Tulare Local Health Care District
dba Tulare Regional Medical Center

Financial Statements

June 30, 2014
(With Comparative Totals for June 30, 2013)

armanino

TABLE OF CONTENTS

MANAGEMENT'S DISCUSSION AND ANALYSIS

- 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, 2014. Please read it in conjunction with the financial statements in this report.

FINANCIAL HIGHLIGHTS

- The District's net position increased by $4.4 million, or 7.9%, primarily attributable to the year's net income. Total assets increased by $7.3 million, or 3.9%. Cash and investments increased by $1.9 million, or 22.1%, resulting from an increase in cash generated from operations. Capital assets increased $15.1 million to $148.8 million with $15 million in net additions to buildings, equipment, and construction in progress, and a small net increase in accumulated depreciation.

- For the year, the District's total operating revenues decreased to $67.3 million, a 10.6% decrease from the prior year, while total operating expenses decreased to $70.3 million, a decrease of 10.1%. The current year decrease in total operating revenues was attributable to decreases in patient volume.

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

  - General construction and equipment for the new tower expansion
  - Acquisition of the IBM Pureflex server
  - Construction of the West Side and Earlimart clinics
  - Patient sleeper chairs, funded by the employee giving campaign

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

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.

MANAGEMENT'S DISCUSSION AND ANALYSIS

TABLE 1
Financial Analysis of the District

Condensed Balance Sheets
(in Thousands)

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

	June 30, 2014	June 30, 2013	Dollar Change	Total % Change
Current and other assets	$ 43,402	$ 51,168	$(7,766)	-15.2%
Capital assets	148,754	133,694	15,060	11.3%
Total assets	$192,155	$184,862	$ 7,293	3.9%
Current and other liabilities	$ 28,984	$ 24,662	$4,322	17.5%
Long-term debt outstanding	103,555	104,955	(1400)	-1.3%
Total liabilities	132,539	129,617	2,922	2.3%
Invested in capital assets – net of debt	46,076	40,622	5,454	13.4%
Restricted	2,258	2,144	114	5.3%
Unrestricted	11,282	12,479	(1,196)	-9.6%
Total net position	59,617	55,245	4,372	7.9%
Total liabilities and net position	$192,155	$184,862	$7,293	3.9%

As reflected in Table 1, net position increased $4.4 million to $59.6 million for the year ended June 30, 2014, primarily attributable to the District's $6.1 million income from GO bond tax revenue.

TABLE 2
Financial Analysis of the District (continued)

Condensed Balance Sheets
(in Thousands)

A summary of the District's balance sheets is presented in Table 2 below:

	June 30, 2013	June 30, 2012	Dollar Change	Total % Change
Current and other assets	$ 51,168	$ 67,199	$(16,031)	-23.9%
Capital assets	133,694	116,376	17,318	14.9%
Total assets	$184,862	$183,575	$ 1,287	0.7%
Current and other liabilities	$ 24,662	$ 28,106	$(3,444)	-12.3%
Long-term debt outstanding	104,955	104,955	0	0%
Total liabilities	129,617	133,061	(3,444)	-2.6%
Invested in capital assets – net of debt	40,622	36,529	4,093	11.2%
Restricted	2,144	11,515	(9,371)	-81.4%
Unrestricted	12,479	2,470	10,009	4052.2%
Total net position	55,245	50,514	4,731	9.4%
Total liabilities and net position	$184,862	$183,575	$ 1,287	0.7%

As reflected in Table 2, net position increased $4.7 million to $55.2 million for the year ended June 30, 2013, primarily attributable to the District's $6.1 million income from GO bond tax revenue.

MANAGEMENT'S DISCUSSION AND ANALYSIS

TABLE 3
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:

	Years Ended			
	June 30, 2014	**June 30, 2013**	**Dollar Change**	**Total % Change**
Net patient services revenue	$64,164	$67,625	$(3,461)	-5.1%
Other operating revenue	3,128	7,302	(4,174)	-57.2%
Total operating revenues	67,293	74,927	(7,634)	-10.2%
Salaries and benefits	31,459	36,200	(4,741)	-13.1%
Medical and other supplies	8,738	11,633	(2,895)	-24.9%
Medical and other fees and services	20,921	22,504	(1,583)	-12.7%
Maintenance, utilities, and rent	2,802	2,658	144	7.0%
Depreciation and amortization	4,402	4,026	376	9.3%
Other	1,941	922	1,019	110.5%
Total operating expenses	70,264	77,943	(7,679)	-9.9%
Operating loss	(2,972)	(3,016)	44	1.5%
Non-operating revenues & expenses	1,227	1,707	(480)	-28.1%
Loss before taxes for GO bond debt	(1,745)	(1,308)	(437)	-33.4%
District taxes for GO bond debt	6,117	6,039	78	1.3%
Change in net position	$ 4,372	$ 4,731	$ (359)	-7.6%%
Net position – beginning of year	$55,245	$50,514	$4,731	9.4%
Net position – end of year	$59,617	$55,245	$4,372	7.9%

MANAGEMENT'S DISCUSSION AND ANALYSIS

TABLE 4
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:

	Years Ended			
	June 30, 2013	**June 30, 2012**	**Dollar Change**	**Total % Change**
Net patient services revenue	$67,625	$66,904	$ 721	1.1%
Other operating revenue	7,302	7,673	(371)	-4.8%
Total operating revenues	74,927	74,577	350	0.5%
Salaries and benefits	36,200	40,058	(3,858)	-9.6%
Medical and other supplies	11,633	12,188	(555)	-4.6%
Medical and other fees and services	22,504	24,091	(1,587)	-6.6%
Maintenance, utilities, and rent	2,658	2,773	(115)	-4.3%
Depreciation and amortization	4,026	3,143	883	28.1%
Other	922	2,912	(1,990)	-68.3%
Total operating expenses	77,943	85,165	(7,222)	-8.5%
Operating loss	(3,016)	(10,588)	7,572	71.5%
Non-operating revenues & expenses	1,707	1,320	387	29.3%
Income before taxes for GO bond debt	(1,308)	(9,268)	7.960	85.9%
District taxes for GO bond debt	6,039	6,088	(49)	-0.8%
Change in net position	$ 4,731	$(3,180)	$ 7,911	248.8%
Net position – beginning of year	$50,514	$53,694	$(3,180)	-5.9%
Net position – end of year	$55,245	$50,514	$ 4,731	9.4%

MANAGEMENT'S DISCUSSION AND ANALYSIS

SOURCES OF REVENUE

Operating revenues – For fiscal year 2014, the District derived 89.2% 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 2014, the District derived 10.8% 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 2014 and 2013:

Acute admissions decreased by 941, or 20.0%, to 3,786, while acute patient days decreased by 3,944, or 21.5%, to 14,366. Outpatient visits (ER visits, home health visits, outpatient surgeries, referred visits for diagnostic services and clinic visits) were 10,264, or 9.1%, below 2013 levels. Although ER visits were up slightly, the remaining outpatient services all experienced declines, contributing to the overall decrease in outpatient activity for 2014.

