Financial Statements
June 30, 2016 and 2015

Tulare Regional Medical Center

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Independent Auditor's Report

The Board of Directors
Tulare Local Health Care District
dba Tulare Regional Medical Center
Tulare, California

Report on the Financial Statements
We have audited the accompanying statement of net position of Tulare Local Health Care District dba Tulare Regional Medical Center (the District) as of June 30, 2016, and the related statement of revenues, expenses, and changes in net positon and statement of cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the District's basic 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 opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. Because of the matter described in the "Basis for Disclaimer of Opinion" paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide for an audit opinion on the discretely presented component unit.

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 District'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 District'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.

Except for the matter described in the Basis for Disclaimer of Opinion paragraph, we believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Basis for Disclaimer of Opinion on the Discretely Presented Component Unit
The financial statements of the Tulare Hospital Foundation (the Foundation) have not been audited as of June 30, 2016, and we were not engaged to audit the Foundation's financial statements as part of our audit of the District's basic financial statements. The Foundation's financial activities are included in the District's basic financial statements as a discretely presented component unit and represent 100% of the assets, net position, and revenues, respectively, of the District's aggregately presented component units.

Disclaimer of Opinion on the Discretely Presented Component Unit
Because of the significance of the matter described in the "Basis for Disclaimer of Opinion on the Discretely Presented Component Unit" paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of the discretely presented component unit of the District. Accordingly, we do not express an opinion on these financial statements.

Unmodified Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the District as of June 30, 2016, and the respective changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Matter

My Correction of CPA Firm's Correction: Note 12, not Note 13. See PDF Page 35 of 46

Correction of an Error
As discussed in Note 13 to the financial statements, certain errors resulting in overstatement of capital assets, bond issuance costs, long-term debt, and reduction of deferred and related party payables, resulting in understated net position as of June 30, 2015, were discovered during the current year. Accordingly, the amount presented for beginning net position has been restated in the 2016 financial statements to correct the errors. As part of our audit of the 2016 financial statements, we also audited the corrections discussed in Note 13. Our opinion is not modified with respect to that matter.

Uncertainties
As discussed in Note 12 to the financial statements, the District has exhausted the existing bond funds, and may not be able to secure the required financing to complete the tower project. The District's plans in regard to this matter are described in Note 5. Our opinion is not modified with respect to that matter.

Other Matter

Required Supplementary Information
Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4-12 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.

Other Information
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's basic financial statements. The Charity Care and Community Support Schedule is presented for purposes of additional analysis and is not a required part of the financial statements.

The Charity Care and Community Support Schedule has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*
In accordance with *Government Auditing Standards*, we have also issued a report dated April 25, 2017, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Eide Bailly LLP

Boise, Idaho
April 25, 2017

Tulare Local Health Care District's (the "District") discussion and analysis is designed to assist the reader in focusing on significant financial issues, provide an overview of the District's financial activity, identify changes in the District's financial position, and identify any material deviations from the financial plan (the approved budget). Unless otherwise noted, all discussion and analysis pertains to the District's financial condition, results of operations and cash flows as of and for the year ended June 30, 2016. Please read it in conjunction with the financial statements in this report.

FINANCIAL HIGHLIGHTS

- The District's net position increased by $16.2 million, or 21.3%, primarily attributable to the year's net income (income before contributions). Total assets increased by $12.9 million, or 6.2%. Cash and investments decreased by $6.7 million, or 37%, resulting from outlays for capital expansion. Capital assets increased $2.5 million to $159.9 million with $2.5 million in net additions to buildings, equipment, and construction in progress, and a net increase in accumulated depreciation.

- For the year, the District's total operating revenues increased to $80.2 million, a 2.0% increase from the prior year, while total operating expenses increased to $77.7 million, an increase of 9.1%. The current year increase in total operating revenues was attributable to an increase in other operating revenues and increases in supplemental funding.

- During the fiscal year, the District made the following significant capital expenditures:

  ✓ General construction and equipment for the new tower expansion
  ✓ Continued investment in the Cerner CommunityWorks system
  ✓ Evolutions fitness center upgrades, including saunas and new flooring
  ✓ Women's Pavilion health center
  ✓ CMS mandated facility upgrades throughout patient care areas

The source of funding for these projects was derived from operations, capital contributions, lease project funds, funds reserved for capital acquisition, and benevolent contributions.

REQUIRED FINANCIAL STATEMENTS

The financial statements of the District include: (a) a balance sheet, (b) a statement of revenues, expenses, and changes in net position, and (c) a statement of cash flows. The balance sheet includes information about the nature of the District's assets and liabilities and classifies them as current or non-current. It also provides the basis for evaluation of the capital structure of the District and for assessing the liquidity and financial flexibility of the District. The District's revenues and expenses are accounted for in the statement of revenues, expenses, and changes in net position. This statement measures the District's operations and can be used to determine whether the District has been able to recover all of its operating costs from patient services and other operating revenue sources. The primary purpose of the statement of cash flows is to provide information about the District's cash from operating, non-capital financing, capital and related financing, and investing activities. It provides answers to such questions as what were the District's sources of cash, what was cash used for, and what was the change in cash balances during the reporting period.

A summary of the District's balance sheets (in thousands) is presented in Table 1 below:

	June 30, 2016	June 30, 2015	$ change	% change
Current and other assets	60,544	50,106	10,438	20.8%
Capital assets	159,919	157,408	2,511	1.6%
Total assets	220,463	207,514	12,949	6.2%
Current and other liabilities	27,715	26,418	1,297	4.9%
Long-term debt outstanding	100,381	105,078	(4,697)	-4.5%
Total liabilities	128,096	131,496	(3,400)	-2.6%
Invested in capital assets - net of debt svc	59,539	38,956	20,583	52.8%
Restricted	11,543	19,724	(8,181)	-41.5%
Unrestricted	21,285	17,471	3,814	21.8%
Total net position	92,367	76,151	16,216	21.3%
Total liabilities and net position	220,463	207,647	12,816	6.2%

As reflected in Table 1, net position increased $16.2 million to $92.4 million for the year ended June 30, 2016, primarily attributable to the District's $2.4 million income from operations and $7.2 million income from property taxes.

TABLE 2
Financial Analysis of the District (continued)

Condensed Statements of Revenues, Expenses, and Changes in Net position
(In Thousands)

The following table presents a summary of the District's revenues, expenses, and changes in net position:

	June 30, 2016	June 30, 2015	$ Change	% Change
Net patient services revenue	$ 76,277	$ 76,502	$ (225)	-0.3%
Other operating revenue	3,959	2,185	1,774	81.2%
Total operating revenue	80,236	78,687	1,549	2.0%
Salaries & benefits	-	12,438	(12,438)	-100.0%
Medical and other supplies	9,233	9,485	(252)	-2.7%
Pro. Fees and purchased services	58,948	38,901	20,047	51.5%
Depreciation and amortization	3,607	4,128	(521)	-12.6%
Other	5,949	6,291	(342)	-5.4%
Total operating expense	77,737	71,243	6,494	9.1%
Operating income	2,499	7,444	(4,945)	-66.4%
Non-operating revenues & expenses	7,219	9,048	(1,829)	-20.2%
Revenue in excess of expenses	9,718	16,492	(6,774)	-41.1%
Change in net position	9,718	16,492	(6,774)	-41.1%
Net position - beginning of year	76,151	59,659	16,492	27.6%
Prior year restatement	6,497			100.0%
Net position - end of year	$ 92,366	$ 76,151	$ 9,718	12.8%

SOURCES OF REVENUE

Operating revenues – For fiscal year 2016, the District derived 91.2% of its total revenues from operations. Operating revenues include, among other items, patient care revenue from Medicare, Medi-Cal, and other federal, state, and local government programs, and commercial insurance payers and patients; cafeteria sales; membership sales and dues from a District-owned health and fitness center; and rental revenue from medical office buildings leased by the District.

