. Securities held by a third-party are registered in the name of the Hospital.

Interest rate risk: The investment policy does not limit investment maturities as a means of managing its exposure to fair value losses from increasing interest rates. At December 31, 2018 and 2017, the money market mutual fund investments were due in less than one year.

Credit risk: State law limits investments in authorized securities to certain credit risk ratings. The money market mutual fund was rated Aaa-mf by Moody's and AAAM by Standard & Poor's.

Concentration of credit risk: The Hospital places no limit on the amounts that may be invested in any single issuer. At December 31, 2018 and 2017, 100 percent of the money market mutual fund investments were with a single issuer.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 2. Deposits and Investments (Continued)

Fair value: The Hospital uses the fair value hierarchy established by generally accepted accounting principles based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets. Level 2 inputs are significant other observable inputs. Level 3 inputs are significant unobservable inputs. The investment in corporate stock is reported at the last reported sales price on the day of valuation and therefore has been classified as Level 1 within the fair value hierarchy. The investment in the money market mutual fund is not reported at fair value, but rather at net asset value per share (NAV).

Note 3. Net Patient Service Revenue

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

Medicare: Payments for acute care services rendered to Medicare program beneficiaries are paid on cost reimbursement principles. The Hospital was designated as a critical access hospital effective December 1, 2005. The Hospital is paid for services at an interim rate with final settlement determined after submission of annual cost reports and audits thereof by the Medicare fiscal intermediary. As of June 27, 2019, cost reports through December 31, 2016, have been final settled.

Medi-Cal: Payments for inpatient services rendered to Medi-Cal patients are based on the State's diagnosis-related group system (DRG's). Under this methodology, services are paid at prospectively determined rates per discharge according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient skilled nursing care services rendered to Medi-Cal program beneficiaries are reimbursed at prospectively determined per diem rates. Outpatient services rendered to Medi-Cal program beneficiaries are reimbursed based on prospectively determined fee schedules. As of June 27, 2019, cost reports through December 31, 2017 have been audited or otherwise final settled.

Retroactive adjustments made to related estimated third-party settlements for prior years are recorded in net patient service revenue in the year the adjustment is determined. The 2018 and 2017 net patient service revenue increased approximately \$191,000 and \$1,350,000, respectively, as a result of retroactive adjustments related to prior years, excluding the final settlement with a Medi-Cal managed care payor as noted below.

The Hospital receives supplemental Medi-Cal funding from various programs through direct grants and intergovernmental transfers (IGT's). Some of these programs include Assembly Bill 113 (AB 113), Hospital Quality Assurance Fee (HQAF), Rate Range IGT, Public Hospital Redesign and Incentives in Medi-Cal (PRIME), and Assembly Bill 915 (AB 915). In general, the IGT and direct grant programs reimburse the Hospital for a portion of the difference between the cost of treating Medi-Cal patients and the amounts reimbursed through Medi-Cal and Medi-Cal managed care contracts. PRIME is unique in that it is a pay-for-performance Medi-Cal program in which the Hospital is using evidence based quality improvement methods to achieve performance targets and improve health outcomes for patients. All funding for PRIME is contingent on meeting these targets and demonstrating continuous improvement. The Hospital recognizes revenue from the various programs when the certainty of receiving the funds is assured, which is generally when payment is received.

During the years ended December 31, 2018 and 2017, the Hospital recognized the net impact of approximately \$3,755,000 and \$3,454,000, respectively, as a reduction of contractual adjustment expense, which is included in net patient service revenue. An increase of \$1,389,000 from HQAF offset an \$852,000 reduction in PRIME, for not meeting and demonstrating the criteria identified above.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 3. Net Patient Service Revenue (Continued)

In April of 2018, the Hospital received a \$5,287,000 settlement from a Medi-Cal managed care payor, \$4,918,000 of which related to claims with dates of service in 2017 and prior. Included in net patient service revenue is \$369,000 and \$4,918,000 for the years ended December 31, 2018 and 2017.

Other: Payments for services rendered to other than Medicare and Medi-Cal patients are based on established rates or on agreements with certain commercial insurance companies, health maintenance organizations and preferred provider organizations which provide for various discounts from established rates.

