

**FALLBROOK REGIONAL
HEATH DISTRICT
FINANCIAL STATEMENTS
JUNE 30, 2017**

FALLBROOK REGIONAL HEALTH DISTRICT

Financial Statements
For the Year Ended June 30, 2017

Table of Contents

	<u>Page</u>
Independent Auditor’s Report.....	1-2
Management’s Discussion and Analysis – Required Supplementary Information (Unaudited)	3-9
<u>Financial Statements</u>	
Statement of Net Position	10
Statement of Revenues, Expenses, and Changes in Net Position	11
Statement of Cash Flows	12
Notes to the Financial Statements.....	13-22



Craig R. Fechter, CPA, MST
Scott A. German, CPA

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
of the Fallbrook Regional Health District
Fallbrook, California

Report on Financial Statements

We have audited the accompanying financial statements of the Fallbrook Regional Health District (the "District"), which comprise the statement of net position as of June 30, 2017, 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.

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 audit. 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

To the Board of Directors
of the Fallbrook Regional Health District
Fallbrook, California

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, 2017, and the respective changes in financial position and cash flows thereof for the year 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 the Management's Discussion and Analysis on pages 3 through 9 be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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.

Fechter & Company
Certified Public Accountants



Sacramento, California
October 11, 2017

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis For the Year Ended June 30, 2017

The Fallbrook Regional Health District (District) has issued its financial statements for the fiscal year ended June 30, 2017 in conformity with the format prescribed by the provisions of Government Accounting Standards Board Statement No. 34 (GASB 34). This report, Management's Discussion and Analysis, is an overview of the financial activities for the fiscal year and is an integral part of the accompanying Basic Financial Statements.

ACCOUNTING METHOD

The District's operations are accounted for as an Enterprise Fund. Enterprise Funds are used by government agencies to account for operations which are financed and managed in a similar manner to private business enterprises, where the costs and expenses (including depreciation) of providing services to the public on a continuing basis are recovered primarily through user charges. The District receives property tax revenues. The District's revenues and expenses are recognized on a full accrual basis; revenues are recognized in the period incurred. All assets and liabilities associated with the activity of the enterprise are included on the Statement of Net Position.

THE BASIC FINANCIAL STATEMENTS

The District has only one fund, therefore the Basic Financial Statements do not reflect the activities of multiple funds. The Basic Financial Statements include the Statement of Net Position, Statement of Revenues, Expenses, and Changes in Net Position (Income Statement), and Statement of Cash Flows. Together with this report, the Basic Financial Statements provide information about the significant events, assumptions, and decisions resulting in the financial performance reflected in those statements.

The Statement of Net Position provides information regarding the financial position of the District, including its capital assets and debts.

The Statement of Revenues, Expenses, and Changes in Net Position (Income Statement) provides information regarding the revenues received by the District, and the expenses incurred in carrying out the District's programs. The ultimate focus of the income statement is the balance of effective current use of funds and planning for the future, as reflected by the amount of net income generated for the fiscal year.

The Statement of Cash Flows provides information regarding the sources and uses of the cash which flowed into and out of the District as a result of its operations and financing decisions.

FINANCIAL ACTIVITIES & FISCAL YEAR 2017 HIGHLIGHTS

Statement of Net Position

The District is a government entity operating under the Local Health Care District Law. In 1950, the residents of the area voted to establish, build, and operate Fallbrook Hospital. In 1971, the hospital was enlarged to its present 47-bed capacity.

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis For the Year Ended June 30, 2017

Since November 1998, the hospital has been leased under a 30-year agreement to Community Health Systems (CHS). The transaction was approved overwhelmingly by over 95% of District voters. A condensed version of the Statement of Net Position is presented in Table A below and the changes which occurred between Fiscal Year ended 2017 and 2016.

TABLE A

	2017	2016	Change
Assets:			
Cash and investments	\$ 6,789,887	\$ 6,319,945	\$ 469,942
All other assets	5,072,913	5,208,356	(135,443)
Total Assets	<u>11,862,800</u>	<u>11,528,301</u>	<u>334,499</u>
Liabilities:			
Current liabilities	94,177	59,142	(35,035)
Long-term liabilities	20,687	4,457	(16,230)
Total Liabilities	<u>114,864</u>	<u>63,599</u>	<u>(51,265)</u>
Net Position:			
Net investment in capital assets	292,910	291,601	1,309
Unrestricted	11,455,026	11,173,101	281,925
Total Net Position	<u>\$ 11,747,936</u>	<u>\$ 11,464,702</u>	<u>\$ 283,234</u>

The \$283,234 increase in Total Net Position reflects the change in net position for the year.