Non-operating revenues – For fiscal year 2016, the District derived 8.8% of its total revenues from investment income and property tax revenue including that associated with the 2005 general obligation bonds as well as an allocation of general property taxes assessed by the County of Tulare on properties residing within the District's geographical boundaries.

OPERATING AND FINANCIAL PERFORMANCE

The following summarizes the District's statements of revenues, expenses, and changes in net position between 2016 and 2015: (Refer to Table 2)

Acute admissions decreased by 370, or 9.9%, to 3,366, while acute patient days increased by 148, or 1%, to 14,825. Outpatient visits (ER visits, home health visits, outpatient surgeries, referred visits for diagnostic services and clinic visits) were 6,512, or 6.2%, below 2015 levels. ER visits were down 2,769, or 7.8%.

Net patient services revenue decreased $225,000, or 0.3%, in 2016. The small decrease in net patient services revenue can be attributed to lower service volumes mostly offset by improvements in supplemental funding. The District recognized $15.7 million of supplemental state funding for Medi-Cal in 2016.

Net patient services revenue per adjusted patient day (the amount of patient services revenue actually collected per equivalent patient encounter) decreased from $2,215 to $2,156, or 2.7%, from 2015 to 2016, primarily due to the factors stated above such as an 11% increase in the average length of stay, which was caused by fewer OB admissions.

Other operating revenue consists primarily of cafeteria sales, health and fitness center membership sales and dues, and rental revenue from medical office buildings leased by the District. Other operating revenue increased by $1.8 million, or 81.2%. This significant increase came as a result of the prior year experiencing a one-time repayment to the federal government of $1.1 million in meaningful use funding.

Salaries and benefits expense decreased $12.4 million, or 100%. As of November 2014 there were no longer any district employees and the workforce was thereafter supplied by HCCA. The prior year reported a little more than 7 months of salaries and benefits. The labor cost became a purchased service and will be covered below under that line item.

Medical and other supplies decreased $252,000, or 2.7%, from the prior year. This decrease can be accounted for in decreased patient volumes.

OPERATING AND FINANCIAL PERFORMANCE (CONTINUED)

Professional fees and purchased services increased $20 million, or 51.5%, primarily due to the outsourcing of all labor to the management company, HCCA, which accounted for $12.3 million of the increase.

Depreciation and amortization expense decreased $521,000, or 12.6%. Most capital acquisitions remained in active Construction in Progress accounts.

Other expenses decreased by $342,000, or 5.4%.

Total operating expenses increased by $6.5 million, or 9.1%, accounted for in increases to purchased services and purchased labor.

Non-operating revenues of $7.8 million for the current fiscal year are comprised of $7.2 million of tax revenue received from the County of Tulare, $340,000 in grants & contributions, $243,000 in investment income on cash and investments, and $6,000 in minor items. Investment income represents interest income and realized and unrealized gains and losses on District investments. District investments by law may only be invested in high-grade, governmental and commercial fixed income securities, and money market funds. Investment income for 2016 increased by $131,000 from the prior year.

Non-operating expenses represent interest expense paid during the fiscal year on the District's short- and long-term debt consisting of revenue bonds and capital leases. Total interest expense of $771,000 decreased by $27,000, or 3.4%, from the prior year.

BUDGET RESULTS

The Board of Directors approves the annual operating budget of the District. The budget remains in effect the entire year but is updated as needed for internal management use to reflect changes in activity and approved variances. A fiscal year 2016 budget comparison and analysis is presented below.

TABLE 3
Actual income and expenses vs. Budget
(In Thousands)

	Actual	Budget	$ Change	% Change
Net patient services revenue	$ 76,277	$ 79,851	$ (3,574)	-4.5%
Other operating revenue	3,959	3,016	943	31.3%
Total operating revenue	80,236	82,867	(2,631)	-3.2%
Salaries & benefits	-	29	(29)	-100.0%
Medical and other supplies	9,233	10,481	(1,248)	-11.9%
Pro. Fees and purchased services	58,948	59,351	(403)	-0.7%
Depreciation and amortization	3,607	4,050	(443)	-10.9%
Other	5,949	1,905	4,044	212.3%
Total operating expense	77,737	75,816	1,921	2.5%
Operating income	2,499	7,051	(4,552)	-64.6%
Non-operating revenues & expenses	7,219	7,634	(415)	-5.4%
Revenue in excess of expenses	9,718	14,685	(4,967)	-33.8%
Change in net position	$ 9,718	$ 14,685	$ (4,967)	-33.8%

In comparing actual versus budgeted results, the following is noted:

The District completed its fiscal year $5 million, or 33.8%, below budgeted income.

The District's operating income was less than budget expectations by $4.5 million, or 64.6%. Net patient services revenue was below budget by $3.6 million, or 4.5%, due to decreases in admissions and outpatient visits. Other operating revenue exceeded budget by $943,000, or 31.3%. The District reacquired eligibility for meaningful use funding.

The District overran the operating expense budget by $2 million, or 2.5%. This variance was primarily due to aggressive budget savings in areas such as utilities and travel not being achieved.

CAPITAL ASSETS

At June 30, 2016, the District had $160 million invested in a variety of capital assets, as reflected in the following schedule (in thousands), which represents a net increase (additions less retirements and depreciation) of $2.5 million from the prior year.

TABLE 4
Comparison of capital assets year over year

	June 30, 2016	June 30, 2015	Dollar change	% change
Land and improvements	3,302	3,302	-	0.0%
Buildings and improvements	44,849	43,403	1,446	3.3%
Leasehold improvements	607	29	578	1993.1%
Equipment	35,894	33,587	2,307	6.9%
Construction in progress	138,189	136,423	1,766	1.3%
Gross capital assets	222,841	216,744	6,097	2.8%
Less accumulated depreciation	(62,922)	(59,336)	(3,586)	6.0%
Net capital assets	159,919	157,408	2,511	1.6%

Current year activity was predominantly focused upon the new tower expansion. General obligation bond funds were exhausted in September 2014. Additional expenditures have been funded with operating cash.

Capital expenditures for purposes other than the tower expansion were held to urgent and critical needs. This consisted of the Cerner Community Works system, CMS-mandated upgrades to the aging facility, as well as the Women's Pavilion and improvements to the fitness & rehab center.

LONG-TERM DEBT

At June 30, 2016, the District had approximately $100.4 million in capital lease obligations and revenue and general obligation bonds outstanding.

Principal balance in thousands

Revenue bond issuance of 2007	$14,200
GO bond series A issuance	$14,845
GO bond series B issuance	$69,680
Bank of America capital equipment lease	$ 626
IBM Financing capital equipment lease	$1,029

The revenue bonds are secured by the assets of the District, and are subject to maintaining minimum liquidity and minimum debt service coverage. The District complied with these requirements in fiscal year 2016.