Net patient service revenue for the years ended December 31, 2018 and 2017, is comprised of the following:

	2018	2017
Inpatient services	\$ 23,362,874	\$ 26,274,824
Inpatient ancillary services	20,864,610	21,309,889
Outpatient services	68,190,526	62,687,462
Gross patient service revenue	112,418,010	110,272,175
Less contractual adjustments and provision for bad debts	(62,366,083)	(62,471,923)
Net patient service revenue	<u>\$ 50,051,927</u>	<u>\$ 47,800,252</u>

Medicare and Medi-Cal revenue accounted for approximately 72 percent of the Hospital's 2018 and 2017 gross patient service revenue. Laws and regulations governing the Medicare and Medi-Cal programs are extremely complex and subject to interpretation. As a result, there is a possibility that estimates will change by a material amount in the near term.

Note 4. Concentration of Credit Risk

The Hospital grants credit without collateral to its patients and third-party payors. Patient accounts receivable from government agencies represent the only concentrated group of credit risk for the Hospital and management does not believe there is any credit risk associated with these governmental agencies. Contracted and other patient accounts receivable consist of various payors including individuals involved in diverse activities, subject to differing economic conditions and management believes they do not represent any concentrated credit risks to the Hospital. The composition of patient accounts receivable by payor at December 31, 2018 and 2017 was as follows:

	2018	2017
Medicare	\$ 5,715,303	\$ 8,771,120
Medi-Cal	7,672,461	9,519,433
Other third-party payors	6,774,696	6,752,076
Self pay	2,575,724	7,492,914
Gross patient accounts receivable	22,738,184	32,535,543
Less allowances for contractual adjustments and bad debts	(17,037,214)	(27,764,117)
Net patient accounts receivable	<u>\$ 5,700,970</u>	<u>\$ 4,771,426</u>

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 5. Assets Limited as to Use

Assets limited as to use as of December 31, 2018 and 2017, were comprised of the following:

	2018	2017
Under trust agreements	\$ 515,833	\$ 419,085
Designated by the Board	1,562,000	1,540,000
Restricted for specific use	5,757,903	2,161,356
For employee flexible spending plan	38,026	27,800
	<u>7,873,762</u>	<u>4,148,241</u>
Less current portion to match current liabilities	(695,026)	(812,800)
	<u>\$ 7,178,736</u>	<u>\$ 3,335,441</u>

Note 6. Capital Assets

The following summarizes changes in the capital assets of the Hospital for the years ended December 31, 2018 and 2017:

	Balance at December 31, 2017	Additions and Transfers	Transfers/ Retirements/	Balance at December 31, 2018
Capital assets not being depreciated:				
Land and land improvements	\$ 440,000	\$ -	\$ -	\$ 440,000
Construction-in-progress	294,505	4,006,818	(3,620,653)	680,670
Total capital assets not being depreciated	<u>734,505</u>	<u>4,006,818</u>	<u>(3,620,653)</u>	<u>1,120,670</u>
Capital assets being depreciated:				
Buildings and improvements	6,918,227	-	106,105	7,024,332
Equipment	14,022,698	190,118	3,336,743	17,549,559
Total capital assets being depreciated	<u>20,940,925</u>	<u>190,118</u>	<u>3,442,848</u>	<u>24,573,891</u>
Less accumulated depreciation for:				
Buildings and improvements	3,446,515	307,184	(8,858)	3,744,841
Equipment	10,681,474	1,538,039	(154,358)	12,065,155
Total accumulated depreciation	<u>14,127,989</u>	<u>1,845,223</u>	<u>(163,216)</u>	<u>15,809,996</u>
Total capital assets being depreciated, net	6,812,936	(1,655,105)	3,606,064	8,763,895
Capital assets, net	<u>\$ 7,547,441</u>	<u>\$ 2,351,713</u>	<u>\$ (14,589)</u>	<u>\$ 9,884,565</u>

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 6. Capital Assets (Continued)