Net patient services revenue decreased $3.5 million, or 5.1%, in 2014. The decrease in net patient services revenue can be attributed to lower patient volumes. The District recognized $8.7 million of supplemental state funding for MediCal in 2014.

Net patient services revenue per adjusted patient day (the amount of patient services revenue actually collected per equivalent patient encounter) increased from $1,849 to $1,949, or 5.4%, from 2013 to 2014, primarily due to two factors: the clinical documentation improvement program, which impacts the case mix index and therefore Medicare inpatient reimbursement; and the change in MediCal inpatient reimbursement from a per-diem methodology to a California DRG methodology.

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 decreased by $4.2 million, or 52.7%. This significant decrease came as a result of the closure and sale of the retail pharmacy business in May 2013.

Salaries and benefits expense decreased $4.7 million, or 13.1%. While salaries and wages decreased by $3.6 million, or 13.7% over prior year, employee benefits expense decreased $1.1 million, or 11.5%, from 2013. This decrease was a result of reduction of paid FTEs to 380 in June 2014, compared to 431 in the prior year. The decrease in patient volume combined with efforts at becoming more efficient with staffing combined to achieve this result.

Medical and other supplies decreased $2.9 million, or 24.9%, from 2013 due to the aforementioned decrease in patient volumes, and the related cost of medical surgical supplies and pharmaceuticals.

MANAGEMENT'S DISCUSSION AND ANALYSIS

OPERATING AND FINANCIAL PERFORMANCE (CONTINUED)

Medical and other fees and services decreased $1.6 million, or 12.7%, primarily due to the reduction of legal fees.

Maintenance, utilities, and rent increased by $145,000, or 5.4%, during 2014 primarily due to an increase in general utility cost throughout the plant, as well as increased telecom costs managed by the IT department.

Depreciation and amortization expense increased $376,000, or 9.3%, as several completed projects were added to the depreciation schedule.

Other expenses increased by $1.0 million, or 110.5%, resulting mainly from a one-time offset in the prior year for $797,000 that did not recur.

Total operating expenses decreased by $7.7 million, or 9.9%, primarily due to salaries and benefits, and medical and other supplies.

Non-operating revenues of $2.0 million for fiscal year 2014 are comprised of $1.6 million of tax revenue received from the County of Tulare, $295,000 in grants & contributions, $104,000 in investment income on cash and investments, and $51,000 in other income. Tax revenue increased by $71,000 in 2014. 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 2014 decreased by $31,000 from 2013 due to a decrease in available cash and a decrease in investment yields.

Non-operating expenses represent interest expense paid during 2014 on the District's short- and long-term debt consisting of revenue bonds and capital leases. Total interest expense of $808,000 decreased by $31,000, or 3.7%, from 2013.

For fiscal year 2014, district taxes for general obligation bond debt remained steady at $6.1 million. This restricted revenue is managed by the County of Tulare.

MANAGEMENT'S DISCUSSION AND ANALYSIS

OPERATING AND FINANCIAL PERFORMANCE (CONTINUED)

The following summarizes the District's statements of revenues, expenses, and changes in net position between 2013 and 2012:

Acute admissions decreased by 610, or 11.4%, to 4,727, while acute patient days decreased by 2,772, or 13.1%, to 18,310. Outpatient visits (ER visits, home health visits, outpatient surgeries, referred visits and clinic visits) were 17,243, or 13.3%, below 2012 levels. Rural health clinic visits and referred visits were significantly down, while emergency room visits held steady.

Net patient services revenue increased $721,000, or 1.1%, in 2013 due to decreases in patient volumes offset by price increases and contracting improvements.

Net patient services revenue per adjusted patient day (the amount of patient services revenue actually collected per equivalent patient encounter) increased from $1,656 to $1,849, or 11.7%, from 2012 to 2013, primarily due to improvements in third party payor contract rates and improved efficiencies within the revenue cycle.

Other operating revenue consists primarily of cafeteria sales, health and fitness center membership sales and dues, retail pharmacy sales, and rental revenue from medical office buildings leased by the District. Other operating revenue decreased by $371,000, or 4.8%. This increase came from a legal judgment against a service provider.

Salaries and benefits expense decreased $4.7 million, or 13.1%. Salaries and wages experienced an 13.4% decrease from 2012 primarily due to a decrease in total worked hours resulting from the decreased inpatient and outpatient volumes noted above. Employee benefits expense decreased 11.5% from 2012, attributable to a decrease in total worked hours and the associated PTO earnings.

Medical and other supplies decreased $555,000, or 4.6%, over 2012 due to the aforementioned decrease in patient volumes, and the related cost of medical surgical supplies and pharmaceuticals.

Medical and other fees and services decreased $1.6 million, or 6.6%, attributable to the insourcing of fitness center personnel that occurred mid-year.

Maintenance, utilities, and rent decreased by $115,000, or 4.3%, during 2013 primarily due to the cost of replacing a CT tube in 2012 that did not recur in 2013.

Depreciation and amortization expense increased $376,000, or 4.4%.

Other expenses decreased by $2.0 million, or 68.3%, resulting mainly from a legal settlement that was recorded as an audit adjustment.

Total operating expenses decreased by $7.7 million, or 9.9%, primarily due to decreased volumes and associated decreases in expenses as explained above.

MANAGEMENT'S DISCUSSION AND ANALYSIS

OPERATING AND FINANCIAL PERFORMANCE (CONTINUED)

Non-operating revenues of $2.3 million for fiscal year 2013 are comprised of $1.5 million of tax revenue received from the County of Tulare, $248,000 in grants and contributions, $102,000 in investment income on cash and investments, and $683,000 in other income. Tax revenue decreased by $61,000 in 2013. Investment income represents interest income and realized and unrealized gains and losses on District and Foundation 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 2013 decreased by $63,000 from 2012 due to decreased available cash to invest combined with declining investment rates.

Non-operating expenses represent interest expense paid during 2013 on the District's short- and long-term debt consisting of revenue bonds and capital leases. Total interest expense of $839,000 increased by $30,000, or 3.7%, from 2012.

For fiscal year 2013, district taxes for general obligation bond debt increased slightly to $6.1 million. This restricted revenue is managed by the County of Tulare.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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 2014 budget comparison and analysis is presented below.

