Hi-Desert Memorial Health Care District
doing business as
Hi-Desert Medical Center

Basic Financial Statements and
Independent Auditors' Reports

June 30, 2015 and 2014

DINGUS | ZARECOR & ASSOCIATES PLLC
Certified Public Accountants

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
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DINGUS | ZARECOR & ASSOCIATES PLLC
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

Board of Directors
Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Joshua Tree, California

Report on the Financial Statements

We have audited the accompanying financial statements of Hi-Desert Memorial Health Care District doing business as Hi-Desert Medical Center (the District) as of and for the years ended June 30, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and the California Controller's minimum audit requirements for California special districts. 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 auditors' 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 auditors consider 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.

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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, 2015 and 2014, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America as well as accounting systems prescribed by the State Controller's Office and state regulations governing special districts.

Other Matters

Required Supplementary Information

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 4, 2015, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters for the year ended June 30, 2015. We issued a similar report for the year ended June 30, 2014, dated December 2, 2014, which has not been included with the 2015 financial and compliance report. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing for each year, and not to provide an opinion on internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Dingus, Zarecor & Associates PLLC

Spokane Valley, Washington
November 4, 2015

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Statements of Net Position
June 30, 2015 and 2014

ASSETS AND DEFERRED OUTFLOW OF RESOURCES	2015	2014
Current assets		
Cash and cash equivalents	**$ 3,472,578**	$ 1,551,585
Investments	**1,429,033**	14,255,815
Receivables:		
Patients, less allowances for uncollectible accounts of approximately $2,077,000 and $3,688,000, respectively	**7,890,311**	9,382,401
Grants	**134,140**	413,028
340b contract pharmacies	**140,322**	298,269
Taxes	**6,803**	9,737
Estimated third-party payor settlements	**149,259**	-
Other	**262,265**	287,024
Inventories	**1,337,048**	1,174,472
Prepaid expenses	**492,940**	752,317
Total current assets	**15,314,699**	28,124,648
Noncurrent assets		
Capital assets, net	**17,002,320**	18,273,712
Total assets	**32,317,019**	46,398,360
Deferred outflow of resources		
Deferred loss on bond refunding	**-**	216,171
Prepaid water treatment capacity fee	**895,326**	969,936
Total deferred outflow of resources	**895,326**	1,186,107
Total assets and deferred outflow of resources	**$ 33,212,345**	$ 47,584,467

See accompanying notes to basic financial statements.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Statements of Net Position (Continued)
June 30, 2015 and 2014

LIABILITIES AND NET POSITION	2015	2014
Current liabilities		
Accounts payable	**$ 2,795,855**	$ 4,012,629
Electronic health records incentive payments payable	**-**	754,458
Patient refunds payable	**1,617,286**	1,594,950
Accrued payroll and related liabilities	**1,561,943**	1,390,593
Accrued paid time off	**561,451**	1,425,722
Estimated third-party payor settlements	**114,745**	571,810
Current portion of long-term debt	**112,659**	1,329,666
Total current liabilities	**6,763,939**	11,079,828
Noncurrent liabilities		
Long-term debt, net of current portion	**820,715**	4,883,595
Total liabilities	**7,584,654**	15,963,423
Net position		
Net investment in capital assets	**16,964,271**	13,241,324
Restricted by donors for specific operating purposes	**131,772**	146,838
Unrestricted	**8,531,648**	18,232,882
Total net position	**25,627,691**	31,621,044
Total liabilities and net position	**$ 33,212,345**	$ 47,584,467

See accompanying notes to basic financial statements.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Statements of Revenues, Expenses, and Changes in Net Position
Years Ended June 30, 2015 and 2014

	2015	2014
Operating revenues		
Net patient service revenue, net of provision for bad debts of $1,765,486 and $6,029,505, respectively	**$ 61,495,512**	$ 58,002,901
Electronic health record incentive payments	**-**	132,458
Grant	**2,500,868**	1,765,967
Other	**274,380**	179,917
Total operating revenues	**64,270,760**	60,081,243
Operating expenses		
Salaries and wages	**30,073,856**	30,116,054
Employee benefits	**7,352,336**	7,402,991
Contract labor	**2,038,316**	1,385,258
Professional fees	**5,915,779**	4,884,735
Purchased services	**6,408,299**	4,819,583
Supplies	**8,323,970**	7,918,890
Insurance	**478,884**	500,317
Leases and rentals	**569,076**	520,782
Depreciation and amortization	**3,146,425**	3,179,898
Repairs and maintenance	**2,637,148**	2,192,932
Utilities	**1,767,510**	1,496,185
Other	**1,248,809**	989,937
Total operating expenses	**69,960,408**	65,407,562
Operating loss	**(5,689,648)**	(5,326,319)
Nonoperating revenues (expenses)		
Tax revenue	**598,376**	585,547
Investment income	**41,040**	480,967
Rental income	**73,186**	80,581
Interest expense	**(387,632)**	(262,254)
Loss on disposal of capital assets	**(597,483)**	(74,434)
Contributions	**12,945**	18,280
Investment fees	**(44,137)**	(72,984)
Total nonoperating revenues (expenses), net	**(303,705)**	755,703
Change in net position	**(5,993,353)**	(4,570,616)
Net position, beginning of year	**31,621,044**	36,191,660
Net position, end of year	**$ 25,627,691**	$ 31,621,044