	Balance at December 31, 2016	Additions and Transfers	Transfers/ Retirements/	Balance at December 31, 2017
Capital assets not being depreciated:				
Land and land improvements	\$ 487,432	\$ -	\$ (47,432)	\$ 440,000
Construction-in-progress	7,241	287,264	-	294,505
Total capital assets not being depreciated	494,673	287,264	(47,432)	734,505
Capital assets being depreciated:				
Buildings and improvements	6,839,169	31,626	47,432	6,918,227
Equipment	13,839,366	183,332	-	14,022,698
Total capital assets being depreciated	20,678,535	214,958	47,432	20,940,925
Less accumulated depreciation for:				
Buildings and improvements	3,145,546	300,969	-	3,446,515
Equipment	9,264,531	1,416,943	-	10,681,474
Total accumulated depreciation	12,410,077	1,717,912	-	14,127,989
Total capital assets being depreciated, net	8,268,458	(1,502,954)	47,432	6,812,936
Capital assets, net	\$ 8,763,131	\$ (1,215,690)	\$ -	\$ 7,547,441

Note 7. Long-Term Debt

As of December 31, 2018 and 2017, debt borrowings were as follows:

	December 31, 2017	Borrowings	Payments	December 31, 2018	Due Within One Year
Capital lease obligation	\$ 489,980	\$ -	\$ (489,980)	\$ -	\$ -
North Sonoma County Healthcare District Certificates of Participation – 2016 Financing Project	4,408,122	7,503,878	(728,000)	11,184,000	746,000
	\$ 4,898,102	\$ 7,503,878	\$ (1,217,980)	\$ 11,184,000	\$ 746,000
	2016	Borrowings	Payments	December 31, 2017	Due Within One Year
Capital lease obligation	\$ 967,493	\$ -	\$ (477,513)	\$ 489,980	\$ 489,980
North Sonoma County Healthcare District Certificates of Participation – 2016 Financing Project	4,936,122	-	(528,000)	4,408,122	728,000
	\$ 5,903,615	\$ -	\$ (1,005,513)	\$ 4,898,102	\$ 1,217,980

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 7. Long-Term Debt (Continued)

Scheduled principal and interest repayments on long-term debt are as follows:

Years ending December 31:	Note Payable		Total Debt Service Requirements
	Principal	Interest	
2019	\$ 746,000	\$ 248,861	\$ 994,861
2020	767,000	265,410	1,032,410
2021	787,000	245,415	1,032,415
2022	807,000	224,903	1,031,903
2023	829,000	203,859	1,032,859
2024-2028	4,345,000	182,258	4,527,258
2029-2031	2,903,000	160,101	3,063,101
	<u>\$ 11,184,000</u>	<u>\$ 1,530,807</u>	<u>\$ 12,714,807</u>

Capital lease: In December 2013, the Hospital entered into a purchase agreement with a third-party (vendor) to acquire an Electronic Health Records (EHR) system including software and equipment. Concurrently, the Hospital executed a "Lease Purchase Agreement" with an unrelated third-party (creditor) to finance the aforementioned EHR system and other equipment. Subsequent to execution of the agreement with creditor, the creditor reduced the amount to be financed from \$2.9 million to \$1.6 million, which represented the estimated cost of the EHR and related software and equipment. By December 31, 2016, all project costs were incurred. The Lease Purchase agreement with the creditor was superseded by the Master Lease Purchase agreement as of December 30, 2014, which includes a bargain purchase option. Based on this agreement, the total capital lease was \$1,781,000, with monthly principal and interest payments of \$41,000 at a rate of 2.58 percent beginning January 30, 2015 through December 30, 2018.

Subsequent to December 31, 2014, the Hospital has decided to abandon certain assets required under the lease described above and to utilize another EHR system. As a result, there is not a related asset for this capital lease recorded on the accompanying statements of net position.

Certificates of participation: On December 29, 2016, the Hospital issued COP, 2016 Financing Program (2016 COP), in the original principal amount of \$12,440,000. The 2016 COP provided funds to: (i) refund its outstanding 2008 COP, executed to finance and refinance the acquisition and improvement of its health facilities; (ii) finance the improvement, renovation, replacement and equipping of the Hospital; and (iii) pay for costs associated with the execution and delivery of the COP.