TABLE 5
Actual vs. Budget
(in Thousands)

	Years Ended			
	June 30, 2014	**June 30, 2014**	**Dollar variance**	**Total % variance**
Net patient services revenue	$64,164	$62,280	$1,884	3.0%
Other operating revenue	3,128	3,921	(793)	-20.2%
Total operating revenues	67,293	66,202	1,091	1.6%
Salaries and benefits	31,459	32,120	(661)	-2.1%
Medical and other supplies	8,738	9,615	(877)	-12.9%
Medical and other fees and services	20,921	18,530	2,391	12.2%
Maintenance, utilities, and rent	2,802	2,426	376	15.5%
Depreciation and amortization	4,402	4,192	210	5.0%
Other	1,941	1,688	253	15.0%
Total operating expenses	70,264	68,571	1,693	2.5%
Operating loss	(2,972)	(2,370)	(602)	-25.4%
Non-operating revenue & expenses	1,227	1,023	204	19.9%
Loss before taxes for GO bond debt	(1,745)	(1,347)	(398)	-29.5%
District taxes for GO bond debt	6,117	4,397	1,720	39.1%
Change in net position	$ 4,372	$ 3,050	$1,322	43.3%

BUDGET RESULTS (CONTINUED)

In comparing actual versus budgeted 2014 results, the following is noted:

The District completed its fiscal year 2014 $1.3 million, or 43.3%, in excess of budgeted income. The excess of profitability compared to budget is attributable to district taxes for GO bond debt, and income from operations.

The District's operating income fell short of budget expectations by $602,000, or 25.4%. Net patient services revenue exceeded budget by $1.9 million, or 3.0%, due to better-than-expected collectability rates. Other operating revenue fell short of budget by $793,000, or 20.2%.

The District realized an unfavorable variance in total operating expenses of $1.7 million, or 2.5%. This unfavorable expense variance was primarily due to fees paid to the operations management company, and costs associated with aligning the District with the management company.

CAPITAL ASSETS

At June 30, 2014, the District had $149 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 $15.1 million from the end of the prior year.

	June 30, 2014	June 30, 2013	Dollar Change	Total % Change
Land and improvements	$ 3,302	$ 3,203	$ 99	3.1%
Buildings and improvements	43,025	43,486	(461)	-1.1%
Leasehold improvements	29	50	(21)	-42.5%
Equipment	31,706	35,523	(3,817)	-10.7%
Construction in progress	124,622	106,803	17,819	16.7%
Gross capital assets	202,684	188,765	13,919	7.4%
Less Accumulated depreciation	53,930	55,071	(1,141)	-2.1%
Net capital assets	$148,754	$133,694	$15,060	11.3%

Material additions during FY 2014 included (in thousands):

Tower 1 construction and financing	$15,689
IBM Pureflex server	$ 598
West Tulare Clinic	$ 330
Earlimart Clinic	$ 91
Tower 2 development	$ 26

Current year activity was predominantly focused upon the new tower expansion. Presently, the Project completion date as required by the Project is now projected for approximately 14-16 months after additional financing is secured.

In addition, a new server platform for the IT system was purchased. Work was completed on the West Tulare clinic, and ongoing development costs were incurred in relation to the future Earlimart clinic. A small amount was also invested in research for the proposed tower 2 project.

MANAGEMENT'S DISCUSSION AND ANALYSIS

LONG-TERM DEBT

At June 30, 2014, the District had approximately $103,855,000 in capital lease obligations and revenue and general obligation bonds outstanding.

Principal balance in thousands

Revenue bond issuance of 2007	$15,230
GO bond series A issuance	$14,955
GO bond series B issuance	$70,000
Bank of America capital equipment lease	$ 3,072
IBM Financing capital equipment lease	$ 598

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 2014.

On August 28, 2014, Fitch Ratings affirmed the 'B' rating on the District's $15.2 million series 2007 bonds, removed the Rating Watch Negative, and improved the Rating Outlook to Stable. Fitch noted the removal from Rating Watch Negative reflects growing clarity and progress on construction plans achieved over the last six months. Fitch noted that a settlement was reached with the previous contractor in July 2014, a new team has been put in place under HCCA leadership, and a completion plan has been established. Fitch also noted the Stable Outlook reflects the dramatic turnaround in operating and financial performance since Fitch's last review in February 2014. Fitch indicated that the positive trend over the last few months indicate performance improvement plans taking hold and signal recovery.

The general obligation bonds represent the general obligation of the District. 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 October 2014, Moody's Investors Services downgraded the District's $85 million general obligation bond rating from Baa1 to Baa3. According to Moody's, "The downgrade primarily reflects the district's significantly narrowed financial operations over the last few years and the risks resulting from its mismanagement of the GO-funded construction project… notwithstanding the district's financial and operational challenges, the Baa3 rating also significantly reflects the fundamental strength of the pledged, voter-approved, unlimited property tax that secure the district's GO bonds."

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%.

MANAGEMENT'S DISCUSSION AND ANALYSIS

ECONOMIC OUTLOOK

In January 2014 the District's Board brought in a new management company, Healthcare Conglomerate Associates (HCCA). HCCA, in conjunction with the District's Board, recruited a new Chief Executive Officer/Chief Restructuring Officer with specific expertise and experience in turning around hospitals. HCCA and the new CEO recommended to the District's Board that the 2015 budget for the first quarter be essentially rolled over from the prior year budget. The Board concurred with that approach. The rationale was that the Hospital and affiliated entities are undergoing significant financial and operational improvements. An operating budget that was developed prior to the start of the 2015 fiscal year (as is typical), would more than likely be obsolete very quickly. Developing a detailed budget also would district from all of the detailed work going on to drastically improve the financial operations.

Through the first three months of fiscal year 2015, the District has posted an unaudited operating income of $1.3 million, a 7% operating margin, putting the District approximately $4.5 million ahead of its prior year operating income for the first three months of the fiscal year. Through September 30, 2014, the District experienced net income before contributions of $2.7 million, or a 13.3% excess margin, representing a positive variance of $3.1 million from its prior year-to-date income before contributions of ($1.4 million).

The operating income and income before contributions variances are attributable to a positive variance in total operating revenue and also expenses, mainly employment expenses.

armanino

INDEPENDENT AUDITOR'S REPORT

The Board of Directors
Tulare Regional Medical Center
Tulare, California

Report on the Financial Statements

We have audited the accompanying financial statements of Tulare Local Health Care District, (dba Tulare Regional Medical Center, or the District) which comprise the statement of net position as of June 30, 2014 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 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. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion the financial statements referred to above present fairly, in all material respects, the financial position of the District as of June 30, 2014, and changes in its financial position and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Other Matters - Uncertainties

As more fully described in Note 13 to the financial statements, the District has materially exceeded the Tower project budget, and may not be able to secure the required financing to complete the project. The District's plans in regard to this matter are also described in Note 13. The financial statements do not include any adjustments to reflect the possible impairment of this asset. Our opinion is not modified with respect to that matter.