See accompanying notes to basic financial statements.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Statements of Cash Flows
Years Ended June 30, 2015 and 2014

	2015	2014
Increase (Decrease) in Cash and Cash Equivalents		
Cash flows from operating activities		
Cash received from and on behalf of patients	**$ 62,561,561**	$ 58,618,360
Cash received (paid) for electronic health records incentive payments	**(754,458)**	886,916
Cash received from grants	**2,779,756**	1,371,279
Cash received from other revenue	**299,139**	336,722
Cash paid to and on behalf of employees	**(38,119,113)**	(37,349,872)
Cash paid to suppliers and contractors	**(30,433,154)**	(23,291,625)
Net cash provided by (used in) operating activities	**(3,666,269)**	571,780
Cash flows from noncapital financing activities		
Cash received from contributions	**12,945**	18,280
Taxes received	**601,310**	581,175
Principal payments on long-term debt	**(74,611)**	(74,610)
Net cash provided by noncapital financing activities	**539,644**	524,845
Cash flows from capital and related financing activities		
Purchase of capital assets	**(2,472,516)**	(3,092,833)
Principal payments on long-term debt	**(5,205,276)**	(1,223,978)
Interest paid	**(171,461)**	(147,367)
Net cash used in capital and related financing activities	**(7,849,253)**	(4,464,178)
Cash flows from investing activities		
Purchase of investments	**(4,380,656)**	(6,666,136)
Proceeds from sale of investments	**17,242,785**	9,934,480
Interest received	**5,693**	306,931
Investment fees	**(44,137)**	(72,984)
Rental income	**73,186**	80,581
Net cash provided by investing activities	**12,896,871**	3,582,872
Net increase in cash and cash equivalents	**1,920,993**	215,319
Cash and cash equivalents, beginning of year	**1,551,585**	1,336,266
Cash and cash equivalents, end of year	**$ 3,472,578**	$ 1,551,585

See accompanying notes to basic financial statements.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Statements of Cash Flows (Continued)
Years Ended June 30, 2015 and 2014

	2015	2014
Reconciliation of Operating Loss to Net Cash Provided by (Used in) Operating Activities		
Operating loss	**$ (5,689,648)**	$ (5,326,319)
Adjustments to reconcile operating loss to net cash provided by (used in) operating activities		
Depreciation and amortization	**3,146,425**	3,179,898
Provision for bad debts	**1,765,486**	6,029,505
Decrease (increase) in assets:		
Receivables:		
Patient accounts, net	**(273,396)**	(6,329,024)
Grants	**278,888**	(394,688)
340b contract pharmacies	**157,947**	(298,269)
Estimated third-party payor settlements	**(149,259)**	-
Other	**24,759**	156,805
Inventories	**(162,576)**	(56,299)
Prepaid expenses	**259,377**	(19,862)
Prepaid water treatment capacity fee	**74,610**	74,610
Increase (decrease) in liabilities:		
Accounts payable	**(1,216,774)**	1,418,545
Electronic health records incentive payments payable	**(754,458)**	754,458
Patient refunds payable	**22,336**	879,182
Accrued payroll and related liabilities	**171,350**	58,881
Accrued paid time off	**(864,271)**	110,292
Estimated third-party payor settlements	**(457,065)**	334,065
Net cash provided by (used in) operating activities	**$ (3,666,269)**	$ 571,780

See accompanying notes to basic financial statements.

1. Reporting Entity and Summary of Significant Accounting Policies:

a. Reporting Entity

Hi-Desert Memorial Health Care District doing business as Hi-Desert Medical Center (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 under Section 115 of the Internal Revenue Code. The District is governed by a five-member Board of Directors, elected from within the district to specified terms of office. The District owns and operates a 59-bed acute care hospital and a 120-bed long-term care facility, both of which are located in Joshua Tree, California. In conjunction with the healthcare facilities, they also operate a home health agency, federally-qualified health centers, and other patient services. The District provides healthcare services primarily to individuals who reside in the local area.

The Hi-Desert Memorial Health Care District Foundation (the Foundation) was formed by the District. The Foundation is a California nonprofit public benefit corporation organized to solicit funds and help promote healthcare services within the district boundaries. The District is the sole corporate member of the Foundation and has the right to appoint all members of the Foundation's Board of Directors. The Foundation's operations are not significant to the District and have not been included in the District's financial statements.

The District entered into a purchase agreement and a lease with HDMC Holdings, LLC (HDMC Holdings) effective July 15, 2015.

The purchase agreement transfers prepaid assets, inventory, personal property (equipment and supplies both capitalized and previously expensed), leases, contracts, licenses and records to HDMC Holdings. The District retained the assets related to the federally-qualified health clinics, Foundation assets, cash and short-term investments, patient accounts receivable, other receivables, cost report settlements, real property, and all liabilities (whether known or unknown) such as accounts payable, accrued payroll, debt, pension and other retirement plans, and cost report settlements. HDMC Holdings obtained malpractice tail coverage for the District. The sales price equals the book value of the prepaid assets and inventory and 50 percent of the vested accrued paid time off. The sales price was estimated as $2,000,000.