In August 2016, Fitch Ratings affirmed the District's $14.2 million revenue bonds' rating of 'BB-'. Fitch also added a Ratings Watch Positive designation, and made the following statement: "TRMC has sustained the trend of strong operating performance since Fitch's last rating review in August 2015. Ongoing work by the management team in place since January 2014 has brought a financial turnaround, and double digit operating EBITDA margins are expected to continue. Operating EBITDA was 14.1% in fiscal 2016 and 16.6% in fiscal 2015 compared to 4.4% in fiscal 2014."

The general obligation bonds represent the general obligation of the District's property tax base. The District has the power and is obligated to cause annual ad valorem taxes to be levied upon all property within the District, subject to taxation by the District, and collected by the County of Tulare for payment, when due, of the principal and interest on the bonds. In September 2015, Moody's Investors Services affirmed the District's $85 million general obligation bond rating at Baa3. According to Moody's, "The affirmation also reflects the district's effective new management team that has made notable improvements to the hospital's financial operations. The rating also incorporates the district's large and growing tax base and below average residential wealth levels."

The Bank of America equipment lease was entered into in 2012 and is payable over 48 months. The purpose of the lease was to purchase a surgical robot, and a variety of pieces of movable equipment for the Tower 1 expansion.

In May 2014, the District entered into a $598,000 master lease agreement for the purpose of acquiring the IBM Pureflex server system. The lease is payable over 48 months at an interest rate of 2.94%. More recently three additional IBM-financed borrowings have been added: $607,180 over 36 months at 4.393%, $64,488 over 36 months at 5.143%, and $291,674 over 36 months at 5.060%. These last three are all related to the electronic medical record (EMR) project mandated by the federal government.

ECONOMIC OUTLOOK

In January 2014 the District's Board brought in a new management company, Healthcare Conglomerate Associates (HCCA). Since then, HCCA has steadily led the District in improving the finances and operations. HCCA strategically brought in key seasoned leadership, with specific expertise in hospital turnarounds, in different phases to guide the District through an extensive financial turnaround, which is on-going. This strategy has proved enormously successful as the District's operating results have significantly improved since January 2014.

Over the last year, the District, under HCCA's leadership, has seen a sustained upgraded bond rating from Fitch Ratings and an affirmation of the rating from Moody's.

The 2017 budget as approved by the District Board shows a continued improvement both in operating income and cash. That budget indicates an 11% operating margin and 100 Days Cash on Hand at the end of 2017.

A public vote to complete the financing for the new patient tower was conducted in August 2016, with the ballot measure failing to pass. However, the full plan to complete the tower continues unabated. HCCA has studied, and continues to explore, strategic alternate funding sources, including government-based opportunities. HCCA has begun active discussion with these organizations, and expects a fully developed proposal in the near future.

The economic future of the District can also expect to be bolstered by HCCA's continuing operational and managerial expertise, as well as its plans to expand patient access through strategically adding medical office locations in appropriate areas of the Central Valley over the next several years. In addition, management's investment in critically needed services such as the new interventional Cardiac Cath Lab, along with a new hospital tower will further substantially improve volumes from the District's catchment area and beyond. This replacement for the 65 year old building which the District currently occupies will facilitate HCCA's strategic plans to provide trauma services with enhanced reimbursement and higher volumes. Cohesive community support is critical to achieving the strategic plans of the healthcare district, and ultimately improving the health status of its residents.

Assets	
Current Assets	
Cash and cash equivalents	$ 11,404,419
Assets limited as to use available for current debt service	6,044,283
Receivables	
Patient, net of estimated uncollectibles of $3,160,000	11,094,457
Estimated third-party payor settlements	15,366,476
Property taxes	5,838,774
Other	2,450,830
Supplies	1,206,592
Prepaid expenses and other	789,846
Total current assets	54,195,677
Noncurrent Cash	
Restricted by trustee for debt reserve	5,498,311
Capital Assets	
Capital assets not being depreciated	140,414,057
Capital assets being depreciated, net	19,505,206
Total capital assets	159,919,263
Other Assets	
Notes receivable	264,478
Total assets	219,877,729
Deferred Outflows of Resources	
Refunding costs	585,183
Total assets and deferred outflows of reources	$ 220,462,912

Liabilities, Deferred Inflows of Resources, and Net Position	
Current Liabilities	
Current maturities of long-term debt	$ 2,082,684
Accounts payable	
Trade	12,006,636
Construction	1,013,840
Related parties	3,405,970
Estimated third-party payor settlements	150,000
Accrued expenses	
Interest	2,652,695
Other	2,756,903
Total current liabilities	24,068,728
Long-Term Debt, Less Current Maturities	98,297,753
Total liabilties	122,366,481
Deferred Inflows of Resources	
Property taxes	5,729,564
Net Position	
Net investment in capital assets	59,538,826
Restricted	
Expendable for debt service	11,542,594
Unrestricted	21,285,447
Total net position	92,366,867
Total liabilities, deferred inflows of resources, and net position	$ 220,462,912

Operating Revenues	
Net patient service revenue (net of provision for bad debts of $7,543,000)	$ 76,277,173
Other revenue	3,959,083
Total operating revenues	80,236,256
Operating Expenses	
Leased employee expense	36,826,628
Professional fees and purchased services	22,121,738
Supplies	9,233,247
Insurance	814,735
Depreciation and amortization	3,607,430
Other	5,133,294
Total operating expenses	77,737,072
Operating Income	2,499,184
Nonoperating Revenues (Expenses)	
Investment income	243,111
Debt issuance costs	(97,402)
Property tax income	7,186,334
Interest expense	(888,470)
Noncapital contributions and grants	339,544
Gain on disposal of capital assets	1,700
Other	4,239
Net nonoperating revenues	6,789,056
Revenues in Excess of Expenses Before Capital Contributions and Grants	9,288,240
Capital Contributions and Grants	430,268
Change in Net Position	9,718,508
Net Position, Beginning of Year, as Previously Reported	76,151,047
Restatement - Note 13	6,497,312
Net Position, Beginning of Year, as Restated	82,648,359
Net Position, End of Year	$ 92,366,867

Operating Activities	
Receipts from and on behalf of patients	$ 64,926,349
Payments to suppliers and contractors	(72,198,489)
Other receipts and payments, net	2,673,941
Net Cash used for Operating Activities	(4,598,199)
Noncapital Financing Activities	
Noncapital contributions and grants	339,544
Increase in notes receivable	(257,728)
Property taxes received	7,077,124
Other	4,239
Net Cash from Noncapital Financing Activities	7,163,179
Capital and Capital Related Financing Activities	
Principal payments on long-term debt	(2,403,577)
Interest paid	(780,267)
Debt issuance costs	(97,402)
Purchase of capital assets	(12,938,791)
Proceeds from sale of capital assets	4,737,658
Capital contributions and grants	430,268
Net Cash used for Capital and Capital Related Financing Activities	(11,052,111)
Investing Activites	
Investment income	243,111
Net Change in Cash	(8,244,020)
Cash and Cash Equivalents, Beginning of Year	31,191,033
Cash and Cash Equivalents, End of Year	$ 22,947,013