Statement of Revenues, Expenses, and Changes in Net Position

The District's business is comprised of three major segments:

- *Grant Program* – The District administers a grant program, giving a portion of the District's annual property tax revenues to non-profit health-related programs serving residents of the Fallbrook, Bonsall, Rainbow, and De Luz areas of northern San Diego County.
- *Community Health Fair* – The purpose of the Fair is to provide health screenings and access to information to residents that are readily accessible in the District for the entire community.
- *Community Collaboratives* – Representatives of the District's healthcare organizations and interested community members meet to network their programs, and identify, develop, and initiate District sponsored health related community programs and address concerns. Additional education opportunity for guest presentations relative to health, health services and conditions; ranging in scope from Aids and Alzheimer's to Suicide, Drug Abuse, and Legislative issues impacting health and well-being.

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis For the Year Ended June 30, 2017

Table B, below, is a condensed version of the Income Statement; it summarizes the District's revenue and expenses, and compares Fiscal Year 2017 results to Fiscal Year 2016.

TABLE B

	<u>2017</u>	<u>2016</u>	<u>Change</u>
Revenues:			
Property tax revenue	\$ 1,793,446	\$ 1,693,339	\$ 100,107
Total Revenues	<u>1,793,446</u>	<u>1,693,339</u>	<u>100,107</u>
Expenses:			
Community healthcare programs	708,686	643,231	(65,455)
Direct care services	99,000	294,000	195,000
Administrative services	360,580	339,490	(21,090)
Salaries and benefits	273,976	249,556	(24,420)
Management and maintenance	279,284	303,453	24,169
Depreciation	564	1,661	1,097
Total Expenses	<u>1,722,090</u>	<u>1,831,391</u>	<u>109,301</u>
Operating Income	<u>71,356</u>	<u>(138,052)</u>	<u>209,408</u>
Non-Operating Income (Expenses):			
Other income	211,878	364,362	(152,484)
Other expenses	-	-	-
Total Non-Operating Income	<u>211,878</u>	<u>364,362</u>	<u>(152,484)</u>
Change in Net Position	<u>\$ 283,234</u>	<u>\$ 226,310</u>	<u>\$ 56,924</u>

Property taxes drive the District's operations and are its primary source of revenues. The increase of \$100,107 in property taxes reflects the continuing turnaround in the real estate market and the general state of the economy within the District's service area.

Total non-operating income decreased by \$152,484 due to the decrease in revenues relating to the building sale, as well as the interest earnings available from investments set aside by the District. The subsidy for Direct Care Services was decreased in this fiscal year, with a drop of \$195,000 over the previous year.

The Grant Allocation increased by \$65,455 because the amounts requested and provided through the grant process varies from year to year.

Salaries and benefits increased by \$26,060 due to the change of staff, including a new Executive Director, as the District's role and responsibilities in the community have changed.

Administrative services reflect an overall increase of \$21,090. There was a decrease to general counsel in the amount of \$43,348. Independent contract services increased by \$22,923, due to a

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis
For the Year Ended June 30, 2017

change in accounting assistance. Consulting fees increased by \$30,961, due to community engagement services. The amount charged for California mandated reimbursement was reduced by \$13,445. Stipends were reduced by \$4,600, and I.T. and web services reduced by \$7,688, and office expense was reduced by \$5,893.

Direct Care Services, which was the agreement to assist the A+ Urgent Care facility for a period of time, in order to provide the Community with a medical facility to partially replace the hospital services, was in the amount of \$99,000.

CAPITAL ASSETS

At June 30, 2017, the District had \$310,763 in capital assets and \$19,162 accumulated depreciation resulting in \$291,601 net capital assets.

A summary of the activity and balances in capital assets is presented in Table C below.