The COP evidence the direct, undivided fractional interests of the registered owners thereof (the Owners) in lease payments to be made by North Sonoma Hospital District (the District) for the lease of the Hospital pursuant to a lease agreement, dated as of December 1, 2016 by and between the District and Northern California Health Care Authority (the Authority). The District leases the Hospital to the Authority to enable the Authority to lease the Hospital back to the District pursuant to the Lease Agreement. Pursuant to an Assignment Agreement, dated as of December 1, 2016 between the Authority and the Trustee (the Assignment Agreement) the Authority assigned to the Trustee, for the benefit of the Owners, its rights under the Lease Agreement, including: (i) its right to receive Lease Payments; (ii) the District's pledge of its Parcel Tax Revenues to secure payment of Lease Payments; and (iii) its right to enforce amounts payable upon default.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 7. Long-Term Debt (Continued)

As of December 31, 2016, the initial proceeds of \$4,936,000 were transferred to the Hospital. The difference between the net carrying value of the 2008 COP at the refunding date and the re-acquisition price of approximately \$254,000 was recognized as a deferred outflow of resources at that time, which was fully amortized at December 31, 2018.

In June 2018, the Hospital drew down the remaining \$7,504,000, which was placed into an escrow account restricted for future capital purchases. As of December 31, 2018, \$5,483,000 remained in escrow, which is recorded in noncurrent assets limited as to use in the accompanying statements of net position.

Pledge of parcel tax revenues: Given there is a first and prior lien on the Parcel Tax Revenues, parcel tax payments are remitted directly to the Trustee, and the Trustee applies taxes collected to the amount due for Lease Payments, in which the Certificates represent undivided fractional interests. Any tax revenues remaining after the Lease Payments are made is remitted to the District. "Parcel Tax Revenues" are the annual amounts collected by the County on behalf of the District from the Parcel Tax. If Parcel Tax Revenues are insufficient to pay Lease Payments when due, the District promises to pay the Lease Payments from any other available revenues of the District, subject to existing and future liens and encumbrances on its other revenues; provided, however, that there is no assurance that such revenues will be available. Until such time as all of the Lease Payments have been fully paid or prepaid, the District: (a) will not suspend, abate, or discontinue any payments provided for in the Lease Agreement; (b) will perform and observe all other agreements contained in the Lease Agreement; (c) will take appropriate action to oppose any effort to modify the Parcel Tax that would adversely affect the payment of the Certificates; and (d) will not terminate the term of the Lease Agreement for any cause.

Optional redemption: The 2016 COP are subject to redemption in whole or in part on any date on or after September 1, 2026, at the principal amount with respect thereto, together with accrued interest to the date fixed for redemption from the proceeds of optional prepayments made by the Hospital pursuant to the lease agreement. The 2016 COP are subject to optional redemption prior to their stated maturity, once per year on any date, at the option of the Hospital, in part, in inverse order of mandatory sinking fund installment payment date, up to 10 percent of the outstanding principal amount of the COP.

Mandatory sinking fund redemption: The 2016 COP are subject to mandatory redemption on March 1 and September 1 in each year on and after March 1, 2017, in the respective principal amounts set forth in the official statement.

Note 8. Retirement Plans

Effective October 1, 2004, the Hospital adopted a Section 457 retirement plan. Employees can contribute to this plan pursuant to plan documents. The Hospital also provides a defined contribution plan under Section 401(a), which allows the Hospital to match 50 percent of the employee's Section 457 contributions limited to a 3 percent maximum compensation level. All permanent employees who have completed 1,000 hours of service are eligible. Employer contributions to these plans for the years ended December 31, 2018 and 2017 were approximately \$349,000 and \$293,000, respectively, which is included in employee benefits expense.

The Hospital used to provide a 403(b) contributory plan. Effective October 1, 2004, this plan was frozen as the new Section 457/401(a) plan previously mentioned replaced it. There have been no contributions to this plan since it was frozen.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 9. Healthcare Foundation Support

The Healthcare Foundation North Sonoma County (the Foundation), is an independent 501(c)(3) organization that has operated capital campaigns to fund operations, a new emergency room, ICU, MRI, and other capital improvements to the Hospital. In 2017, the Foundation disbursed approximately \$2,273,000 in capital contributions to the Hospital. In 2018, the Foundation disbursed approximately \$220,000 in unrestricted contributions to the Hospital.

Note 10. Commitments and Contingencies

Electronic health record payments: The American Recovery and Reinvestment Act of 2009 included provisions for implementing health information technology under the Health Information Technology for Economic and Clinical Health Act (HITECH). The provisions were designed to increase the use of electronic health record (EHR) technology and establish the requirements for a Medicare and Medicaid incentive payment program for eligible providers that adopt and meaningfully use certified EHR technology.