Reconciliation of Cash and Cash Equivalents to the Statement of Net Position	
Cash in current assets	$ 17,448,702
Cash in noncurrent cash	5,498,311
Total cash	$ 22,947,013
Reconciliation of Operating Income to Net Cash used for Operating Activities	
Operating income	$ 2,499,184
Adjustments to reconcile operating income to net cash used for operating activities	
Depreciation	3,607,428
Provision for bad debts	7,543,039
Changes in assets and liabilities	
Patient receivables	(8,075,940)
Other receivables	(1,285,142)
Estimated third-party payor settlements	(10,772,644)
Supplies	(123,275)
Prepaid expenses	(209,332)
Accounts payable	1,490,346
Estimated third-party payor settlements	(45,277)
Accrued expenses	773,414
Net Cash used for Operating Activities	$ (4,598,199)
Supplemental Disclosure of Noncash Capital and Capital Related Financing Activities	
Increase in accounts payable for construction and equipment	$ 210,476
Equipment financed through capital lease arrangement	$ 963,342

	(Unaudited)
Assets	
Cash and cash equivalents	$ 295,462
Contributions receivable, net	178,301
Accounts receivable	37,897
Long-term investments	574,650
Total assets	$ 1,086,310
Net Assets	
Unrestricted	$ 792,131
Temporarily restricted	260,551
Permanently restricted	33,628
Total net assets	1,086,310
Total liabilities and net assets	$ 1,086,310

		(Unaudited)
Unrestricted Net Assets		
Support and revenue		
Contributions	$	3,463
Special events		147,802
Investment income		38,645
Total support and revenue		189,910
Expenses		
Contributions		89,340
General services and administrative		73,830
Total expenses		163,170
Increase in Unrestricted Net Assets		26,740
Change in Net Assets		26,740
Net Assets, Beginning of Year		1,059,570
Net Assets, End of Year	$	1,086,310

Note 1 - Reporting Entity and Summary of Significant Accounting Policies

The financial statements of the Tulare Local Health Care District (dba Tulare Regional Medical Center, e.g. the District) have been prepared in accordance with generally accepted accounting principles in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting and reporting policies and practices used by the District are described below.

Reporting Entity

The District 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 District is a political subdivision of the State of California and has been recognized by the Internal Revenue Service as exempt from federal income taxes under Internal Revenue Code Section 501(a). The District is governed by a five- member Board of Directors, elected from within the District's geographical political divisions to specified terms of office. The District is located in Tulare, California and operates a 112-bed general acute care hospital facility, a home health agency, several rural health care clinics and other patient service programs. The District provides health care services primarily to individuals who reside in the local geographic area.

In January 2014 the District retained the services of Health Care Conglomerates Associates (HCCA) to manage and operate the healthcare services of the District. The agreement with HCCA requires that HCCA recruit and provide senior leadership. That agreement was replaced in May 2014 by a new long-term agreement with HCCA. The new 15-year agreement specifically named HCCA to manage the operations of the District. On November 9, 2014, all District employees transitioned to HCCA employment. The District now leases the employees from HCCA. Transitioning to a private employer has provided an enhanced level of professionalism, efficiency, and overall improved labor productivity for the workforce serving the District.

For financial reporting purposes, the District has included all funds, organizations, agencies, boards, commissions, and authorities. The District has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the District are such that the exclusion would cause the District’s financial situation to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization’s governing body and (1) the ability of the District to impose its will on that organization or (2) the potential for the organization to provide specific benefits or impose specific financial burdens on the District.

Discretely Presented Component Unit

Tulare Hospital Foundation (the Foundation) was established to procure and extend financial aid toward the operation, maintenance, and modernization of facilities of the District. Funds raised are distributed to the Tulare, California community primarily through the purchases of property and equipment, supplies, and support. The Foundation has been determined to be and is presented as a discretely presented component unit in the District’s financial statements. Financial statements of the Foundation can be obtained by contacting the Foundation’s President.

Measurement Focus and Basis of Accounting

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Revenues are recognized when earned, and expenses are recorded when the liability is incurred.

Basis of Presentation

The statement of net position displays the District's assets, liabilities, and deferred inflows, with the difference reported as net position. Net position is reported in the following categories/components:

> *Net investment in capital assets* consists of net capital reduced by the outstanding balances of any related debt obligations and deferred inflows of resources attributable to the acquisition, construction or improvement of those assets or the related debt obligations and increased by balances of deferred outflows of resources related to those assets or debt obligations.
>
> *Restricted net position*:
>
> Expendable – Expendable net position results when constraints placed on net position use are either externally imposed or imposed through enabling legislation.
>
> Nonexpendable – Nonexpendable net position is subject to externally imposed stipulations which require them to be maintained permanently by the District.
>
> *Unrestricted net position* - Consists of net position not meeting the definition of the preceding categories. Unrestricted net position often has constraints on resources imposed by management which can be removed or modified.

When an expense is incurred that can be paid using either restricted or unrestricted resources (net position), the District's policy is to first apply the expense toward the most restrictive resources and then toward unrestricted resources.

Use of 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. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash

Cash and cash equivalents include highly liquid investments with an original maturity of three months or less, excluding internally designated or restricted cash and investments. For purposes of the statement of cash flows, the District considers all cash and investments with an original maturity of three months or less as cash and cash equivalents.

Assets Limited to Use Available for Current Debt Service

Assets limited to use available for current debt service, consists of cash restricted for debt service designated for the accrued interest related to the General Obligation Revenue bonds. Future debt service payments for the bonds are assessed periodically and deposited into this fund. The funds are included with the cash deposited in a financial institution.

Patient Receivables

Patient receivables are uncollateralized customer and third-party payer obligations. Payments of patient receivables are allocated to the specific claims identified on the remittance advice or, if unspecified, are applied to the earliest unpaid claim.

The carrying amount of patient receivables is reduced by a valuation allowance that reflects management's estimate of amounts that will not be collected from patients and third-party payors. Management reviews patient receivables by payor class and applies percentages to determine estimated amounts the will not be collected from third parties under contractual agreements and amounts that will not be collected from patients due to bad debts. Management considers historical write off and recovery information in determining the estimated bad debt provision.

Property Tax Receivable

Property tax receivable is recognized on the lien date, which is January 1 of the tax year in Tulare County. The property tax receivable represents taxes certified by the Board of Directors to be collected in the next fiscal year. However, by statute, the tax asking becomes effective on the first day of the following year. Although the property tax receivable has been recorded, the related revenue is considered a deferred inflow of resources – unavailable revenue and will not be recognized as revenue until the year in which it is levied.

Lien date	January 1
Lien date (unsecured)	June 30
Levy date	January 1, succeeding year
Due dates (secured)	November 1 and February 1
Due dates (unsecured)	August 31

Supplies

Supplies are stated at lower of cost (first-in, first-out) or market and are expensed when used.

Noncurrent Cash

Noncurrent cash includes amounts restricted by trustee for debt reserve. Deposits are recorded at historical cost.

Investment Income

Interest on deposits is included in nonoperating revenues when earned.

Capital Assets

Capital asset acquisitions in excess of $5,000 are capitalized and recorded at cost. Depreciation is provided over the estimated useful life of each depreciable asset and is computed using the straight-line method. Equipment under capital lease obligations are amortized on the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. Amortization is included in depreciation in the financial statements. using the following asset lives:

Land improvements	5-20 years
Buildings and improvements	20-40 years
Equipment	3-7 years

Gifts of long-lived assets such as land, buildings, or equipment are reported as additions to unrestricted net position, and are excluded from revenues in excess of expense. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted net position.