TABLE C

	Balance July 1, 2016	Additions	Deletions	Balance June 30, 2017
Capital assets, depreciable:				
Buildings and improvements	\$ 291,240	\$ -	\$ -	\$ 291,240
Furniture and fixtures	2,375	-	-	2,375
Equipment	17,148	126	-	17,274
Subtotal	<u>310,763</u>	<u>126</u>	<u>-</u>	<u>310,889</u>
Accumulated depreciation	<u>(19,162)</u>	<u>(1,660)</u>	<u>-</u>	<u>(20,822)</u>
Capital Assets, Net	<u>\$ 291,601</u>	<u>\$ (1,534)</u>	<u>\$ -</u>	<u>\$ 290,067</u>

DEBT ADMINISTRATION

The District has no debt.

ECONOMIC OUTLOOK

The Fiscal Year 2016/2017 budget reflects a minimal increase in revenues, as property values/taxes are not anticipated to change much. Interest income is projected to increase, as funds have been received through the sale of the hospital building. Overhead is expected to remain about the same in the coming fiscal year. Capital expenditures are budgeted at \$0.

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis For the Year Ended June 30, 2017

MAJOR INITIATIVES

COMMUNITY HEALTHCARE PROGRAMS 2016-2017

Throughout fiscal year 2016-2017, the District sponsored and/or collaborated with local agencies and providers to identify, develop, support and/or deliver no-cost programs for prevention, education, treatment or services for the health and well-being of the residents of the community. Highlights of the Community Healthcare Programs were:

- The Community Collaborative Committee met each month for networking, identifying, assessing healthcare concerns and issues, and gaining information and resources to facilitate access to healthcare, and health promoting programs and services.
- Programs and events co-sponsored by the District also included the annual Prostate Screening (PSA) event, the Woman of Wellness, "WOW" educational monthly meeting program, and the annual Health and Fitness Fair.

2016-2017 Grant Program

The biggest Community Healthcare Program undertaken each year by FHD is the Grant Program. Only qualified, nonprofit, 501(c)(3), agencies may apply. Those who are awarded funding must meet strict criteria and provide comprehensive financial and service reports periodically throughout the grant year.

The District's focus: Prevention, Education, Treatment, and Ancillary Services

- Amount requested: \$809,069
- Amount funded: \$708,686
- Twenty-one grants awarded:
 - 7 Youth programs
 - 4 Seniors
 - 10 All ages

YOUTH

- Funding for two (2) health and wellness after-school programs provided throughout the elementary and middle school districts.
- Funding for children and youth who do not qualify for Medi-Cal or other public services who suffer from severe mental health disorders.
- Funding to address social and emotional needs of students with Asperger's Syndrome through a designated staff and center.
- Funding to continue a preschool ophthalmic screening and eye care program; inclusive of glasses and/or need treatment and follow-up care for children ages 2 to 6 years.
- Funding to engage youth in proactive prevention of access to and use of alcohol and drugs; and to bring awareness to youth, parents, educators and law enforcement.

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis For the Year Ended June 30, 2017

- Funding to provide a K-12 Safety Program to educate and inspire students to make life-saving choices regarding drugs and alcohol; car, bicycle, water safety and violence.

SENIORS

- Funding to evaluate and assist senior citizens with healthcare and home safety management through in home evaluations, safety checks and resource availability as well as assessments to help guide seniors to keep them living at home, independently.
- Funding to provide a program for senior and disabled residents and their caregivers that provides a secure and safe environment for activities and respite.
- Funding to provide senior and disabled citizens free transportation to medical and dental appointments, physical therapy, grocery stores and pharmacies which assists also in maintain budgets to ensure that medical care and food are accessible priorities.
- Funding to provide nutrition to needy seniors who have mobility and activities of daily living challenges through a home delivered meal program. Program through which needs can be assessed and referral to support programs can be made as identified.
- Volunteers dispatched through the 911 system at request of emergency responders.