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 1 - 15 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.

Report on Summarized Comparative Information

We have previously audited the District's 2013 financial statements, and our report dated December 9, 2013, expressed an unmodified opinion on those audited financial statements and our report emphasized other matters related to OIG Self-Reporting and Going Concern uncertainties that have been removed for the current year. In our opinion, the summarized information presented herein as of and for the year ended June 30, 2013, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Armanino LLP

Armanino LLP
San Ramon, California

November 24, 2014

TULARE REGIONAL MEDICAL CENTER
Statement of Net Position
June 30, 2014
(with comparative totals for 2013)

ASSETS

	2014	2013
Current assets		
Cash and cash equivalents	$ 10,568,946	$ 8,657,613
Assets limited as to use available for current debt service	7,389,395	8,648,655
Patient accounts receivable, net of allowances	7,033,711	7,763,678
Other receivables and physician advances	9,743,501	7,305,939
Inventories	961,953	1,349,617
Prepaid expenses and deposits	422,634	976,027
Total current assets	36,120,140	34,701,529
Assets limited as to use, long term	6,153,681	15,177,000
Capital assets, net of accumulated depreciation	148,753,523	133,693,937
Bond issuance costs, net of accumulated amortization	1,128,068	1,289,694
Total assets	$ 192,155,412	$ 184,862,160

LIABILITIES AND NET POSITION

	2014	2013
Current liabilities		
Current maturities of debt borrowings	$ 2,036,139	$ 1,698,152
Accounts payable and accrued expenses	14,134,570	11,180,505
Accrued payroll and related liabilities	2,068,077	2,382,591
Estimated current third party payor settlements	1,976,974	1,101,828
Self-insurance program accrual	1,039,656	918,000
Total current liabilities	21,255,416	17,281,076
Deferred revenue	9,464,703	9,079,552
Debt borrowings, net of current maturities	101,818,427	103,256,666
Total liabilities	132,538,546	129,617,294
Net position		
Net investment in capital assets	46,076,431	40,621,937
Restricted, by bond indenture for debt service	2,258,443	2,143,763
Unrestricted	11,281,992	12,479,166
Total net position	59,616,866	55,244,866
Total liabilities and net position	$ 192,155,412	$ 184,862,160

The accompanying notes are an integral part of these financial statements.

TULARE REGIONAL MEDICAL CENTER
Statement of Revenues, Expenses and Changes in Net Position
For the Year Ended June 30, 2014
(with comparative totals for 2013)

	2014	2013
Operating revenues		
Net patient service revenue	$ 64,164,408	$ 67,624,586
Other operating revenue	3,128,424	7,302,491
Total operating revenues	67,292,832	74,927,077
Operating expenses		
Salaries and wages	22,982,604	26,624,721
Employee benefits	8,476,407	9,575,495
Professional fees	7,821,892	9,132,574
Contract labor and registry	397,725	311,439
Supplies	8,738,478	11,632,935
Purchased services	12,701,563	13,060,524
Repairs and maintenance	354,568	310,416
Utilities and phone	1,645,543	1,438,533
Building and equipment rent	802,268	908,813
Insurance	790,171	605,835
Depreciation and amortization	4,402,184	4,025,809
Other operating expenses	1,150,970	315,715
Total operating expenses	70,264,373	77,942,809
Operating loss	(2,971,541)	(3,015,732)
Nonoperating revenues (expenses)		
District tax revenues	1,584,532	1,513,773
Investment income	104,281	101,961
Interest expense	(808,491)	(839,225)
Grants and contributions	295,404	247,812
Other income	51,120	683,011
Total nonoperating net revenues	1,226,846	1,707,332
Excess of expenses over revenues	(1,744,695)	(1,308,400)
District taxes related to general obligation bonds debt service	6,116,695	6,039,069
Increase in net position	4,372,000	4,730,669
Net position at beginning of the year	55,244,866	50,514,197
Net position at end of the year	$ 59,616,866	$ 55,244,866

The accompanying notes are an integral part of these financial statements.

TULARE REGIONAL MEDICAL CENTER
Statement of Cash Flows
For the Year Ended June 30, 2014
(with comparative totals for 2013)

	2014	2013
Cash flows from operating activities		
Cash received from patients and third-parties on behalf of patients	$ 63,331,959	$ 65,207,971
Cash received from operations, other than patient services	3,128,424	7,302,491
Cash payments to suppliers and contractors	(30,386,398)	(38,684,206)
Cash payments to employees and benefit programs	(31,773,525)	(37,063,346)
Net cash provided by (used in) operating activities	4,300,460	(3,237,090)
Cash flows from noncapital financing activities		
District tax revenues	1,584,532	1,513,773
Non-capital grants, contributions and other	(357,686)	193,559
Net cash provided by noncapital financing activities	1,226,846	1,707,332
Cash flows from capital and related financing activities		
Net purchase of capital assets	(18,317,096)	(21,182,218)
District tax revenues for debt service	6,116,695	5,402,866
Principal payments on debt borrowings	(1,698,151)	(1,640,656)
Net cash used in capital financing activities	(13,898,552)	(17,420,008)
Cash flows from investing activities		
Net (purchase) or sale of investments	10,178,298	14,336,004
Interest and dividends received from investments	104,281	101,961
Net cash provided by investing activities	10,282,579	14,437,965
Net increase (decrease) in cash and cash equivalents	1,911,333	(4,511,801)
Cash and cash equivalents at beginning of year	8,657,613	13,169,414
Cash and cash equivalents at end of year	$ 10,568,946	$ 8,657,613
Non-cash Activity:		
Acquisiton of equipment through capital lease obligation	$ 597,899	$ -

The accompanying notes are an integral part of these financial statements.

TULARE REGIONAL MEDICAL CENTER
Statement of Cash Flows (continued)
For the Year Ended June 30, 2014
(with comparative totals for 2013)

	2014	2013
Reconciliation of operating loss to net cash provided by (used in) operating activities		
Operating loss	$ (2,971,541)	$ (3,015,732)
Adjustments to reconcile operating loss to net cash provided by operating activities		
Depreciation and amortization	4,402,184	4,025,809
Changes in operating assets and liabilities		
Patient accounts receivables	729,967	825,399
Other receivables	(2,437,562)	(4,065,093)
Inventories	387,664	211,397
Prepaid expenses and deposits	553,395	(51,870)
Accounts payable and accrued expenses	2,954,065	(1,104,949)
Accrued payroll and related liabilities	(314,514)	(863,130)
Estimated third party payor settlements	875,146	823,079
Self-insured program accrual	121,656	(22,000)
Net cash provided by (used in) operating activities	$ 4,300,460	$ (3,237,090)

The accompanying notes are an integral part of these financial statements.