The Hospital is entitled to receive Medicare and Medicaid incentive payments for the adoption of certified EHR technology, as it has satisfied the statutory and regulatory requirements. The Hospital recognizes income related to Medicare and Medicaid incentive payments using a grant model based upon when it has determined that it is reasonably assured that the Hospital will be meaningfully using EHR technology for the applicable period and the cost report information is reasonably estimable. The Hospital recognized revenue from Medicare and Medicaid incentive payments totaling \$102,000 and none, respectively, for the years ended December 31, 2018 and 2017. The incentive payments are included in other operating revenue in the statement of revenues, expenses and changes in net position. The Hospital's attestation of compliance with the meaningful use criteria is subject to audit by the federal government or its designee. During 2019, the California Department of Healthcare Services (DHCS) conducted an audit of the Hospital's Medicaid EHR. While the final results of their audit have not been received, the Hospital believes there will not be a material financial impact to the financial statements as a result of the audit.

Operating leases: The Hospital leases various equipment and facilities under operating leases expiring at various dates. Total building and equipment rent expense for the years ended December 31, 2018 and 2017, were approximately \$1,218,000 and \$1,163,000, respectively, and included in building and equipment rent expense. Future minimum lease payments for future years under operating leases that have initial or remaining lease terms in excess of one year as of December 31, 2018, are as follows:

Years ending December 31:	
2019	\$ 942,298
2020	700,921
2021	649,810
2022	607,643
2023	269,410
Thereafter	1,794,934
	<u>\$ 4,965,016</u>

Litigation: The Hospital may from time-to-time be involved in litigation and regulatory investigations, which arise in the normal course of doing business. After consultation with legal counsel, management estimates that matters existing as of December 31, 2018, will be resolved without material adverse effect on the Hospital's future financial position, results from operations or cash flows.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 10. Commitments and Contingencies (Continued)

Capital commitments: At December 31, 2018, the Hospital had contractual obligations of approximately \$3,600,000 related to various projects being funded by the 2016 COP.

Regulatory and compliance matters—general regulatory compliance: The health care industry is subject to voluminous and complex laws and regulations of federal, state and local governments. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement laws and regulations, anti-kickback and anti-referral laws and false claims prohibitions, and in the case of tax-exempt hospitals, the requirements of tax exemption. In recent years, government activity has increased with respect to eligibility for critical access hospital designation, investigations and allegations concerning possible violations of reimbursement, false claims, anti-kickback, and anti-referral statutes and regulations by health care providers. The Hospital believes it is generally in compliance with applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. The Hospital records a liability when it becomes aware that it has billed amounts or entered into transactions or relationships that may violate these governmental laws or regulations.

Medical malpractice insurance: The Hospital maintains commercial malpractice liability insurance coverage under a claims-made policy covering losses up to \$5 million per claim and up to \$15 million in the aggregate, with a per claim deductible of \$10,000. The Hospital plans to maintain the insurance coverage by renewing its current policy, or by replacing it with equivalent insurance. Based upon the Hospital's claims experience, management has determined that the potential liability for such claims is not material to the financial statements.

Workers' compensation program: The Hospital maintains workers' compensation self-insurance coverage under a claims-made policy covering losses on a per-occurrence basis in excess of \$350,000 with an aggregate limit of \$1,000,000. Outstanding claims and incurred but not reported claims (IBNR) are evaluated through a combination of case-by-case reviews and application of historical experience. The amount recorded for outstanding and IBNR claims are estimated by an independent actuary.

The change in the workers' compensation claims liabilities, which are included in the amount of \$254,000 within accounts payable and other accrued expenses and \$905,000 within estimated workers' compensation liability, net of current portion on the statements of net position, is approximately as follows:

	2018	2017
Claims payable, beginning of year	\$ 1,072,000	\$ 219,000
Incurred claims	239,000	1,009,000
Claim payments	(152,000)	(156,000)
Claims payable, end of year	<u>\$ 1,159,000</u>	<u>\$ 1,072,000</u>

Health self-insurance: The health care plan for the Hospital's employees is administered by a third-party administrator. The Organization acts as a self-insurer for employee health care claims with excess coverage for claims exceeding \$100,000 per covered person with an aggregate minimum stop loss of \$2,986,000, which may be adjusted upward by the carrier dependent upon certain factors, for the policy year ended December 31, 2018. For the year ended December 31, 2018, the carrier adjusted the aggregate stop loss to \$3,451,000. Administrative expenses and claims for the health care plan included in expense were approximately \$3,598,000 and \$2,944,000 for the years ended December 31, 2018 and 2017, respectively.