The lease agreement leases all real property and permanently affixed equipment except for the federally-qualified health clinics and Foundation real property. The annual rent is $2,000,000 with a 30-year term through July 2045. Additional lease payments could be due after four years subject to QAF funding levels. HDMC Holdings has committed to certain capital improvements, physician recruitment, service expansion, and clinical services to be offered subject to quality issue exceptions within the first 10 years and then also to financial and strategic exceptions after 10 years. The lease contains a purchase option for HDMC Holdings to purchase the real property at fair market value at lease termination.

b. Summary of Significant Accounting Policies

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 the disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

1. Reporting Entity and Summary of Significant Accounting Policies (continued):

b. Summary of Significant Accounting Policies (continued)

Enterprise fund accounting – The District's accounting policies conform to accounting principles generally accepted in the United States of America as applicable to proprietary funds of governments. The District uses enterprise fund accounting. Revenue and expenses are recognized on the accrual basis using the economic resources measurement focus.

Cash and cash equivalents – Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less.

Investments and investment income – Investments are recorded at fair value. Fair value is determined using quoted market prices. Investment income includes dividend and interest income and gains and losses on fair value of investments.

Deferred loss on bond refunding – The deferred loss on bond refunding is being amortized over the term of the refunding debt using the effective interest method. The refunding debt was paid off during fiscal year 2015.

Inventories – Inventories consist of medical supplies, drugs, and food and are stated at cost using the first-in, first-out method.

Compensated absences – The District's employees earn paid time off (PTO) for vacation, holidays, and short-term illnesses based upon years of service. The related liability is accrued during the period in which it is earned and will be paid to an employee upon either termination or retirement.

Net position – Net position of the District is classified into three components. *Net investment in capital assets* consists of capital assets net of accumulated depreciation and reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted net position* is noncapital net position that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the District. *Unrestricted net position* is the remaining net position that does not meet the definition of *net investment in capital assets* or *restricted*.

Operating revenues and expenses – The District's statements of revenues, expenses, and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues result from exchange transactions, including grants for specific operating activities associated with providing healthcare services — the District's principal activity. Nonexchange revenues, including taxes and contributions received for purposes other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide healthcare services, other than financing costs.

Restricted resources – When the District has both restricted and unrestricted resources available to finance a particular program, it is the District's policy to use restricted resources before unrestricted resources.

1. Reporting Entity and Summary of Significant Accounting Policies (continued):

b. Summary of Significant Accounting Policies (continued)

Grants and contributions – From time to time, the District receives grants from the state of California and others as well as contributions from individuals and private organizations. Revenues from grants and contributions (including contributions of capital assets) are recognized when all eligibility requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are restricted to specific capital acquisitions are reported after nonoperating revenues and expenses. Grants that are for specific projects or purposes related to the District's operating activities are reported as operating revenue. Grants that are used to subsidize operating deficits are reported as nonoperating revenue. Contributions, except for capital contributions, are reported as nonoperating revenue.

Subsequent events – The District has evaluated subsequent events through November 4, 2015, the date on which the financial statements were available to be issued.

2. Bank Deposits:

The District had bank deposits consisting of cash and cash equivalents in various financial institutions, which are collateralized in accordance with the California Government Code (CGC), except for $250,000 per account that is federally insured.

The CGC and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial risk for deposits. Custodial risk for deposits is the risk that, in the event of the failure of a depository financial institution, the District would not be able to recover its deposits or would not be able to recover collateral securities that are in possession of an outside party.

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 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:

The District's investment balances and maturities were as follows:

	2015			
		Investment Maturities (in Years)		
	Fair Value	Less than One	One to Five	Over Five
Cash and money market accounts	**$ 795,627**	$ 795,627	$ -	$ -
U.S. Treasury obligations	**381,778**	-	381,778	-
U.S. Agency obligations	**251,628**	251,628	-	-
Total investments	**$ 1,429,033**	$ 1,047,255	$ 381,778	$ -

	2014			
		Investment Maturities (in Years)		
	Fair Value	Less than One	One to Five	Over Five
Cash and money market accounts	**$ 332,235**	$ 332,235	$ -	$ -
Certificates of deposit	**203,748**	-	104,443	99,305
Municipal bonds	**152,903**	-	-	152,903
Corporate bonds and notes	**3,486,152**	237,309	2,753,013	495,830
U.S. Treasury obligations	**3,264,268**	1,098,914	1,471,222	694,132
U.S. Agency obligations	**4,660,031**	-	4,660,031	-
Mortgage backed securities	**1,976,803**	-	945,483	1,031,320
Equities	**179,675**	179,675	-	-
Total investments	**$ 14,255,815**	$ 1,848,133	$ 9,934,192	$ 2,473,490

The District's investment policy allows for various forms of investments generally set to mature within a few months to 10 years. The policy identifies certain provisions which address interest rate risk, credit risk, and concentration of credit risk.

Interest rate risk – Interest rate risk is the risk that changes in market interest 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. One of the ways the District manages its exposure to interest rate risk is by purchasing a combination of shorter-term and longer-term investments and by timing cash flows from maturities so that a position of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations. Information about the sensitivity of the fair values of the District's investments to market interest rate fluctuations is provided by the preceding schedules that show the distribution of the District's investments by maturity.

Credit risk – Credit risk is the risk that the issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization, such as Moody's Investor Service, Inc., or Standard and Poor's. The District's investment policy for corporate bonds and notes is to invest in companies with total assets in excess of $500 million and having an "A" or higher rating by rating agencies.

Custodial credit risk – Custodial credit risk is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer), the District will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The District's investments are generally held by broker-dealers or banks' trust departments used by the District to purchase securities.