Notes Receivable

Advances to physicians are comprised of physician income guarantees and/or business loans to those physicians requiring assistance to begin a local practice. The District has entered into agreements with certain physicians whereby the District guarantees their income for a specified period of time. These agreements are structured so that if a physician maintains a practice in the area for a specified period of time, the income guarantee in excess of collections may be forgiven in compliance with all federal and State laws and regulations. The allowance for doubtful accounts is primarily attributed to three physician advances that are potentially uncollectible.

Deferred Outflows of Resources

Deferred outflows of resources represent a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The deferred outflow of resources reported in the financial statements is deferred refunding costs which are amortized over the shorter of the remaining life of the refunded bonds or the refunding debt as a component of interest expense.

Deferred Inflows of Resources

Deferred inflows of resources represent an increase in net position that applies to future periods and so will not be recognized as an inflow of resources (revenue) until then. The deferred outflows of resources reported in the financial statements are unavailable property taxes. Property taxes will be recognized as revenue in the year they become available.

Operating Revenues and Expenses

The District's statement of revenues, expenses, and changes in net position distinguishes between operating and nonoperating revenues and expenses. Operating revenues and expenses of the District result from exchange transactions associated with providing health care services – the District's principal activity, and the costs of providing those services, including depreciation and excluding interest cost. All other revenues and expenses are reported as nonoperating.

Net Patient Service Revenue

The District has agreements with third-party payors that provide for payments to the District at amounts different from its established rates. Payment arrangements include prospectively determined rates, discounted charges, and per diem payments. 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.

Charity Care

The District provides health care services to patients who meet certain criteria under its charity care policy without charge or at amounts less than established rates. Since the District does not pursue collection of these amounts, they are not reported as patient service revenue. The estimated cost of providing these services was $54,000 for the year ended June 30, 2016, calculated by multiplying the ratio of cost to gross charges for the hospital by the gross uncompensated charges associated with providing charity care to its patients.

Grants and Contributions

The District may receive grants as well as contributions from individuals and 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 revenues in excess of expenses.

Electronic Health Record Incentives

The American Recovery and Reinvestment Act of 2009 (ARRA) amended the Social Security Act to establish incentive payments under the Medicare and Medicaid programs for certain hospitals and professionals that demonstrate meaningful use of certified Electronic Health Records (EHR) technology.

To qualify for the EHR incentive payments, hospitals and physicians must meet designated EHR meaningful use criteria. In addition, hospitals must attest that they have used certified EHR technology, satisfied the meaningful use objectives, and specify the EHR reporting period. This attestation is subject to audit by the federal government or its designee. The EHR incentive payment to hospitals for each payment year is calculated as a product of (1) an initial amount; (2) the Medicare share; and (3) a transition factor applicable to that payment year.

The District recognizes EHR incentive payments as revenue when there is reasonable assurance that the District will comply with the conditions attached to the incentive payments. EHR incentive payments are included in other operating revenue in the accompanying financial statements. The amount of EHR incentive payments recognized are based on management's best estimate and those amounts are subject to change with such changes impacting the period in which they occur.

The District recognized revenue of $887,769 for the year ended June 30, 2016 related to EHR incentive payments. These incentive payments are included in other revenue in the accompanying financial statements.

Subsequent Events

The District has evaluated subsequent events through April 25, 2017, the date which the financial statements were available to be issued.

Note 2 - Net Patient Service Revenue

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

Medicare: Inpatient acute care and outpatient services rendered to Medicare program beneficiaries are paid at prospectively determined rates per visit. These rates vary according to a patient classification system based on clinical, diagnostic, and other factors. The clinics are designated as Certified Rural Health Clinics by the Medicare program. As a result, clinical services rendered to Medicare program beneficiaries are reimbursed at cost (subject to various limits). The District is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the District and audits thereof by the Medicare Administrative Contractor (MAC). The District's Medicare cost reports have been audited by the MAC through the year ended June 30, 2014.

Medi-Cal: Inpatient acute rendered to Medi-Cal program beneficiaries are paid at prospectively determined rates per discharge. Outpatient services rendered to Medi-Cal program beneficiaries are paid at prospectively determined rates per outpatient ambulatory patient group The District's Medi-Cal cost reports have been settled by the fiscal intermediary through June 30, 2012.

The District has also entered into payment agreements with certain commercial insurance carriers and other organizations. 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.

Concentration of net revenues by major payor accounted for the following percentages of the District's patient service revenues for the year ended June 30, 2016:

Medicare	25%
Medicare managed care	13%
Medi-Cal	5%
Medi-Cal managed care	36%
Other commercial payors	15%
Self pay and other	6%
	100%

Laws and regulations governing the Medicare, Medi-Cal, and other programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates may change by material amounts in the near term as final settlements are determined. The net patient service revenue for the year ended June 30, 2016, increased approximately $550,000 due to adjustments to amounts previously estimated.

The Centers for Medicare and Medicaid Services (CMS) has implemented a Recovery Audit Contractor (RAC) program under which claims are reviewed by contractors for validity, accuracy, and proper documentation. A demonstration project completed in several other states resulted in the identification of potential overpayments, some being significant. If selected for audit, the potential exists that the District may incur a liability for a claims overpayment at a future date. The District is unable to determine if it will be audited and, if so, the extent of the liability of overpayments, if any. As the outcome of such potential reviews is unknown and cannot be reasonably estimated, it is the District's policy to adjust revenue for deductions from overpayment amounts or additions from underpayment amounts determined under the RAC audits at the time a change in reimbursement is agreed upon between the District and CMS.

Note 3 - Deposits

The carrying amounts of deposits as of June 30, 2016, is included in the District's statement of net position as follows:

Carrying Amount	
Cash and deposits	$ 11,404,419
Cash equivalents in Local Agency Investment Fund	9,560,297
Money market funds	1,982,297
Total	$ 22,947,013

Deposits are reported in the following statement of net position captions:

Cash	$ 11,404,419
Assets limited as to use available for current debt service	6,044,283
Restricted by trustee for debt reserve	5,498,311
	$ 22,947,013

Deposits – Custodial Credit Risk

Custodial credit risk is the risk that, in the event of a bank failure, bank deposits may not be returned to it. The District has a collateralization agreement with the bank, which mitigates custodial credit risk. The District's deposits in banks at June 30, 2016, were entirely covered by federal insurance or by collateral held by the District's custodial bank in the District's name.

Under the provisions of the California Government Code (CGC), California banks and savings and loan associations are required to secure the District's deposits by pledging government securities as collateral. The market value of pledged securities must equal to at least 110% of the District's deposits. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the District's total deposits. The pledged securities are held by the pledging financial institution's trust department in the name of the District.

Interest Rate Risk

The District invests in various money market funds, which are classified as assets limited as to use.

Interest rate risk is the risk that changes in market rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment the greater the sensitivity of its fair value to changes in market interest rates. The District does not have any policies specifically addressing interest rate risk.

Credit Risk

California Government Code, Section 53635, places the following concentration limits on the state investment pool and county investment pool: No more than 40% may be invested in eligible commercial paper, no more than 10% may be invested in the outstanding commercial paper of any single issuer, and no more than 10% of the outstanding commercial paper of any single issuer may be purchased.

Investment Income

Investment income, primarily interest income, for the year ended June 30, 2016 was $243,111.