1. Organization and Significant Accounting Policies

Reporting entity

Tulare Local Health Care District (dba Tulare Regional Medical Center, e.g. 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 is generally not subject to federal or state income taxes. 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.

Basis of preparation

The District's financial statements are presented in accordance with the pronouncements of the Governmental Accounting Standards Board (GASB). For purposes of presentation, transactions deemed by management to be ongoing, major or central to the provision of health care services are reported as operational revenues and expenses. The financial statement presentation, required by GASB Statements No. 34, 37 and 38 provides a full accrual basis, comprehensive, entity-wide perspective of the District's assets, results of operations and cash flows. The District follows the "business-type activities" reporting requirements of GASB Statement No. 34.

Management's discussion and analysis

GASB Statement 34 requires that financial statements be accompanied by a narrative introduction and analytical overview of the District's financial activities in the form of "management's discussion and analysis" (MD&A). This analysis is similar to the analysis provided in the annual reports of organizations in the private sector.

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 and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents

The District considers cash and cash equivalents to include certain investments in highly liquid debt instruments, when present, with an original maturity of a short-term nature or subject to withdrawal upon request.

1. Organization and Significant Accounting Policies (continued)

Investments

Investments in participating interest-earning investment contracts are recorded at amortized cost, which approximates fair value for these investments, and all other investments are stated at fair value in the statements of net assets based upon published market quotations, where available. Investment income or loss (including realized gains and losses on investments, interest and dividends) and unrealized gains and losses on investments are reported in the statement of revenues, expenses and changes in net assets.

Investments held by the District are included within assets limited as to use as of June 30, 2014.

The District invests in various investment securities including corporate bonds, government securities and US treasury notes. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the accompanying financial statements.

Patient accounts receivable

Patient accounts receivable consist of amounts owed by various governmental agencies, insurance companies and private patients. The District manages its receivables by regularly reviewing the accounts, inquiring with respective payer's as to collectability and providing for allowances on their accounting records for estimated contractual adjustments and uncollectible accounts.

Inventories

Inventories are consistently reported from year to year at cost determined by average costs and replacement values which are not in excess of market. The District does not maintain levels of inventory values such as those under a first-in, first out or last-in, first out method.

Assets limited as to use

Assets limited as to use include amounts designated by the Board of Directors for the replacement or purchases of capital assets, amounts required for future bond obligations and other specific purposes, and amounts held by trustees under specified agreements. See footnote 8 for the composition of assets limited as to use at June 30, 2014.

1. Organization and Significant Accounting Policies (continued)

Capital assets

Capital assets are stated at cost when purchased or constructed, or, for donated property, at the asset's estimated fair value at the time the donated property is received. Depreciation is provided using the straight-line method over the assets' estimated useful lives ranging from 5 to 30 years. Depreciation for tenant improvements is provided using the straight-line method over the shorter of the assets estimated useful life or the lease term. Whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recovered, the District, using its best estimates and projections, reviews for impairment the carrying value of long-lived identifiable assets to be held and used in the future. Any impairment losses identified are recognized when determined. Recoverability of assets is measured by comparison of the carrying amount of the asset to the net undiscounted future cash flows expected to be generated from the asset. If the future undiscounted cash flows are not sufficient to recover the carrying value of the assets, the assets carrying value is adjusted to fair value. As of June 30, 2014, the District has determined that no capital assets are significantly impaired; refer to Footnote 13 Commitments and Contingencies, for discussion of current status of construction in progress.

Depreciation and amortization expense was $4,402,184 for the year ending June 30, 2014.

Bond issue costs

Bond issue costs are comprised of deferred financing cost of the issuance of revenue and general obligation bonds. Amortization of these issuance costs is computed by the straight-line method over the life of the repayment agreements. For current and advance refundings which result in defeasance of debt, the difference between the reacquisition price and the net carrying amount of the old debt, together with any unamortized deferred financing costs, is deferred and amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter, in accordance with GASB 23. Amortization expense was $161,626 for the year ended June 30, 2014.

Compensated absences

The District's employees earn paid-time-off benefits at varying rates depending on years of service; Paid-time-off benefits accumulate up to a specified maximum level. Employees are paid for both accumulated vacation and other accumulated paid time off benefits if they leave either upon termination or before retirement. The accrued paid time off liability as of June 30, 2014 was $1,213,757.

1. Organization and Significant Accounting Policies (continued)

Risk management

The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and medical malpractice. Commercial insurance coverage is purchased for claims arising from such matters. In the case of employee health coverage, the District is self-insured for those claims and is discussed further in the footnotes.

Net position

Net position is comprised of the following three components:

Net investment in capital assets: consists of capital assets (both restricted and unrestricted), net of accumulated depreciation and reduced by the outstanding principal balances of any debt borrowings that were attributable to the acquisition, construction, or improvement of those capital assets.

Restricted net assets: consist of externally designated constraints placed on those net assets by creditors (such as through debt covenants), grantors, contributors, law or regulations of other governments or government agencies, or law or constitutional provisions or enabling legislation.

Unrestricted net assets: consists of net assets that do not meet the definition or criteria of the previous two categories.

Net patient service revenues

Net patient service revenues are reported in the period at the estimated net realized amounts from patients, third-party payors and others including estimated retroactive adjustments under reimbursement agreements with third-party programs. Normal estimation differences between final reimbursement and amounts accrued in previous years are reported as adjustments of current year's net patient service revenues.

Charity care

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

1. Organization and Significant Accounting Policies (continued)

District tax revenues

The District receives approximately 2% of its financial support from property taxes. These funds are used to support operations and meet required debt service agreements. They are classified as non-operating revenue as the revenue is not directly linked to patient care. Property taxes are levied by the County on the District's behalf during the year, and are intended to help finance the District's activities during the same year. Amounts are levied on the basis of the most current property values on record with the County. The County has established certain dates to levy, lien, mail bills, and receive payments from property owners during the year. Property taxes are considered delinquent on the day following each payment due date.

Deferred revenue

The District records property tax revenues received in support of its general obligation bonds to the extent of the current year's debt service associated with these bonds. Property taxes and other funds received on behalf of the general obligation bonds that exceed the current year's debt service payments are recorded as deferred revenue, to be recognized in future years as the debt service payments become due.

Grants and contributions

From time to time, the District receives grants from various governmental agencies and private organizations. The District also receives contributions from related foundation and auxiliary organizations, as well as from individuals and other private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or capital acquisitions. These amounts, when recognized upon meeting all requirements, are reported as components of the statement of revenues, expenses and changes in net position.