3. Investments (continued):

Concentration of credit risk – Concentration of credit risk is the risk of loss attributed to the magnitude of the District's investment in a single issuer. The District's investment allows concentrations of over 5% in government backed securities.

Foreign currency risk – Foreign currency risk relates to adverse effects on the fair value of an investment from changes in exchange rates involving currencies outside the United States. The District has no investments in foreign currencies as it is not allowed within their investment policy.

4. Patient Accounts Receivable:

Patient accounts receivable are reduced by an allowance for uncollectible accounts. In evaluating the collectibility of accounts receivable, the District analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for uncollectible accounts and provision for bad debts. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for uncollectible accounts. For receivables associated with services provided to patients who have third-party coverage, the District analyzes contractually due amounts and provides an allowance for uncollectible accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). For receivables associated with self-pay patients (which include both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the District records a significant provision for bad debts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for uncollectible accounts.

4. Patient Accounts Receivable (continued):

The District's allowance for uncollectible accounts for self-pay patients decreased 44% as of June 30, 2015, as compared to June 30, 2014, due to increased collection efforts on self-pay accounts, as well as decrease in uninsured patients primarily due to the Affordable Care Act and the State of California's Medicaid expansion. The District does not maintain a material allowance for uncollectible accounts from third-party payors, nor did it have significant writeoffs from third-party payors.

Patient accounts receivable reported as current assets consisted of these amounts:

	2015	2014
Receivables from patients and their insurance carriers	**$ 1,394,407**	$ 3,938,214
Receivables from Medicare	**3,116,003**	2,711,714
Receivables from Medicaid	**5,457,071**	6,420,540
Total patient accounts receivable	**9,967,481**	13,070,468
Less allowance for uncollectible accounts	**(2,077,170)**	(3,688,067)
Patient accounts receivable, net	**$ 7,890,311**	**$** 9,382,401

5. Capital Assets:

The District capitalizes assets whose costs exceed $2,500 and with an estimated useful life of more than two years; lesser amounts are expensed. Capital assets are stated at cost or estimated fair value at the date of donation. Expenditures for maintenance and repairs are charged to operations as incurred; betterments and major renewals are capitalized. When such assets are disposed of, the related costs and accumulated depreciation or amortization are removed from the accounts and the resulting gain or loss is classified in nonoperating revenues or expenses.

All capital assets, other than land and construction in progress, are depreciated or amortized (in the case of capital leases), using the straight-line method over the shorter period of the lease term or the estimated useful life of the capital assets. Such amortization is included in the depreciation and amortization in the basic financial statements. Useful lives have been estimated as follows:

Land improvements	10 to 25 years
Buildings and improvements	2 to 35 years
Equipment	2 to 20 years

5. Capital Assets (continued):

Capital asset additions, retirements, transfers, and balances were as follows:

	Balance June 30, 2014	Additions	Retirements	Transfers	Balance June 30, 2015
Capital assets not being depreciated					
Land	$ 1,073,183	$ -	$ -	$ -	**$ 1,073,183**
Construction in progress	3,038,523	701,927	(633,703)	(2,210,182)	**896,565**
Total capital assets not being depreciated	4,111,706	701,927	(633,703)	(2,210,182)	**1,969,748**
Capital assets being depreciated					
Land improvements	4,416,066	-	(85,446)	-	**4,330,620**
Buildings and improvements	30,963,675	231,131	(149,035)	1,018,773	**32,064,544**
Equipment	30,285,685	1,590,300	(2,711,287)	1,191,409	**30,356,107**
Total capital assets being depreciated	65,665,426	1,821,431	(2,945,768)	2,210,182	**66,751,271**
Less accumulated depreciation and amortization for					
Land improvements	(1,328,271)	(226,218)	85,445	-	**(1,469,044)**
Buildings and improvements	(24,948,985)	(756,099)	149,065	-	**(25,556,019)**
Equipment	(25,226,164)	(2,164,108)	2,696,636	-	**(24,693,636)**
Total accumulated depreciation and amortization	(51,503,420)	(3,146,425)	2,931,146	-	**(51,718,699)**
Total capital assets being depreciated, net	14,162,006	(1,324,994)	(14,622)	2,210,182	**15,032,572**
Capital assets, net	**$ 18,273,712**	**$ (623,067)**	**$ (648,325)**	**$ -**	**$ 17,002,320**

5. Capital Assets (continued):

	Balance June 30, 2013	Additions	Retirements	Transfers	Balance June 30, 2014
Capital assets not being depreciated					
Land	$ 1,073,183	$ -	$ -	$ -	**$ 1,073,183**
Construction in progress	4,533,324	1,658,292	-	(3,153,093)	**3,038,523**
Total capital assets not being depreciated	5,606,507	1,658,292	-	(3,153,093)	**4,111,706**
Capital assets being depreciated					
Land improvements	1,624,264	-	(133,720)	2,925,522	**4,416,066**
Buildings and improvements	30,706,532	283,826	(26,683)	-	**30,963,675**
Equipment	30,609,802	1,151,087	(1,702,775)	227,571	**30,285,685**
Total capital assets being depreciated	62,940,598	1,434,913	(1,863,178)	3,153,093	**65,665,426**
Less accumulated depreciation and amortization for					
Land improvements	(1,195,484)	(205,048)	72,261	-	**(1,328,271)**
Buildings and improvements	(24,340,826)	(751,909)	143,750	-	**(24,948,985)**
Equipment	(24,575,584)	(2,222,941)	1,572,361	-	**(25,226,164)**
Total accumulated depreciation and amortization	(50,111,894)	(3,179,898)	1,788,372	-	**(51,503,420)**
Total capital assets being depreciated, net	12,828,704	(1,744,985)	(74,806)	3,153,093	**14,162,006**
Capital assets, net	**$ 18,435,211**	**$ (86,693)**	**$ (74,806)**	**$ -**	**$ 18,273,712**

At June 30, 2015, construction in progress consisted of various projects whose completion dates and estimated costs to complete will be re-evaluated after the lease of hospital operations, as discussed in Note 1.