Note 4 - Capital Assets

Capital assets as of June 30, 2016 were comprised of the following:

	Balance June 30, 2015	Additions	Transfers and Retirements	Balance June 30, 2016
Capital assets not being depreciated				
Land	$ 2,225,137	$ -	$ -	$ 2,225,137
Construction in progress	133,166,242	12,474,683	(7,452,005)	138,188,920
Total capital assets not being depreciated	$ 135,391,379	$ 12,474,683	$ (7,452,005)	$ 140,414,057
Capital assets being depreciated				
Land improvements	$ 1,076,735	$ -	$ -	$ 1,076,735
Building and improvements	43,402,724	184,150	1,262,410	44,849,284
Leasehold improvements	28,797	-	578,593	607,390
Equipment	33,586,890	1,453,778	853,240	35,893,908
Total capital assets being depreciated	$ 78,095,146	$ 1,637,928	$ 2,694,243	$ 82,427,317
Less accumulated depreciation for				
Land improvements	(862,216)	$ (31,352)	$ -	(893,568)
Building and improvements	(28,871,888)	(1,676,761)	-	(30,548,649)
Leasehold improvements	(28,797)	(65,466)	-	(94,263)
Equipment	(29,573,584)	(1,833,851)	21,804	(31,385,631)
Total accumulated depreciation	(59,336,485)	$ (3,607,430)	$ 21,804	(62,922,111)
Net capital assets being depreciated	$ 18,758,661			$ 19,505,206
Capital assets, net	$ 154,150,040			$ 159,919,263

As of June 30, 2016, the District had recorded $138,188,920 as construction-in-progress representing cost capitalized of $133,184,782 for the "Tower Project" and $5,004,138 for other various remodeling, major repair, equipment installation and other expansion projects on the District's premises. The District capitalized related interest expense, net of interest earnings on capital related funding, to the District expansion project of approximately $6,029,617 for the year ending June 30, 2016. Estimated costs to complete all projects as of June 30, 2016 are approximately $55 million.

As to the ongoing construction of the four-story, 115,000 square foot "Tower Project" specifically, the District entered into a construction contract March 2010 and construction began May 2010. The original completion date was December 2012; however, due to delays caused by several setbacks, the new completion date is now projected for approximately 14 to 16 months after additional financing is secured. The District Board unanimously agreed to pursue public financing to complete the tower. Although the General Obligation bond did not pass in August 2016, the Board remains committed to this project. That is evidenced by their approval in March 2017 of alternate financing, which will involve either the Housing and Urban Development FHA 242 program, or Office of Statewide Health Planning and Development Cal Mortgage.

Note 5 - Leases

The District leases (as lessor), certain owned facilities to various parties. Total lease income for the year ended June 30, 2016 was approximately $429,100. Lease income is included within other revenue in the statements of revenues, expenses, and changes in net position.

The District leases certain equipment under noncancealable long-term lease agreements. Certain leases have been recorded as capitalized leases and others as operating leases. Total lease expense for the year ended June 30, 2016 for all operating leases was $402,291. The capitalized leased assets consist of:

Major movable equipment	$ 2,870,541
Less accumulated amortization	(1,393,685)
	$ 1,476,856

The amortization expense for the capital leases are included as a component of depreciation and amortization.

Minimum future lease payments for the capital and operating leases are as follows:

Years Ending June 30,	Capital Leases	Operating Lease Expense
2017	$ 1,156,792	$ 365,100
2018	360,512	112,319
2019	197,671	93,292
2020	-	3,150
Total minimum lease payments	1,714,975	$ 573,861
Less interest	(59,538)	
Present value of minimum lease payments	$ 1,655,437	

Note 6 - Long-Term Debt

A schedule of changes in the District's long-term debt for the year ended June 30, 2016 is as follows:

	Balance June 30, 2015	Additions	Payments	Balance June 30, 2016	Due Within One Year
Bonds Payable					
Series 2005A GO Bond	$ 14,910,000	$ -	$ (65,000)	$ 14,845,000	$ 85,000
Series 2005B GO Bond	69,900,000	-	(220,000)	69,680,000	330,000
Series 2007 Revenue Bond	14,725,000	-	(525,000)	14,200,000	550,000
Capital Leases					
BA Capital lease	1,860,586	-	(1,234,454)	626,132	626,132
IBM Pureflex lease	425,086	-	(201,969)	223,117	205,700
IBM equipment lease	-	898,854	(145,161)	753,693	266,704
IBM software lease	-	64,488	(11,993)	52,495	19,148
Total long-term debt	$ 101,820,672	$ 963,342	$ (2,403,577)	$ 100,380,437	$ 2,082,684

Future interest due and principal maturities of debt borrowings, at June 30, 2016 are as follows:

	Long-Term Debt		
Years Ending June 30,	Principal	Interest	Total
2017	$ 2,082,684	$ 5,132,140	$ 7,214,824
2018	1,478,245	5,062,967	6,541,212
2019	1,499,500	4,994,485	6,493,985
2020	1,500,000	4,928,113	6,428,113
2021	1,700,000	4,853,916	6,553,916
2022-2026	12,235,000	22,551,627	34,786,627
2027-2031	20,755,000	18,208,743	38,963,743
2032-2036	29,865,000	11,562,697	41,427,697
2037-2041	29,265,008	2,990,165	32,255,173
Total	$ 100,380,437	$ 80,284,853	$ 180,665,290

Under the terms of the refunding revenue bonds and general obligation bonds agreements, the District is required to maintain certain deposits with a trustee. Such deposits are included with assets limited as to use in the financial statements.

The loan agreement also requires that the District satisfy certain measures of financial performance.

The interest payments for the general obligation bonds issued in 2009 are subsidized over the life of the issue by a U.S. Government stimulus program entitled "Build America Bonds" by approximately 32%, leaving the tax revenues to cover approximately 68%.

Note 7 - Pension Plan

The District discontinued the defined contribution pension plan effective August 26, 2015.

Note 8 - Related Party Transaction

As discussed in Note 1, the District is controlled by HCCA. The District incurred expenses of for management services and personnel costs from HCCA during the year ended June 30, 2016 of $36,826,628 which is included as leased employee expense in the statement of revenues, expenses and changes in net position. The total amount incurred and due to HCCA as of June 30, 2016 was $3,405,970 which is made up of a payable for management services and personnel costs of $4,244,564 offset with a receivable for reimbursable benefits of $838,594. These amounts are included in related party payables in the statement of net position.

Note 9 - Concentration of Credit Risk

The District grants credit without collateral to its patients, most of whom are insured under third-party payor agreements. The mix of receivables from third-party payors and patients at June 30, 2016 was as follows:

Medicare	24%
Commercial and other payors	24%
Medi-Cal program	46%
Self pay and other	6%
	100%

Note 10 - Commitment and Contingent Liabilities

Risk Management

The District is exposed to various risks of loss from torts; theft of, damage, of assets; business interruptions; errors and omissions; natural disasters. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage during the year.

Medical Malpractice Coverage

The District has joined together with other providers of health care services to form Beta Healthcare Group ("Beta"), a public entity risk pool (the "Pool") currently operating as a common risk management and insurance program for its members. The District purchases medical malpractice insurance from the Pool under a claims-made policy. The District pays an annual premium to the Pool for its torts insurance coverage. The District purchases excess liability insurance through a commercial insurer for amounts in excess of the coverage provided under Beta. The Pool's governing agreements specifies that the Pool will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of stop-loss amounts. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate costs of the incidents. At June 30, 2016, the District has accrued $180,000 for estimated malpractice costs.