ALL AGES

- Funding to increase access to psychiatric care for persons afflicted with biological brain disorders, behavioral/mental conditions that require medication and/or counseling treatment.
- Funding to provide a wide range of primary care, dental care and prevention services to underserved person of the District population.
- Funding to support the vision of nutritionally balanced supplemental food to those whose income is below the Federal guideline for poverty level.
- Funding to recruit, train, monitor and schedule the volunteer base that provides assistance with over 200 weekly therapy sessions for children and adults; also to fund Speech Therapy to increase receptive and expressive communication capabilities.
- Funding to facilitate a nutrition/diabetes/health education program at the community clinic and to continue health education and diabetes screening services in district schools as well as for seniors.
- Funding to continue and to expand dental care program for restorative and preventive services; and to screen children in local schools for existing or potential decay.
- Funding to continue development and implementation of community outreach to establish appropriate housing and support programs to provide a quality, safe living environment for special needs citizens.
- Funding to support courier program of transportation of District residents to healthcare provider appointments. Only program that will take persons to appointments out of the immediate Fallbrook community.
- Funding to facilitate Homecare Services for low and moderate income seniors and handicapped individuals to assist them to continue to live within their own homes.

FALLBROOK REGIONAL HEALTH DISTRICT

Management's Discussion and Analysis For the Year Ended June 30, 2017

- Funding of program to provide emotional and practical support to victims experiencing a trauma and to first responders.

During the fiscal year 2016-2017, the District received a total of \$809,069 in grant requests and approved distribution of \$708,686 to qualified applicants. This brings the total amount granted by the District since June 1999 to \$7,912,234.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

Fallbrook Regional Health District
138 South Brandon Road
Fallbrook, CA 92028
(760) 731-9187 Office
(760) 731-9131 Fax
Email: fallbrookbealthcare@earthlink.net
Website: www.fallbrookhealthcaredistrict.org

FINANCIAL STATEMENTS

**FALLBROOK HEALTHCARE DISTRICT
STATEMENT OF NET POSITION
JUNE 30, 2017**

ASSETS

Current Assets:	
Cash and cash equivalents	\$ 2,542,642
Investments	4,247,245
Reimbursement receivable	-
Taxes receivable	14,050
Interest receivable	7,817
Prepaid expenses	<u>46,776</u>
Total current assets	<u>6,858,530</u>
Non-current assets:	
Assets held for resale (Note 10)	4,711,360
Capital assets, net of accumulated depreciation	<u>292,910</u>
Total non-current assets	<u>5,004,270</u>
TOTAL ASSETS	<u><u>\$ 11,862,800</u></u>

LIABILITIES AND NET POSITION

Current liabilities:	
Accrued liabilities	<u>94,177</u>
Total current liabilities	<u>94,177</u>
Compensated absences	<u>20,687</u>
Total liabilities	114,864
Net Position	
Invested in capital assets, net	292,910
Unrestricted	<u>11,455,026</u>
Total net position	<u>11,747,936</u>
TOTAL LIABILITIES AND NET POSITION	<u><u>\$ 11,862,800</u></u>

The accompanying notes are an integral part of these financial statements

FALLBROOK HEALTHCARE DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2017

Operating revenues:	
Property taxes	\$ 1,793,446
	<u>1,793,446</u>
Total operating revenues	<u>1,793,446</u>
Operating expenses:	
Community healthcare programs	708,686
Direct care services	99,000
Administrative services	360,580
Salaries and benefits	273,976
Management and maintenance	279,284
Depreciation	564
	<u>1,722,090</u>
Total operating expenses	<u>1,722,090</u>
Operating income (loss)	<u>71,356</u>
Non-operating revenues and (expenses):	
Interest and investment income	21,248
Lease income	57,600
Gain on disposal of assets	133,030
	<u>211,878</u>
Total non-operating revenues and (expenses)	<u>211,878</u>
Change in net position	283,234
Beginning net position	<u>11,464,702</u>
Ending net position	<u><u>\$ 11,747,936</u></u>

The accompanying notes are an integral part of these financial statements

**FALLBROOK HEALTHCARE DISTRICT
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2017**

Cash flows from operating activities:

Cash received from County of San Diego for property taxes	\$ 1,779,396
Cash payments to vendors for goods and services	(709,356)
Cash payments to employees for services	(257,746)
Cash payments to grantees for programs	(705,629)
	<u>106,665</u>
Net cash provided by operating activities	<u>106,665</u>

Cash flows from capital and related financing activities:

Proceeds from lease of property	57,600
	<u>57,600</u>
Net cash provided by (used in) capital and related financing activities	<u>57,600</u>

Cash flows from capital and related financing activities:

Post-lease termination settlement activities (Note 10)	291,012
	<u>291,012</u>
Net cash provided by (used in) capital and related financing activities	<u>348,612</u>