6. Prepaid Water Treatment Capacity Fee:

The District constructed and capitalized a water treatment plant. The District retains ownership of the water treatment plant. Joshua Basin Water District (JBWD) operates the water treatment plant. In 2014, the District entered into a note payable with JBWD for a capacity fee of $1,119,156. The capacity fee note payable will be repaid annually at $74,610 for 15 years. A deferred outflow of resources and a note payable were recorded. The prepaid water treatment capacity fee is amortized to utilities expense over the 15-year term.

7. Long-term debt:

A schedule of changes in the District's long-term debt and capital lease obligation is as follows:

	Balance June 30, 2014	Additions	Reductions	Balance June 30, 2015	Amounts Due Within One Year
Long-term debt					
Banc of America Public Capital Corp master equipment lease/purchase agreement	$ 5,169,169	$ -	$ (5,169,169)	$ -	**$ -**
Note payable to Joshua Basin Water District	969,936	-	(74,611)	895,325	**74,610**
Olympus capital lease obligation	74,156	-	(36,107)	38,049	**38,049**
Total long-term debt	$ 6,213,261	$ -	$ (5,279,887)	$ 933,374	**$ 112,659**

	Balance June 30, 2013	Additions	Reductions	Balance June 30, 2014	Amounts Due Within One Year
Bonds and notes payable					
Banc of America Public Capital Corp master equipment lease/purchase agreement	$ 6,358,883	$ -	$ (1,189,714)	$ 5,169,169	**$ 1,218,949**
Note payable to Joshua Basin Water District	1,044,546	-	(74,610)	969,936	**74,610**
Olympus capital lease obligation	108,420	-	(34,264)	74,156	**36,107**
Total bonds and notes payable	7,511,849	$ -	$ (1,298,588)	$ 6,213,261	**$ 1,329,666**

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

- Banc of America Public Capital Corporation master equipment lease/purchase agreement in the original amount of $8,560,000; interest at 2.43%. The District paid off the outstanding balance in 2015.
- Note payable to Joshua Basin Water District in the original amount of $1,119,156, due in annual installments of $74,610 plus variable interest at the California Local Agency Investment Fund Quarterly rate (0.28% at June 30, 2015) through July 2026 for prepaid water treatment capacity fee.
- Olympus capital lease obligation in the original amount of $108,420, principal and interest at 5.25% due in monthly installments of $3,262 through June 2016; collateralized by equipment.

7. Long-term Debt (continued):

Aggregate annual principal and interest payments over the terms of long-term debt are as follows:

Years Ending June 30,	Principal	Interest	Total
2016	$ 112,659	$ 3,061	$ 115,720
2017	74,610	2,298	76,908
2018	74,610	2,089	76,699
2019	74,610	1,880	76,490
2020	74,610	1,671	76,281
2021-2025	373,052	5,223	378,275
2026-2027	149,223	627	149,850
	$ 933,374	**$ 16,849**	**$ 950,223**

8. Commitments Under Noncancelable Operating Leases:

Following is a summary of future minimum obligations under noncancelable operating leases for equipment and buildings:

Years	Amount
2016	$ 497,383
2017	440,301
2018	181,864
2019	80,977
2020	24,133
	$ 1,224,658

9. Net Patient Service Revenue:

The District recognizes patient service revenue associated with services provided to patients who have third-party payor coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for charity care, the District recognizes revenue on the basis of its standard rates for services provided (or on the basis of discounted rates, if negotiated or provided by policy). On the basis of historical experience, a significant portion of the District's uninsured patients will be unable or unwilling to pay for the services provided. Thus, the District records a significant provision for bad debts related to uninsured patients in the period the services are provided. The District's provisions for bad debts and writeoffs decreased 71% for the year ended June 30, 2015, as compared to June 30, 2014, due to a decrease in uninsured patients primarily due to the Affordable Care Act and the State of California's Medicaid expansion.

The District has not changed its charity care and uninsured discount policies during fiscal years 2015 or 2014. Patient service revenue, net of contractual adjustments and discounts (but before the provision for bad debts), recognized in the period from these major payor sources, is as follows:

	2015	2014
Patient service revenue (net of contractual adjustments and discounts):		
Medicare	$ **20,624,191**	$ 23,286,697
Medi-Cal	**27,329,915**	22,677,094
Other third-party payors	**8,406,850**	8,618,138
Supplemental payments	**4,236,090**	2,403,444
340b contract pharmacies	**615,797**	632,107
Patients	**3,773,984**	8,595,747
	64,986,827	66,213,227
Less:		
Charity care	**(1,725,829)**	(2,180,821)
Provision for bad debts	**(1,765,486)**	(6,029,505)
Net patient service revenue	$ **61,495,512**	$ 58,002,901

The District renders services to patients under contractual arrangements with the Medicare and Medi-Cal programs, in addition to various health maintenance and preferred provider organizations. A summary of the payment arrangements with major third-party payors follows:

- *Medicare* – Inpatient acute care, outpatient and skilled nursing facility services rendered to Medicare program beneficiaries are paid at prospectively determined rates. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The District is reimbursed for some items at a tentative rate with final settlement determined after submission of annual cost reports by the District and audits thereof by the Medicare administrative contractor.