Condensed financial information of Beta Healthcare Group as of and for the year ended December 31, 2015, is as follows:

Total assets	$ 433,786,141
Total liabilities	208,359,682
Fund balance	$ 225,426,459
Total revenues	$ 78,224,948
Total expenditures	(68,056,193)
Member dividends	(10,400,000)
Other changes in fund balance	(4,807,567)
Net decrease in fund balance	$ (5,038,812)

Other Commitments

The District has entered information or related service contracts with various providers, resulting in commitments as of June 30, 2016 of $2,280,000.

Note 11 - Litigation

Construction Delays

The District entered into a construction contract with Harris Construction Co., Inc. (Harris) for the construction of the "Tower Project" (the Project) in March 2010. Construction began around May 2010 and is presently ongoing. In early 2012, the District was informed by Harris that there were issues involving delaminated concrete within the Project that required remediation efforts. It was the position of the District that Harris was responsible for the concrete issue which has caused substantial delay to the Project. Harris contended that other delays were caused by alleged errors, omissions and deficiencies in the Project plans and drawings which have resulted in additional costs and other related impacts for Harris. The matter was settled with consideration given to both parties. The District is paying Harris approximately $6.9 million over a 48-month period, which began August 1, 2014 and incorporates a $33,750 payment each month, along with four quarterly installment payments totaling $1 million. The settlement also required Harris to disengage from the Project and dismiss all litigation against the District. Presently, the Project completion date is projected for approximately 14 to 16 months after additional financing is secured.

Other Litigation

The District is involved in numerous other litigation matters which generally arise in the normal course of doing business. After consultation with legal counsel, management estimates that these other matters existing as of June 30, 2016 will be resolved without material adverse effect on the District's future financial position, results from operations or cash flows.

Note 12 - Restatement

During 2016, the District identified misstates related to the 2015 financial statements. The District restated its previously issued financial statements to appropriately reflect the June 30, 2015 net position. The following is a summary of the effects of the restatement in the District's June 30, 2015 Net Position.

Net position, as previously reported	$ 76,151,047
Removal of bond issuance costs	(264,223)
Recognition of accrued property taxes	9,418,651
HCCA payable adjustment	(1,729,421)
HCCA payroll adjustment	(927,695)
Total restatement	6,497,312
Net position, as restated	$ 82,648,359

Supplementary Information
June 30, 2016

Tulare Regional Medical Center

The District maintains records to identify and monitor the level of charity care and community service it provides. These records include: the amount of charges foregone, (based on established rates), for services and supplies furnished under its charity care and community service policies, the estimated cost of those services and supplies, and statistics quantifying the level of charity care as a percentage of expenses of the District as a whole. The following is a summary of the Districts' charity care and community benefit expense for the year ended June 30, 2016, in terms of service to the poor and benefits to the broader community.

Benefits for the Poor	
Traditional charity care	$ 210,498
Unpaid Medi-Cal and County indigent program charges	101,363,003
Total	101,573,501
Benefits for the Broader Community	
Unpaid Medical program charges	57,449,749
Total Community Benefits	$ 159,023,250

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Directors
Tulare Local Health Care District
dba Tulare Regional Medical Center
Tulare, California

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of Tulare Local Health Care District dba Tulare Regional Medical Center (the District) which comprise the statement of net position as of June 30, 2016, and the related statements of revenues, expenses and changes 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 April 25, 2017.

Internal Control Over Financial Reporting
In planning and performing our audit of the financial statements, we considered the 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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. However, as described in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and another deficiency that we consider to be a significant deficiency.

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 District's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be material weaknesses (2016-A through 2016-F).

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. We consider the deficiency described in the accompanying schedule of findings and questioned costs to be significant deficiencies (2016-G).

Compliance and Other Matters
As part of obtaining reasonable assurance about whether the 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*.

District's Response to Finding
The District's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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 District'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 District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Eide Bailly LLP

Boise, Idaho
April 25, 2017

2016–A Report Preparation
Material Weakness in Internal Control Over Financial Reporting

Criteria
Management should have an internal control system in place designed to provide for the preparation of the financial statements being audited. This includes the ability to prepare the required footnote disclosures in accordance with Generally Accepted Accounting Principles (GAAP) and Governmental Accounting Standards Board (GASB). Additionally, this includes posting of all material adjustments necessary to close the year and accurately reflect the activity of the District throughout the year.

Condition
The District does not have an internal control system designed to provide for the preparation of the financial statements and related footnotes being audited in accordance with generally accepted accounting principles.

Cause
A process was not in place during the fiscal year to prepare financial statements.

Effect
Management relied on the auditing firm to report financial data in accordance with GAAP.

Recommendation
Management should implement a process for the preparation of the financial statements.

Views of Responsible Officials

We would like to clarify that there is a process in place, albeit that does meet all of the criteria required by Eide Bailly (EB). In an organization the size of TRMC there is no internal audit department that can keep abreast of GAAP and other pronouncements; we rely upon the expertise of our independent auditors. 2016 financials were prepared in the manner in which financial statements are prepared in prior years. The audit firms of Armanino LLP and TCA Partners LLP did not present comments or conclusions to the effect of EB's comments. For example, the treatment of the financial statements of the TDH Auxiliary and the Tulare Hospital Foundation was a wholesale departure from past treatment by audit professionals. Additionally, the treatment of general obligation bond revenue, as well as the treatment of unamortized bond costs, were a wholesale departure from past treatment, and therefore, were not prepared in advance in the way anticipated by EB. The process used internally for the interim statements is based upon our understanding of what the independent audit professionals will require. As 2016 is the first year audited by EB, we incurred a number of first year surprises in audit expectations. Procedural updates have since been incorporated into 2017 preparation practices.

2016–B Pervasive Errors and Difficulty Obtaining Appropriate Audit Support
Material Weakness in Internal Control Over Financial Reporting

Criteria
Management should have an internal control system in place designed to identify unusual transactions or activity within the general ledger, as well as have an organized management structure in place for retention and providing of supporting documentation.

Condition
As auditors, we experienced difficulty in obtaining appropriate support for our requests throughout the audit process. Additionally, the support provided was often incorrect or incomplete, and ultimately required adjustment, which resulted in material changes to the financial statements.

Cause
An effective process was not in place to identify potential and actual errors in accounting activity. Additionally, the management structure of the District lacked appropriate organization to provide timely and proper support for audit requests.

Effect
There were several corrected misstatements that were triggered by an ineffective process such as:

- Reclassifications to properly present long-term versus current portions.
- Adjustments and reclassifications to remove or properly clear debit balances in liability accounts.
- Adjustments to properly recognize remaining amortization of prepaid expenses.
- Adjustments to remove duplicated entries.
- Adjustment to recognize investment income related to bond reserve funds.
- Adjustments to amounts improperly recorded as accruals.
- Adjustments to record the recognition of deferred revenue.
- Adjustments to expense current period bond issuance costs.
- Adjustments to expense the portions of software that do not qualify for capitalization.
- Adjustment to agree the general ledger to the supporting detail for Clinic accounts receivable.
- Adjustment to adjust inventory in the general ledger to the inventory count details.
- Adjustment to reconcile beginning net position and clear out intercompany balances.

Additionally, significant audit efficiencies were lost due to lack of timely audit support.

Recommendation
Management should implement a process to ensure the general ledger is complete and has all transactions recorded for the fiscal year, as well as improve communication between members of the management team to expedite the providing of audit requests.