Operating revenues and expenses

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

2. Cash - Custodial Credit Risk

As of June 30, 2014, the District had deposits invested in various financial institutions in the form of operating cash and cash equivalents amounting to $10,568,946. All of these funds were held in deposits, which are collateralized in accordance with the California Government Code (CGC), except for $250,000 per account that is federally insured.

Under the provisions of the 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.

3. Investments

Interest rate risk

The District invests in various investment securities including corporate bonds, government securities and US treasury notes, 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.

At June 30, 2014, scheduled maturities of fixed income securities consisted of the following:

Maturing in	
Less than 1 year	$920,848

Credit risk

The District's credit rating risk is governed by Section 53601 of the California Government Code, which, among others, limits investments in money market mutual funds to those funds with the highest ranking by at least one of the national rating agencies and investments in corporate bonds are limited to those with a minimum ranking of A by at least one national rating agencies. The District did not hold any investments at June 30, 2014 that had ratings of less than A by national rating agencies. There are no investment limits on the securities of the U.S. Treasury as these investments are backed by the full faith and credit of the United States government.

3. Investments (continued)

Credit risk (continued)

The following is a summary of the credit quality distribution for securities with credit exposure as rated by Moody's Investor Service at June 30, 2014:

Aaa	$920,848

Concentration of credit risk

The District diversifies its portfolio as required by the California Government Code. At June 30, 2014, more than 5 percent of the District's investments are invested in the following:

Freddie Mac fixed income	21%

4. Net Patient Service Revenues

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

Payments for inpatient acute care services rendered to Medicare program beneficiaries are based on prospectively determined rates, which vary according to the patient diagnostic classification system. Outpatient services are generally paid under an outpatient classification system subject to certain limitations. The District is subject to cost reimbursable services in rural health care services. Filed cost reports are subject to final settlements determined after submission of the annual cost reports and audits thereof by the Medicare fiscal intermediary. At June 30, 2014, cost reports through June 30, 2012 have been final settled.

Medi-Cal

For traditional Medi-Cal (non-Medi-Cal managed care) services, payments for inpatient services rendered to patients are made based on reasonable costs (for discharged patients up until December 31, 2013) while outpatient payments are based on pre-determined charge screens. Effective January 1, 2014, for traditional Medi-Cal patients, the state of California changed to reimbursing based on an APR-DRG methodology, which varies according to a patient diagnostic classification system and is roughly analogous to the payment system for traditional Medicare patients. The District is paid for cost reimbursement services at an interim rate with final settlement determined after submission of annual cost reports and audits thereof by Medi-Cal. At June 30, 2014, cost reports through June 30, 2011, have been final settled. Medi-Cal managed care services are paid on a pre-determined rate and are not subject to cost reimbursement.

4. Net Patient Service Revenues (continued)

Other

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

Net patient service revenues summarized by service are as follows:

Daily hospital services	$ 40,656,736
Inpatient ancillary services	67,092,486
Outpatient services	139,135,921
Gross patient service revenues	246,885,143
Less deductions from revenue	(182,720,735)
Net patient service revenues	$ 64,164,408

Medicare and Medi-Cal revenue accounts for approximately 71% of the District's gross patient revenues. Laws and regulations governing the Medicare and Medi-Cal 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.

5. Patient Accounts Receivable and Concentration of Credit Risk

The District grants credit without collateral to its patients and third-party payors. Patient accounts receivable from government agencies represent the only concentrated group of credit risk for the District and management does not believe that there are any credit risks associated with these governmental agencies. Contracted and other patient accounts receivable consist of various payors including individuals involved in diverse activities, subject to differing economic conditions and do not represent any concentrated credit risks to the District.

Concentrations of patient accounts receivable at June 30, 2014 are as follows:

Medicare	$ 8,010,169
Medi-Cal and Medi-Cal managed care	17,481,274
Other third party payors	7,231,136
Self-pay and other	2,374,565
Gross patient accounts receivable	35,097,144
Less allowances for contractual adjustments and bad debts	(28,063,433)
Net patient accounts receivable	$ 7,033,711

6. Charity Care and Community Benefit Expense

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 District's charity care and community benefit expense for the year ended June 30, 2014, in terms of services to the poor and benefits to the broader community:

Benefits for the poor	
Traditional charity care	$ 960,090
Unpaid Medi-Cal and County indigent program charges	86,545,918
Total quantifiable benefits for the poor	87,506,008
Benefits for the broader community	
Unpaid Medicare program charges	27,887,910
Total quantifiable benefits for the broader community	27,887,910
Total quantifiable community benefits	$115,393,918

7. Other Receivables

Other receivables as of June 30, 2014 were comprised of the following:

Advances to physicians	$1,327,859
Tulare County property taxes	10,000
Net receivable from State disproportionate share and other programs	9,314,259
Grants receivable	169,652
Other receivables	285,020
Less allowance for doubtful accounts	(1,363,289)
	$9,743,501

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.

8. Assets Limited as to Use

Assets limited as to use as of June 30, 2014 were comprised of the following:

Assets held under bond indenture agreements for construction projects	
US Treasury notes	$ 920,848
US government agency securities	250,613
Money Market Funds	6,013
	1,177,474
Assets held under bond indenture agreements	
Money market funds	1,866,152
Cash in County Treasury	9,856,995
Bond rebate receivable	642,455
	12,365,602
Total	13,543,076
Less restricted trust funds available for current debt service	(7,389,395)
Assets limited as to use - long-term	$ 6,153,681

9. Capital Assets

Capital assets as of June 30, 2014 were comprised of the following:

	Balance at June 30, 2013	Transfers / Additions	Reclasses / Retirements	Balance at June 30, 2014
Land and land improvements	$ 3,202,881	$ 234,281	$ (135,291)	$ 3,301,871
Buildings and improvements	43,536,500	-	(482,673)	43,053,827
Equipment	35,222,724	772,256	(4,289,354)	31,705,626
Construction-in-progress	106,803,093	18,589,762	(770,544)	124,622,311
Totals at historical cost	188,765,198	19,596,299	(5,677,862)	202,683,635
Less accumulated depreciation for				
Land improvements	(974,948)	(79,499)	238,114	(816,333)
Buildings and improvements	(26,624,151)	(1,445,062)	960,977	(27,108,236)
Equipment	(27,472,162)	(2,715,997)	4,182,616	(26,005,543)
Total accumulated depreciation	(55,071,261)	(4,240,558)	5,381,707	(53,930,112)
Capital assets, net	$133,693,937	$15,355,741	$ (296,155)	$148,753,523

10. Debt Borrowings

As of June 30, 2014 debt borrowings were as follows:

General obligation bonds, election of 2005, series A (2007); interest at 4.00% to 4.65% due semiannually; principal due in annual amounts ranging from $15,000 on August 1, 2012 to $2,000,000 due on August 1, 2037; collateralized by tax revenues.	$ 14,955,000
Series 2007 refunding revenue bonds; interest at 3.75% to 5.20% due semiannually; principal due in annual amounts ranging from $405,000 due on November 1, 2008 to $1,210,000 due on November 1, 2032; collateralized by District revenues.	15,230,000
General obligation bonds, election of 2005, series B (2009); interest at 6.45% to 8.00% due semiannually; principal due in annual amounts ranging from $100,000 on August 1, 2014 to $7,240,000 due on August 1, 2039; collateralized by tax revenues.	70,000,000
Note payable to a financial institution; interest at 1.913%; principal and interest payments of $104,938 Payable monthly through December, 2016; collateralized by equipment.	3,071,667
Equipment lease: Note payable to a financial Institution; interest at 2.94%; principle and interest payments of $17,459 payable monthly through July 2017; collateralized by equipment.	597,899
Total debt borrowings	103,854,566
Less current maturities of debt borrowings	(2,036,139)
	$101,818,427

10. Debt Borrowings (continued)

Future interest due and principal maturities of debt borrowings, at June 30, 2014 are as follows:

	Interest	Principal	Total
2015	$ 5,229,928	$ 2,036,139	$ 7,266,067
2016	5,168,010	2,244,178	7,412,188
2017	5,100,339	1,796,832	6,897,171
2018	5,045,742	1,152,417	6,198,159
2019	4,991,341	1,305,000	6,296,341
2020 - 2024	23,759,124	9,710,000	33,469,124
2025 - 2029	19,907,834	16,910,000	36,817,834
2030- 2034	14,793,812	26,760,000	41,553,812
2035 - 2039	6,496,250	34,700,000	41,196,250
2040	188,240	7,240,000	7,428,240
	$90,680,620	$103,854,566	$194,535,186

The Series 2007 refunding revenue bonds require that the District maintain a long-term debt service coverage ratio of not less than 1.25 times, or 1.10 times if the District maintains 50 days or greater cash on hand. For the year ended June 30, 2014, the District did meet the debt service coverage ratio requirement.

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%.

In February 2014, Fitch Ratings downgraded the $15.2 million refunding revenue bonds, series 2007 to "B" from a "B+" and placed the bonds on Rating Watch Negative. In August 2014, as noted in the Subsequent Events footnote #19 below, Fitch affirmed the "B" rating, removed the Rating Watch Negative, and improved the Outlook to "Stable." Fitch noted: "the positive trend indicates performance improvement plans taking hold and signal recovery."

11. Employees' Retirement Plans

The "Tulare Local Hospital District Money Purchase Pension Plan" (the Retirement Plan) is a defined contribution money purchase pension plan established by the District to provide retirement benefits for substantially all District employees. The annual contribution to the Retirement Plan by the District is determined based on a percentage of the compensation paid to eligible employees and varies for each participant based on their respective years of employment at the District. In order to be eligible to participate, the District has required that employees agree to contribute to a deferred compensation arrangement. Total amounts contributed by the District to the Retirement Plan for the year ended June 30, 2014 was approximately $498,000. The required employee contributions have been treated as contributed under a deferred compensation arrangement under the Internal Revenue Code Section 457.

11. Employees' Retirement Plans (continued)

The District has also established the "Tulare Local Hospital District Social Security Alternative Savings Plan" (the SSA Plan) to provide retirement benefits to employees as an alternate method of pension and other benefit opportunities similar to those provided by Social Security. The SSA Plan is available to all employees of the District who would otherwise have been covered by Social Security. The District and employee level of contributions to the SSA Plan depend on the employees' most recent date of employment and differentiate between those employed prior to 1987 and later years, based on certain regulations.

Originally, the employee contributions to the SSA Plan were treated as contributions to a deferred compensation arrangement under the Internal Revenue Code Section 457. Effective January 1, 1987, the employee contributions have been treated as "pick-up" contributions under the Internal Revenue Code Section 414(h)(2). The District's contribution to the SSA Plan for the year ended June 30, 2014 was approximately $782,000.

12. Post -Retirement Benefits

In years past, the District's SSA Plan provided for post-retirement health care benefits for employees who retire on or after age 55 and prior to July 31, 1998, with at least five years of service at the District. Under this program, the District reimburses eligible health care expenses for the retirees. Health care benefits are provided until the retiree is eligible for the Medicare program.

The District was also required to purchase Part A coverage under the Medicare Program for those eligible retirees who were hired between January 1, 1983 and April 1, 1986. During that period, and under the conditions of the SSA Plan, the District was not required to withhold social security payroll taxes from its employees in order to fund their respective Medicare future benefit. Regulations changed effective April 1, 1986, which required the funding to commence again for any new hire after the effective date. As a result of this "three-year" period, the SSA Plan requires the District provide Part A coverage for these employees upon acceptance into the Medicare Program. The District is not required to purchase Part A coverage if the retiree is eligible for the Medicare Program either through credits gained before January 1, 1983, employment credits at another place of employment, or eligibility through the retiree's current or former spouse.

The District has "board-designated" funds to meet these obligations. At June 30, 2014, the board funded post-retirement health care benefit liability, as determined by actuarial studies, was approximately $66,000. The discount rate used in determining the accumulated post-retirement health care benefit cost was 7% for each year. The assumed health care cost trend rate was 7.5% in 1998, grading down to 5% in 2003 and beyond. The District has amended its benefit plans to redesign future benefits to exclude post-retirement obligations.

13. Commitments and Contingencies

Construction-in-progress

As of June 30, 2014, the District had recorded $124,622,311 as construction-in-progress representing cost capitalized of $121,693,142 for the "Tower Project" and $2,896,285 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 $4,960,000 for the year ending June 30, 2014. Estimated costs to complete all projects as of June 30, 2014 are approximately $35 million, of which $15.7 million pertains to the contract with the general contractor.

As to the ongoing construction of the four-story, 115,000 square foot "Tower Project" specifically, the District entered into a construction contract around March, 2010 and construction began around May, 2010. The original completion date was December, 2012, however due to delays caused by several setbacks (as more fully described in footnote 14), the new completion date is now projected for approximately 14-16 months after additional financing is secured.

At June 30, 2014, there was approximately $1.2 million remaining in the bond project fund. As of the date of this report, the District's Board of Directors is actively reviewing various options related to securing financing to complete the "Tower Project". Management believes they will successfully obtain the necessary financing to complete the project.