Cash flows from investing activities:

Fixed asset additions	(4,472)
Interest revenue	10,042
	<u>10,042</u>
Net cash provided by investing activities	<u>5,570</u>

Net increase (decrease) in cash and cash equivalents	460,847
Cash and cash equivalents, beginning of year	2,081,795
	<u>2,081,795</u>
Cash and cash equivalents, end of year	<u>\$ 2,542,642</u>

Reconciliation of operating income (loss) to net cash provided by (used) by operating activities:

Operating income	\$ 71,356
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:	
Depreciation	564
Changes in operating assets and liabilities:	
Tax receivable	(14,050)
Prepaid items and deposits	(2,470)
Accrued liabilities	35,035
Compensated absence	16,230
	<u>16,230</u>
Net cash provided (used) by operating activities	<u>\$ 106,665</u>

The accompanying notes are an integral part of these financial statements

NOTES TO THE FINANCIAL STATEMENTS

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 1: Summary of Significant Accounting Policies

The financial statements of the Fallbrook Regional Health District (the “District”) have been prepared in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) as it applies to government units. The Governmental Accounting Standards Board (“GASB”) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the District’s accounting policies are described below.

A. Reporting Entity

The District, formerly known as the Fallbrook Hospital District, is organized under the provisions of the Health and Safety Code of the State of California to provide and operate health care facilities in Fallbrook, California, an unincorporated area within the County of San Diego, California (“County”).

B. Basis of Accounting and Measurement Focus

The financial statements include a Statement of Net Position, a Statement of Revenues, Expenses, and Changes in Net Position, and a Statement of Cash Flows.

The Statement of Net Position reports separate sections for Deferred Outflows of Resources and Deferred Inflows of Resources, where applicable.

Deferred Outflows of Resources represent outflows of resources (consumption of net position) that apply to future periods and that, therefore, will not be recognized as an expense until that time.

Deferred Inflows of Resources represent inflows of resources (acquisition of net position) that apply to future periods and that, therefore, are not recognized as revenue until that time.

These financial statements are accounted for using the “*economic resources*” measurement focus and the accrual basis of accounting. Accordingly, all of the District’s assets and liabilities, including capital assets, are included in the accompanying Statement of Net Position. The Statement of Revenues, Expenses, and Changes in Net Position presents the change in net position. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned while expenses are recognized in the period in which the liability is incurred. The Statement of Revenues, Expenses, and Changes in Net Position presents increases (revenues) and decreases (expenses) in total net position. Operating revenues are those revenues that are generated from property tax only. All other revenues are reported as non-operating revenues. Operating expenses are those expenses that are essential to the primary operations of the District. All other expenses are reported as non-operating expenses.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 1: **Summary of Significant Accounting Policies** - continued

C. Investments

Investment Valuation

Highly liquid investments with maturities of one year or less at the time of purchase are stated at amortized cost. All other investments are stated at fair value. Market value is used as fair value for those securities for which market quotations are readily available.

State Investment Pool

The District participates in the Local Agency Investment Fund (LAIF), an investment pool managed by the State of California. LAIF has invested a portion of the pool funds in Structured Notes and Asset-Backed Securities. These Structured Notes and Asset-Backed Securities are subject to market risk as a result of changes in interest rates. LAIF's investments are subject to credit risk with the full faith and credit of the State of California collateralizing these investments.

CalTrust Investment

The District also participates in CalTrust, which is a pool of diversified marketable bonds; including federal, federal agency, corporate, and California municipal bonds. The bonds are pooled in a Medium Term account and the pool is managed by Nottingham Investment Administration. CalTrust investments are subject to market risk as a result of changes in interest rates.

D. Property Taxes

Property taxes are levied on March 1 and are payable in two installments: November 1 and February 1 of each year. Property taxes become delinquent on December 10 and April 10, for the first and second installments, respectively. The lien date is March 1. The County of San Diego, California ("County") bills and collects property taxes and remits them to the District according to a payment schedule established by the County.

The County is permitted by State law to levy on properties at 1% of full market value (at time of purchase) and can increase the property tax rate at no more than 2% per year. The District receives a share of this basic tax levy proportionate to what it received during the years 1976-1978.