Views of Responsible Officials
EB was not able to obtain necessary working papers during their original scheduled work time, including their onsite work. This was a result of a convergence of obligations within the Finance department that stretched human resources to the point where all needs could not be met concurrently: the Cerner conversion tasks, the Great Plains conversion tasks, and concurrent Medicare and MediCal audits. It was an unfortunate occurrence that deprived EB staff of adequate responsiveness of hospital staff. Included in the above bullet points are, again, items that were unexpected based upon previous audit treatments. Hospital staffing was not adequate to provide sufficient advance reconciliation of a number of general ledger accounts and we have taken measures to bolster staffing in 2017.

2016–C Material Prior Period Adjustments
Material Weakness in Internal Control Over Financial Reporting

Criteria
Management should have an internal control system in place designed to identify material transactions for inclusion in the financial statements being audited.

Condition
As auditors, we identified material misstatements that related to prior periods.

Cause
A process was not in place to identify transactions that would have a material effect on the financial statements.

Effect
The auditing firm identified material audit adjustments that related to the prior period including:

- An adjustment to properly recognize deferred property tax revenues, property tax levy and deferred inflow or resources.
- An adjustment to recognize debt issuance costs as an expense.
- An adjustment to adjust payroll accruals related to the Health Care Conglomerate Associates (HCCA) payroll process.
- An adjustment to recognize a payable and receivable related to the payroll processing transactions with HCCA.

As a result of these prior period adjustments, the beginning balance in net position was understated by approximately $6,500,000.

Recommendation
Management should implement a process for the identification of transactions that could materially misstate the financials.

Views of Responsible Officials
The treatment of deferred property tax revenues, etc., was performed according to the specific instructions of two prior audit firms who each examined the issue at great length. The same is true of the treatment of debt issuance costs. We rely upon our independent auditor to advise us how to treat such issues. EB’s treatment is very different from past audit treatment, and we have made procedural changes in 2017 to accommodate the new instructions.

We agree there was a weakness relating to accounting for the HCCA payroll costs. This area was not neglected by any means; with no precedent, model, or template for carrying out the accounting, it proved challenging to understand and plan for appropriate accounting procedures.

2016–D Material Adjustments and Reconciliation Process
Material Weakness in Internal Control Over Financial Reporting

Criteria
Management should have an internal control system in place designed to identify material transactions for inclusion in the financial statements being audited.

Condition
As auditors, we identified material misstatements that related to the period under audit.

Cause
A process was not in place to properly reconcile account balances in the general ledger and to adjust the balances to the proper amounts. As a result we identified transactions that had a material effect on the financial statements.

Effect
The auditing firm identified material audit adjustments and reclassifications that related to the period under audit including:

- An adjustment to the allowance for the Hospital and ER Professional contractuals.
- Adjustments to record the receivables related to supplemental third party funding.
- An adjustment to eliminate the IBNR accrual as a result of the outsourcing of the labor pool to HCCA.
- An adjustment to cash for transactions not recorded in the general ledger.
- An adjustment to the late charge accrual and the associated effects on contractual allowances.
- An adjustment to adjust deprecation on assets that were impaired in the prior year.
- An adjustment to record the current year tax levy.
- An adjustment to record the current year payable and receivable related to the payroll processing transactions with HCCA.
- A reclassification of intercompany labor accrual due to a duplicated entry.
- A reclassification to recognize the current portion of restricted funds available for current debt service.
- A reclassification to reflect the Build America Bond interest receipt as a payable to Tulare County.
- A reclassification of patient accounts receivable refunds to a liability account.
- A reclassification to recognize the current portion of leases.
- A reclassification of ER Professional charity care expense to contractual expenses.
- A reclassification of litigation payments that were recorded in construction in process.

The result of these audit adjustments was a decrease of net position by approximately $3,000,000.

Recommendation
Management should implement a process for the identification of transactions that could materially misstate the financials.

Views of Responsible Officials
This issue is largely related to insufficient staffing to perform the work at hand. Finance staff was redirected for hundreds of hours during 2016 to respond to Public Record Act requests and perform analyses made necessary by requests from legal counsel. We will take steps to ensure material account balances are reconciled in 2017. We rely upon our independent auditor to advise us of GAAP requirements and pronouncements.

2016–E Review Process
Material Weakness in Internal Control Over Financial Reporting

Criteria
Management should have an internal control system in place with documented reviews.

Condition
As auditors, we identified material misstatements that related to the period under audit due to a lack of controls surrounding the review process.

Cause
An effective documented review process was not in place to prevent, detect, or correct material misstatements on a timely basis.

Effect
Material audit adjustments were identified by management and the auditors during the audit process.

Recommendation
Management should implement a documented review process that will effectively prevent, detect, or correct material misstatements on a timely basis as part of the reconciliation and journal entry processes.

View of Responsible Officials
Same response as for 2016-D.

2016-F Related Party Material Adjustments

Material Weakness in Internal Control Over Financial Reporting

Criteria
Management should have an internal control system in place designed to identify related party relationships and appropriately account for all related party activity according to signed agreements.

Condition
As auditors, we identified material misstatements specifically regarding transactions with a related party, HCCA, which relate to not only the period under audit, but the prior period. Due to the nature of the related parties and increased scrutiny of related party transactions by outside parties, the appropriate activity should have been recorded properly without adjustments by the auditor.

Cause
A process was not in place to identify related party transactions that would have a material effect on the financial statements.

Effect
The auditing firm identified material related party audit adjustments that related to the prior period including:

- An adjustment to adjust payroll accruals related to the HCCA payroll process.
- An adjustment to recognize a payable and receivable related to the payroll processing transactions with HCCA.
-

The auditing firm identified material related party audit adjustments that related to the period under audit including:

- An adjustment to record the current year payable and receivable related to the payroll processing transactions with HCCA.

Recommendation
Management should implement a process for the identification of transactions that could materially misstate the financials.

View of Responsible Officials
The treatment of HCCA related transactions has been a great challenge for Finance staff. The nature of the contractual arrangement between the District and HCCA is unique. There is no accounting model or template available to turn to in order to understand how to properly treat it. In addition, the sheer volume of payroll related transactions has made the accounting very cumbersome. We concede the lag in both timing and understanding of what is appropriate.

2016-G Accumulated Passed Adjustments
Significant Deficiency in Internal Controls Over Financial Reporting

Criteria
Management should have an internal control system in place designed to identify all necessary transactions for inclusion in the financial statements being audited.

Condition
As auditors, we identified significant transactions and account balances that though incorrect were not of a material threshold requiring recording of the entries. However, we note that this is indicative of the pervasive adjustments noted throughout our auditing procedures.

Cause
An effective process was not in place to identify unusual relationships, account balances, or errors in accounting transactions.

Effect
The auditing firm identified passed audit adjustments and reclassifications that related to the period under audit including:

- Passed adjustment to resolve a variance between book and bank value in cash
- Passed prior period adjustment to recognize grant revenue and depreciation on West Side Clinic
- Passed prior period adjustment for items included in Construction in Process that were subsequently expensed
- Passed audit adjustment to realize investment income
- Passed audit adjustment to remove incurred but not reported claims
- Passed audit adjustment to increase hospital contractual allowance

The results of the passed adjustments would have been to decrease revenues in excess of expenses by approximately $289,000.

Recommendation
Management should implement a process for the identification of transactions that could misstate the financials.

Views of Responsible Officials
Same response as for 2016-D.