Operating leases

The District leases various equipment and facilities under operating leases expiring at various dates. Total building and equipment rent expense for the year ended June 30, 2014 was $802,268. Approximate future minimum lease payments for the succeeding years under operating leases as of June 30, 2014, which have initial or remaining lease terms in excess of one year are as follows:

Year Ending June 30,	Operating Leases
2015	$ 624,000
2016	519,000
2017	489,000
2018	84,000
2019	66,000
Total minimum lease payments	$1,783,000

13. Commitments and Contingencies (continued)

Employee health insurance

The District provides health benefits to employees through a self-funded plan financed by the District operations. Estimated liabilities are recorded for claims which most likely have been incurred but are not yet reported for claims processing and payment (IBNR). As of June 30, 2014, the IBNR was estimated at $889,656. Commercial insurance is provided for "stop-loss" coverage for significant claims.

Workers compensation program

The District is a participant in the Association of California Hospital Districts Alpha Fund (the Fund) which administers a self-insured worker's compensation plan for participating hospital employees of its member hospitals. The District pays premiums to the Fund which are adjusted annually. If participation in the Fund is terminated by the District, the District would be liable for its share of any additional premiums necessary for final disposition of all claims and losses covered by the Fund.

Health Care Reform

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, and government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the District is in compliance with fraud and abuse as well as other applicable government laws and regulations. While no material regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

14. Litigation

Construction delays

Around March, 2010, the District entered into a construction contract with Harris Construction Co., Inc. (Harris) for the construction of the "Tower Project" (the Project). Construction began around May, 2010 and is presently ongoing. The initial completion date was approximately December, 2012. In early 2012, the District was informed by Harris that there were issues involving delaminated concrete within the Project that required remediation efforts. Although the issue was resolved, it caused delays in the completion of the Project. Presently, the Project completion date as required by the Project is now projected for approximately 14-16 months after additional financing is secured. and due to the failure of Harris to achieve Project completion by that date, as required by the contract, the District had elected to assess liquidated damages (at the contractual rate of $10,000 per day) until completion is achieved, but is not withholding those liquidated damages from monthly progress billings.

It was the position of the District that Harris remained 100% responsible for the concrete issue which has caused substantial delay to the Project. Harris advised the District that it believes 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 District disputed many of these claims.

On January 9, 2014, Harris filed a complaint with the Fresno Superior Court which was served on the District on March 12, 2014. The complaint contained various allegations and the matter was settled July 25, 2014. The terms of the settlement included consideration given by both parties. Specific terms included the District paying Harris approximately $7.9 million over a 48 month period. The 48 months began August 1, 2014 and incorporated a $33,750 payment each month to Harris. The settlement also required Harris to disengage from the project and dismiss all litigation against the District.

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, 2014 will be resolved without material adverse effect on the District's future financial position, results from operations or cash flows.

15. Related Party Transactions

The Tulare Hospital Foundation (the Foundation), has been established as a nonprofit public benefit corporation under the Internal Revenue Code Section 501(c)(3) to solicit contributions on behalf of the District. Substantially all funds raised except for funds required for operation of the Foundation, are distributed to the District or held for the benefit of the District. The Foundation's funds, which represent the Foundation's unrestricted resources, are distributed to the District in amounts and in periods determined by the Foundation's Board of Trustees, who may also restrict the use of funds for District property and equipment replacement or expansion or other specific purposes. The Foundation, as specified in their mission statement, contributes annually, both in service and in funding, towards the healthcare of the residents of the Tulare healthcare service area, including the District. The Tulare District Hospital Auxiliary (the Auxiliary) is a similar non-profit organization established to help solicit contributions for the District and also donates funds towards the healthcare effort of the Tulare area, including the District.

16. Uncertainties

In previous financial statements over the last several years, the Corporate Integrity Agreement has been referenced. On October 24, 2014 the Office of Inspector General (OIG) of the Department of Health and Human Services officially notified the District that it successfully completed the five year term of the Corporate Integrity Agreement. This was originally entered into in 2009 and has now been formally lifted.

Generally accepted accounting principles require that loss contingencies be properly disclosed and reflected in the financial statements, however, it is not possible to disclose what outcome, if any, the aforementioned "uncertainties" may have on the financial position of the District as of June 30, 2014.

For the year ended June 30, 2014, management does not believe that there is any material impact on the financial position of the District as a result of the aforementioned "uncertainties".

17. Management Services Agreement

In January 2014 the District retained the services of HealthCare 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. The agreement includes the obligation for HCCA to recruit and provide senior leadership to the District

18. Continued Hospital Operations

The District suffered operating losses from hospital operations through March 2014. Beginning in April 2014, however, financial results began to turn around. This was due to the District retaining the services of HCCA in January 2014 to manage hospital operations. Beginning in April 2014 and through the most recently published internal financial statements in September 2014, the hospital has generated profits from hospital operations. HCCA brought in the services of nationally recognized experts in hospital turnarounds to guide the financial and operational improvement process. Those experts developed and implemented operational improvement plans which have had a significant positive financial impact as compared to prior year results. The District anticipates the positive financial trends will continue under HCCA leadership.

19. Subsequent Events

The District has evaluated subsequent events through November 24, 2014, the date the financial statements were available to be issued.

Harris Settlement

On July 25, 2014, the District entered into a Settlement Agreement with Harris Construction, the former Construction Contractor. The terms of the settlement included consideration given by both parties. Specific terms included the District paying Harris approximately $7.9 million over a 48 month period. The 48 months began August 1, 2014 and incorporated a $33,750 payment each month to Harris. The settlement also required Harris to disengage from the project and dismiss all litigation against the District.

District Employee Transition to HCCA

On November 9, 2014, all District employees transitioned to HCCA employment. Going forward the District will essentially lease the employees from HCCA. Transitioning to a private employer is anticipated to provide an enhanced level of professionalism, efficiency, and overall improved labor productivity for these employees.

Fitch Ratings Letter/Press Release on August 28, 2014

On this date, Fitch Ratings affirmed the 'B' rating on the District's $15.2 million series 2007 bonds, removed the Rating Watch Negative, and improved the Rating Outlook to Stable. Fitch noted the removal from Rating Watch Negative reflects growing clarity and progress on construction plans achieved over the last six months. Fitch noted that a settlement was reached with the previous contractor in July 2014, a new team has been put in place under HCCA leadership, and a completion plan has been established. Fitch also noted the Stable Outlook reflects the dramatic turnaround in operating and financial performance since Fitch's last review in February 2014. Fitch indicated that the positive trend over the last few months indicate performance improvement plans taking hold and signal recovery.

19. Subsequent Events (continued)

Fitch Ratings Letter/Press Release on August 28, 2014 (continued)

No subsequent events, other than the events disclosed above, have occurred that would have a material impact on the presentation of the District's financial statements.