9. Net Patient Service Revenue (continued):

- *Medi-Cal* – Services to Medi-Cal beneficiaries are paid at prospectively determined rates per procedure or discharge. Prior to January 1, 2014, inpatient services were paid on a cost reimbursement method. Reimbursements were at tentative rates with final settlement determined after submission of annual cost reports and audits by Medi-Cal.

- *Other* – Agreements with health maintenance and preferred provider organizations provide for per diem or discounted payments for inpatient services and negotiated discounts from standard charges for outpatient services.

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 will change by a material amount in the near term. Net patient service revenue increased by approximately $132,000 in 2015 and decreased by $148,000 in 2014, due to differences between original estimates and final settlements.

The District provides charity care to patients who are financially unable to pay for the healthcare services they receive. The District's policy is not to pursue collection of amounts determined to qualify as charity care. Accordingly, the District does not report these amounts in net operating revenues or in the allowance for uncollectible accounts. The District determines the costs associated with providing charity care by aggregating the applicable direct and indirect costs, including salaries and wages, benefits, supplies, and other operating expenses, based on data from its costing system. The costs of caring for charity care patients for the years ended June 30, 2015 and 2014, were approximately $620,000 and $722,000, respectively.

10. Electronic Health Records Incentive Payment:

The District recognized Medicaid electronic health records (EHR) incentive payments during the year ended June 30, 2014. The EHR incentive payments are provided to incent hospitals to become meaningful users of EHR technology. EHR incentive payments are therefore reported as operating revenue.

The District recognizes the Medicare incentive payment on the date that the District has successfully complied with meaningful use criteria during the entire EHR reporting period. The District attested to meaningful use with Centers for Medicare and Medicaid Services (CMS) during the federal fiscal year ended September 30, 2013. The Medicare EHR reporting period is through September 30 of each year. The District was later deemed to have not met meaningful use by CMS as of September 30, 2013. The District has recorded a repayment of the $754,458 as a liability at June 30, 2014. The District did not meet meaningful use criteria in fiscal years 2014 or 2015.

The District recognizes the first of its four Medicaid incentive payments in the year that certified EHR technology is adopted, implemented, or upgraded or when such technology is meaningfully used under the Medicare EHR incentive program. The subsequent three payments will be issued when meaningful use is demonstrated under Medicare. A Medicaid incentive payment of $886,916 was recognized as revenue for the year ended June 30, 2014. Subsequent payments have not been received as the District did not meet meaningful use criterial under Medicare.

11. Property Taxes:

The San Bernardino County Treasurer acts as an agent to collect property taxes levied in the County for all taxing authorities. Taxes are levied annually and are due in equal installments in November and April. Property taxes are recorded as revenue when levied. Since state law allows for sale of property for failure to pay taxes, no estimate of uncollectible taxes is made

12. Deferred Compensation Plan and Pension Plan:

The District provides a single employer-defined contribution pension plan covering regular full-time employees who are at least 21 years old and have six months of service with the District. Employer funding into this plan is based on a contribution level equal to 1% of compensation, plus 1% of compensation in excess of the Social Security Compensation Base in effect at the beginning of each plan year. This plan complies with section 401(a) of the Internal Revenue Code.

The District also funds a matching contribution equal to 50% of the employee's contributions made into a 457(b) deferred compensation plan. The name of the plan is Hi-Desert Medical Center Deferred Compensation Plan. Deferrals in excess of 4% are not matched. The District's matching 457(b) plan contributions are deposited into the 401(a) plan. All funds of both plans are maintained and administered by the Variable Annuity Life Insurance Company (VALIC) and Voya Financial, formerly ING/Aetna Financial Services. Employees become fully vested in their accounts after five years of service. The District's contributions to these plans were approximately $417,000 and $420,000 for the years ended June 30, 2015 and 2014, respectively. Employee contributions to the plans were approximately $1,129,000 and $1,735,000 for the years ended June 30, 2015 and 2014, respectively.

13. Risk Management and Contingencies:

Risk management – The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; natural disasters; and employee health, dental, and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Medical malpractice claims – The District has professional liability insurance coverage with Beta Healthcare Group. The policy provides protection on a "claims-made" basis whereby claims filed in the current year are covered by the current policy. If there are occurrences in the current year, these will only be covered in the year the claim is filed if claims-made coverage is obtained in that year or if the District purchases insurance to cover prior acts. The current professional liability insurance provides $10,000,000 per claim of primary coverage with an annual aggregate limit of $20,000,000. The policy has a $5,000 deductible per claim.

Tail coverage – HDMC Holdings obtained professional and general liability insurance policies for an unlimited extended reporting period so that the professional and general liability coverage was effectively converted to an occurrence basis coverage from claims-made coverage as part of the sales and lease agreements described in Note 1.

13. Risk Management and Contingencies (continued):

Workers' compensation program – The District is a participant in the Association of California Hospital District's Alpha Fund (the Fund) which administers a self-insured workers' 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.