Property taxes are recognized in the fiscal year for which the taxes have been levied. No allowance for doubtful accounts was considered necessary.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 1: **Summary of Significant Accounting Policies** - continued

E. Assets Held for Resale

The District's assets held for resale are stated at the lower of fair market value or cost. These assets consist of a hospital building and a wellness center building and were acquired as part of the lease termination settlement with Fallbrook Hospital Corporation (Note 10). At June 30, 2017, the balance of assets held for resale was \$4,711,360.

F Capital Assets

The District's capital assets are stated at cost. Depreciation has been provided over the estimated useful lives of the assets using the straight-line method, generally 3-10 years. The capitalization threshold is \$500.

G. Compensated Absences

It is the District's policy to permit contract employees to accumulate earned but unused vacation leave time. Non-contract employees may accumulate earned but unused vacation leave time up to a maximum of thirty (30) days. All employees may accrue unused sick leave time up to a maximum of thirty (30) days. Upon termination, all employees are entitled to a lump sum payment of 25% of accrued sick leave, not to exceed fifteen (15) days. At June 30, 2017, compensated absences balance was \$22,327.

H. Net Position

Net position represents the difference between all other elements in the statement of net position and should be displayed in the following three components:

Net Investment in Capital Assets component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted component of net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets.

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

At June 30, 2016, the District had no restricted component of net position.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 1: **Summary of Significant Accounting Policies** - continued

H. **Net Position** - continued

Use of Restricted and Unrestricted Net Position

When an expense is incurred for purposes for which both restricted and unrestricted component of net position is available, the District's policy is to apply restricted component of net position first.

I. **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 amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Note 2: **Lease Agreement with Fallbrook Hospital Corporation**

Effective November 1, 1998, the District entered into a Lease Agreement ("Agreement") with Fallbrook Hospital Corporation ("Corporation"), a healthcare system located in the County to operate the Fallbrook Hospital for the benefit of District residents. While the hospital license remains in the name of the District, the Corporation has the responsibility of maintaining the license, maintaining the hospital in good condition, maintaining appropriate accreditations and adequate insurance, and providing quarterly status reports to the District. In connection with the Agreement, the District entered into a 30-year Transfer and Lease Agreement with the Corporation, whereby the District's assets and liabilities, except land, investment funds, debt established pursuant to certain loan agreements, and the deferred compensation program, were transferred to the Corporation. In November 1998, the District exercised its option to have the Corporation prepay the receivable to the District. Rental income to the District from the Corporation for the remaining term of the Agreement is \$1 per year.

At the end of the Agreement's 30-year term, the Corporation will transfer back to the District all assets and liabilities pursuant to terms substantially identical to those of the Transfer and Lease Agreement.

On March 31, 2015, the District and the Corporation entered into a Lease Termination Settlement Agreement to early terminate the Agreement. See Note 10 for further details.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 3: **Cash and Cash Equivalents**

The following is a summary of cash and cash equivalents at June 30, 2017:

	<u>Amount</u>
Cash and Cash Equivalents:	
Bank deposits	\$ 1,094,155
LAIF	1,448,487
Total Cash and Cash Equivalents	<u>\$ 2,542,642</u>

A. Cash Deposits

The carrying amount of the District’s cash deposits was \$1,094,155 as of June 30, 2016. Bank balances before reconciling items were \$1,096,751 at that date, which were fully insured or collateralized with securities held by the pledging financial institutions in the District’s name as discussed below.

The California Government Code requires California banks and savings and loan associations to secure the District’s cash by pledging securities as collateral. This Code states that collateral pledged in this manner shall have the effect of perfecting a security interest in such collateral superior to those of a general creditor. Thus, collateral for cash is considered to be held in the District’s name. The market value of pledged securities must equal at least 110% of the District’s cash. California law also allows financial institutions to secure the District’s cash by pledging first trust deed mortgage notes having a value of 150% of the District’s total cash.

B. Local Agency Investment Funds

The District’s deposit with LAIF at June 30, 2017, includes a portion of the pool funds invested in structured notes and asset-backed securities and similar transactions. These investments may include the following:

Structured Notes – Debt securities (other than asset-backed securities) whose cash-flow characteristics (coupon rate, redemption amount, or stated maturity) depend on one or more indices and/or that have imbedded forwards or options.