**North Sonoma County Healthcare District
d/b/a Healdsburg District Hospital**

Notes to Financial Statements

Note 10. Commitments and Contingencies (Continued)

Liabilities are reported when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNR). Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. Included within Claims Payable are estimated reinsurance receivables of \$250,000, and none, for the years ended December 31, 2018 and 2017, respectively.

The change in the balance of self-insured health claims liabilities, which are included in accounts payable and other accrued expenses on the statements of net position, is approximately as follows:

	2018	2017
Claims payable, beginning of year	\$ 455,000	\$ 291,000
Incurred claims	3,455,000	2,730,000
Claim payments	(3,530,000)	(2,566,000)
Claims payable, end of year	<u>\$ 380,000</u>	<u>\$ 455,000</u>

Health care reform: As a result of enacted federal health care reform legislation, substantial changes are anticipated in the United States health care system. Such legislation includes numerous provisions affecting the delivery of health care services, the financing of health care costs, reimbursement of health care providers and the legal obligations of health insurers, providers and employers. These provisions are currently slated to take effect at specified times over approximately the next decade.

Seismic retro-fit: The State of California issued seismic safety regulations in 1994, which have been amended on several occasions since then. The regulations call for stringent structural building standards. The Hospital is required to comply with earthquake retrofit requirements and has until 2030 to be compliant with such regulations. Management is evaluating its facilities and is considering all options.

Note 11. Recent Accounting Standards Not Yet Adopted

GASB Statement No. 83, *Certain Asset Retirement Obligations*, issued December 2016, will be effective for the Hospital beginning with its fiscal year ending December 31, 2019. Under Statement No. 83, a government that has legal obligations to perform future asset retirement activities related to its tangible capital assets is required to recognize a liability and a corresponding deferred outflow of resources. The Statement identifies the circumstances that trigger the recognition of these transactions. The Statement also requires the measurement of an asset retirement obligation to be based on the best estimate of the current value of outlays expected to be incurred while the deferred outflow of resources associated with the asset retirement obligation will be measured at the amount of the corresponding liability upon initial measurement and generally recognized as an expense during the reporting periods that the asset provides service. The Statement requires disclosures including a general description of the asset retirement obligation and associated tangible capital assets; the source of the obligation to retire the assets; the methods and assumptions used to measure the liability; and other relevant information.

**North Sonoma County Healthcare District
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Notes to Financial Statements

Note 11. Recent Accounting Standards Not Yet Adopted (Continued)

GASB Statement No. 87, *Leases*, issued June 2017, will be effective for the Hospital beginning with its fiscal year ending December 31, 2020, with earlier adoption encouraged. Statement No. 87 establishes a single approach to accounting for and reporting leases by state and local governments. Under this statement, a government entity that is a lessee must recognize (1) a lease liability and (2) an intangible asset representing the lessee's right to use the leased asset. In addition, the Hospital must report the (1) amortization expense for using the lease asset over the shorter of the term of the lease or the useful life of the underlying asset, (2) interest expense on the lease liability and (3) note disclosures about the lease. The Statement provides exceptions from the single-approach for short-term leases, financial purchases, leases of assets that are investments, and certain regulated leases. This statement also addresses accounting for lease terminations and modifications, sale-leaseback transactions, non-lease components embedded in lease contracts (such as service agreements), and leases with related parties.

GASB Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placement*, issued March 2018, will be effective for the Hospital beginning with its fiscal year ending December 31, 2019, with earlier adoption encouraged. Statement No. 88 clarifies which liabilities governments should include in their note disclosures related to debt. This Statement defines debt that must be disclosed in the notes to financial statements as a liability that arises from a contractual obligation to pay cash in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. Governments must also disclose amounts of unused lines of credit, assets pledged as collateral for debt and the terms specified in debt agreements related to significant events of default with finance-related consequences, termination events with finance-related consequences, and subjective acceleration clauses. Within the notes, governments should separate information regarding direct borrowings and direct placements of debt from other debt.