Seismic retrofit – The California Hospital Facilities Seismic Safety Act (SB 1953) specifies certain requirements that must be met at various dates in order to increase the probability that a California hospital can maintain uninterrupted operations following a major earthquake. By January 1, 2013, all general acute care buildings were required to be "life-safe". Extensions have been granted to many hospitals, and management is in the process of developing a plan to bring the District into compliance by the extended deadlines.

Litigation – The District may from time-to-time be involved in litigation and regulatory investigations which arise in the normal course of doing business. After consultation with legal counsel, management estimates that matters existing as of June 30, 2015, will be resolved without material adverse effect on the District's future financial position, results from operations, or cash flows.

Industry regulations – The healthcare 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, accreditations, and government healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government activity continues with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare 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 statutes, as well as other applicable government laws and regulations.

While no 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 known or unasserted at this time.

14. Concentration of Risk:

Patient accounts receivable – The District grants credit without collateral to its patients, most of whom are local residents, and are insured under third-party payor agreements. The majority of these patients are geographically concentrated in and around eastern San Bernardino County.

14. Concentration of Risk (continued):

The mix of receivables from patients was as follows:

	2015	2014
Medi-Cal	**50 %**	53 %
Medicare	**28**	20
Patients	**17**	22
Other third-party payors	**5**	5
	100 %	100 %

Physicians – The District is dependent on local physicians practicing in its service area to provide admissions and utilize hospital services on an outpatient basis. A decrease in the number of physicians providing these services or changes in their utilization patterns may have an adverse effect on hospital operations.

SINGLE AUDIT

AUDITORS' SECTION

DINGUS | ZARECOR & ASSOCIATES PLLC
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Joshua Tree, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and the California Controller's minimum audit requirements for California special districts, the financial statements of Hi-Desert Memorial Health Care District doing business as Hi-Desert Medical Center (the District), which comprise the statements of net position as of June 30, 2015, and the related statements of revenues, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 4, 2015.

Internal Control Over Financial Reporting

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

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and questioned costs that we consider to be a significant deficiency (2015-001).

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Compliance and Other Matters

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

District's Response to Finding

The District's response to the finding identified in our audit is described in the accompanying corrective action plan. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

Dingus, Zarecor, and Associates

Spokane Valley, Washington
November 4, 2015

DINGUS | ZARECOR & ASSOCIATES PLLC
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

Board of Directors
Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Joshua Tree, California

Report on Compliance for Each Major Federal Program

We have audited Hi-Desert Memorial Health Care District doing business as Hi-Desert Medical Center's (the District) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2015. The District's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the District's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

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Basis for Qualified Opinion on U.S. Department of Health and Human Services' Health Centers Cluster

As described in the accompanying schedule of findings and questioned costs, the District did not comply with requirements regarding CFDA 93.527 Health Centers Cluster as described in finding number 2015-002 for Program Income. Compliance with such requirement is necessary, in our opinion, for the District to comply with requirements applicable to these programs.

Qualified Opinion on U.S. Department of Health and Human Services' Health Centers Cluster

In our opinion, except for the instance of noncompliance described in the Basis for Qualified Opinion paragraph, the District complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the U.S. Department of Health and Human Services' Health Centers Cluster for the year ended June 30, 2015.

Unmodified Opinion on Compliance for the Other Major Federal Program

In our opinion, the District complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its other major federal program identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs for the year ended June 30, 2015.

Other Matters

The District's response to the noncompliance finding identified in our audit is described in the accompanying corrective action plan. The District's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified a deficiency in internal control over compliance that we consider to be a material weakness.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 2015-002 to be a material weakness.

District's Response to Finding

The District's response to the internal control over compliance finding identified in our audit is described in the accompanying corrective action plan. The District's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Dingus, Zarecor & Associates PLLC

Spokane Valley, Washington
November 4, 2015

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Schedule of Audit Findings and Questioned Costs
Year Ended June 30, 2015

Section I – Summary of Auditors' Results

Financial Statements:

Type of auditors' report issued:	***Unmodified***			
Internal control over financial reporting:				
• Material weakness(es) identified?	____	yes	X	no
• Significant deficiency(ies) identified that are not considered to be material weakness(es)?	X	yes	____	none reported
Noncompliance material to financial statements noted?	____	yes	X	no

Federal Awards:

Internal control over major programs:				
• Material weakness(es) identified?	X	yes	____	no
• Significant deficiency(ies) identified that are not considered to be material weakness(es)?	____	yes	X	none reported
Type of auditors' report issued on compliance for major programs:	***Unmodified for Medical Assistance Program and qualified for Health Centers Cluster.***			
Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of OMB Circular A-133?	X	yes	____	no

Identification of major programs:

CFDA Number(s)	*Name of Federal Program or Cluster*
93.527	Health Centers Cluster
93.778	Medical Assistance Program

Dollar threshold used to distinguish between type A and type B programs: $300,000

Auditee qualified as low-risk auditee?	____	yes	X	no

Section II – Financial Statement Findings

2015-001 Auditor Detected Journal Entries

Condition	Various journal entries were proposed by the audit team to achieve accurate account balances. Adjustments were made to 340b contract pharmacy revenue, grant revenue, lease expense and net position.
Criteria	[ ] Compliance Finding [X] Significant Deficiency [ ] Material Weakness
Context	This finding appears to be a systemic problem.
Cause	Most auditor-detected journal entries related to properly capturing financial information on the accrual basis of accounting as required by generally accepted accounting principles (GAAP).
Effect	Account balances were not accurately stated and significant adjustments were required.
Recommendation	340b contract pharmacy and grant revenue should be recorded on the accrual basis of accounting.