Asset-Backed Securities – Generally, mortgage-backed securities entitle their purchasers to receive a share of the cash flows from a pool of assets such as principal and interest repayments from a pool of mortgages (for example, collateralized mortgage obligations) or credit card receivables.

As of June 30, 2017, the District had \$1,448,487 invested in LAIF, which had invested 0% of the pool investment funds in Structured Notes and Asset-Backed Securities. The reported value of the pool is the same as the fair value of the pool shares.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 4: **Investments**

The District is generally authorized under state statutes to invest in:

- Obligations of the U.S. Government, its agencies, and instrumentalities
- Certificates of deposit and other evidences of deposit at commercial banks and savings and loan institutions
- Prime bankers acceptances
- Prime commercial paper
- Negotiable certificates of deposit
- Repurchase agreements
- Money market funds
- State of California Local Agency Investment Fund
- Medium-term notes

The following is summary of investments at June 30, 2017:

	<u>Credit Rating</u>	<u>Amount</u>
Investments:		
CalTrust	Not Rated	\$ 4,247,245
Total Investments		<u>\$ 4,247,245</u>

Investments held by the District, grouped by maturity date at June 30, 2017, were as follows:

	<u>Amount</u>
Investments:	
CalTrust	\$ 4,247,245
Total Investments	<u>\$ 4,247,245</u>

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 5: **Capital Assets**

Capital assets activities for the year ended June 30, 2016, are as follows:

	Balance July 1, 2015	Additions	Deletions	Balance June 30, 2016
Capital assets, depreciable:				
Buildings and improvements	\$ 291,240	\$ -	\$ -	\$ 291,240
Furniture and fixtures	2,375	-	-	2,375
Equipment	17,148	126	-	17,274
Subtotal	<u>310,763</u>	<u>126</u>	<u>-</u>	<u>310,889</u>
Accumulated depreciation	<u>(19,162)</u>	<u>(1,660)</u>	<u>-</u>	<u>(20,822)</u>
Capital Assets, Net	<u>\$ 291,601</u>	<u>\$ (1,534)</u>	<u>\$ -</u>	<u>\$ 290,067</u>

Note 6: **Commitment and Contingencies**

Earthquake Retrofit

Senate Bill 1953 imposes certain requirements that acute care hospitals would be required to meet within a specified time. These requirements include conducting seismic evaluations. Hospitals determined to pose certain risks shall only be used for non-acute care purposes after January 1, 2008. After January 1, 2030, all hospitals must be in compliance. The District is not liable for compliance with Senate Bill 1953 in accordance with the Agreement with the Fallbrook Hospital Corporation.

Note 7: **Insurance**

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters for which the District carries insurance through Special District Risk Management Authority (“SDRMA”). SDRMA is a risk pooling joint powers authority formed under the California Government Code to provide insurance coverage for SDRMA’s member districts. SDRMA purchases excess insurance from commercial carriers to reduce its exposure to large losses.

There were no instances in the past three years where a settlement exceeded the District’s coverage provided through SDRMA.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 8: **Transfers To/From Fallbrook Hospital Corporation**

All property tax revenues, as they are incrementally collected and paid to the District, will remain with the District and will not be shared, except as allocated by separate resolution. During the fiscal year ended June 30, 2017, no transfers were made to the Corporation.

Cost report settlements for all years prior to the Agreement have been settled.

Note 9: **Defined Contribution Pension Plan**

The District has a Section 408(p) defined contribution pension plan as allowed under the Internal Revenue Code. The plan type sponsored by the District is the Savings Incentive Match Plan for Employees of Small Employers (SIMPLE), which was effective on January 6, 2006. The Plan is a defined contribution retirement plan in which the employer's contribution is nondiscretionary and is based on a formula that is not related to profit. The Plan sponsor guarantees no benefit and bears no investment risk while the Plan participants bear all investment risk and have no guaranteed level of benefits.

Eligible non-contract employees may begin participating in the Pension Plan following a one year probationary employment period. The Administrator may begin participating the first day of the month following the employment date of work. The Plan is entirely funded by District contributions of up to 3% of the participants' gross pay for employees hired on or after March 1, 2006 who contribute up to 3% of their salary to the deferred compensation plan. Participants are fully vested upon joining the plan. Plan provisions and contribution requirements are established and may be amended by the District. Participants are eligible to begin receiving benefits at age 55.

The District's payroll for employees covered by the Plan for the year ended June 30, 2016, was \$0. Total employer contributions paid by the District amounted to \$0.

Funds paid into the Plan by the District are placed in a SIMPLE IRA account at a financial institution determined by the Plan participants. The financial information of the defined contribution pension plan is not in the accompanying financial statements.

Note 10: **Lease Termination Settlement**

The District leased the Fallbrook Hospital to the Fallbrook Hospital Corporation (the "Corporation") pursuant to a 30 year lease (the "Lease") in November 1998, which was set to terminate on its own terms in November 2028. Upon the expected termination of the Lease in 2028, the District was to absorb significant financial responsibilities, including, but not limited to, the repurchase of termination assets, reimbursement of prepaid rent (if any), and the need for working capital to keep the Fallbrook Hospital operating.

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 10: **Lease Termination Settlement** - continued

In order to ensure that the District had sufficient resources to accommodate the upcoming financial obligations, on December 14, 2011, the District's Board voted unanimously in favor of creating a lease termination contingency reserve which was expressly dedicated to address those expenses required of the District at the time that the lease with Fallbrook Hospital Corporation was set to end.

However, in December 2013, the District was presented with a Government Code claim (per section 910 of the California Government Code) from the Corporation. The claim was for the District's "refusal" to reimburse the Corporation for its operating losses for several hospital core services. In February 2014, the District issued a *Notice of Rejection of the First Code Claim* to the Corporation and declined to reimburse the core services losses.

Per the Lease, after notifying the District and providing reasonable supporting documentation substantiating the core service losses, the Corporation is allowed to commence the process of closing the core services that are operating at a loss. The District received notice from the Corporation on May 21, 2014, that the Corporation was initiating the process for closing of many of the core services. On September 11, 2014, the District and the Corporation signed the Agreement Regarding Continuation of Services in which the Corporation agreed to continue to provide certain core services through November 17, 2014. The District agreed to pay the Corporation \$711,000 for these services which was actually paid out during the 2014/2015 fiscal year.

Finally, on January 29, 2015, the District and the Corporation signed the *Settlement Agreement/Termination Agreement and Mutual Release* ("Settlement Agreement") in order to terminate the Lease Agreement and Operating Agreement effective March 31, 2015. The District agreed to pay the Corporation \$5 million by February 11, 2015. The Settlement Agreement released the District from the Corporation's previous breach of contract and operating loss coverage claims. It also released the District from any obligations under any repurchase agreements related to "Termination Assets" in the original Lease Agreement in 1998.

The District regained use rights for the Fallbrook Hospital Building, the Wellness Center Building, and the Urgent Care Building. At June 30, 2016, the Urgent Care building was being leased to a third party operator. The District is holding the other properties for sale or for lease. The District recorded the \$5 million settlement fee to these repurchased "Termination Assets" as follows:

FALLBROOK REGIONAL HEALTH DISTRICT

Notes to the Financial Statements
For the Year Ended June 30, 2017

Note 10: **Lease Termination Settlement** - continued

Address	<u>Description</u>	<u>Sq. Feet</u>	<u>Allocation %</u>	<u>Termination Fee Allocation*</u>
Assets Held for Resale:				
624 E. Elder	Fallbrook Hospital	75,840	88.35%	\$ 4,417,520
138 Brandon	Wellness Center	<u>5,000</u>	<u>5.83%</u>	<u>291,240</u>
		80,840	94.18%	4,708,760
Building and Improvements:				
617 Alvarado	Urgent Care Building	<u>5,000</u>	<u>5.82%</u>	<u>291,240</u>
		<u>85,840</u>	<u>100.00%</u>	<u>\$ 5,000,000</u>

* Schedule pertains to allocation of settlement payment under Termination and Settlement Agreement and is neither reflective of nor intended to represent the fair market value of the entire real property and improvements thereon.

Note 11: **Subsequent Events**

Subsequent events have been evaluated through October 11, 2017. On September 29, 2017 the District was able to sell the former hospital building located at 624 East Elder Street, Fallbrook, CA 92028 for the amount of \$4,265,053 to Fallbrook Partners, LLC located at 520 Capitol Mall, Suite 800, Sacramento, CA.