Section III – Federal Award Findings and Questioned Costs

2015-002 Application of Sliding Fee Discounts

Program Information:

Federal Agency	U.S. Department of Health and Human Services
CFDA	93.537 Health Centers Cluster
Award Numbers	H80CS26610 – November 1, 2013 – January 31, 2016
Condition	During our testing of sliding fee discounts for Health Centers Cluster patients qualifying for reduced charge visits, we identified seventeen incidents of no income verification being performed.
Criteria	[X] Compliance Finding [ ] Significant Deficiency [X] Material Weakness OMB Circular A-133 *Compliance Supplement, Part 3, Compliance Requirement J, Program Income* states, "Health centers must have a schedule of fees or payments for the provision of their health services consistent with locally prevailing rates or charges and designed to cover their reasonable costs of operation. They are also required to have a corresponding schedule of discounts applied and adjusted on the basis of the patient's ability to pay."

Section III – Federal Award Findings and Questioned Costs (continued)

2015-002 Application of Sliding Fee Discounts (continued)

Context	This finding appears to be a systemic problem.
Cause	The District did not have adequate processes and review procedures in place to properly administer the sliding fee program.
Effect	Patients may have been granted the incorrect sliding fee percentage.
Questioned Costs	None identified.
Recommendation	We recommend personnel be properly trained on all the requirements of the sliding fee application process in compliance with the *OMB Circular A-133 Compliance Supplement* requirements. We recommend all support reviewed during the application process be kept for future review.

AUDITEE'S SECTION

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2015

Federal Grantor/Pass-through Grantor/Program Title	CFDA Number	Grant Number	Federal Expenditures
U.S. Department of Health and Human Services			
Health Centers Cluster			
Affordable Care Act Grants for New and Expanded Services under the Health Center Program	93.527	H80CS26610	**$ 972,401**
Rural Health Care Services Outreach, Rural Health Network Development and Small Health Care Provider Quality Improvement Program	93.912	P10RH26416	**55,726**
Pass-through program from San Bernardino County Department of Behavioral Health	93.778	13-444	**656,402**
Medical Assistance Program		13-571	
		13-599	
Total U.S. Department of Health and Human Services			**1,684,529**
U.S. Department of Transportation			
Pass-through program from State of California Department of Transportation	20.521	643705	**97,857**
New Freedom Program		642712	
Total U.S. Department of Transportation			**97,857**
Total Expenditures of Federal Awards			**$ 1,782,386**

See accompanying independent auditors' report.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Note to Schedule of Expenditures of Federal Awards
Year Ended June 30, 2015

1. Basis of Presentation:

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Hi-Desert Memorial Health Care District doing business as Hi-Desert Medical Center, and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Corrective Action Plan
Year Ended June 30, 2015

The current year Schedule of Findings and Questioned Costs reported one matter in Section II – Financial Statement Findings. One matter was reported in Section III – Federal Award Findings and Questioned Costs.

Current year audit findings:

Finding Number **Corrective Action Plan**

2015-001 **Auditor-Detected Journal Entries**

Audit adjustments were made to 340b contract pharmacy revenue, grant revenue, lease expense, and net position.

The 340b contract pharmacy program started in March 2014 and is still in the initiation process. The District recorded 340b contract pharmacy activity as a restricted net position account in 2015 and required an audit adjustment to correct.

The District will take the following corrective action to ensure 340b contract pharmacy activity is accurately recorded:

- Once the annual reports have been received from the District's 340b contract pharmacy vendors, pharmacy revenue and expenses will be reconciled with the general ledger accounts. In addition, pharmacy asset and liability accounts will be adjusted within the annual journal entry to reflect current year balances.

The District brought on four San Bernardino County Behavioral Health programs July 1, 2013. There was an accrual entry made for each of the programs at year end based upon the billing invoices. The programs' estimates were underestimated and required an audit adjustment to correct.

The District will take the following corrective action to ensure grant revenues are accurately recorded:

- An annual detailed report for each program will be requested at year end from San Bernardino County once invoices have been submitted to determine the actual revenue to be received.
- Once the reports have been received the accounts receivable accounts will be reconciled and a final year end revenue accrual will be posted.

Finding Number
2015-002 **Application of Sliding Fee Discounts**

The District will take the following corrective action to ensure income for the sliding fee scale is documented properly:

- On a patient's first visit, an application for the sliding fee scale will be completed in its entirety.
- Front office staff will ask for documentation to verify income stated on the application. Appropriate documentation includes the prior year's W-2 or income tax return, or the two most recent pay stubs.
- If patient has no documentation to verify income with them, self-attestation will be allowed for that visit only.
- Patient will be informed that the clinic will accept the application without documentation for current (first) visit only. Patient will be required to submit verification on subsequent appointments or will not be granted the sliding fee. Patient will be responsible for 100 percent of charges.
- Management may use discretion to allow self-attestation for future visits due to special circumstances. Patient will be responsible for 100 percent of charges until such time that management approves the application due to special circumstances.
- Clinic staff will be trained on the policy for required documentation for approval of the sliding fee application.

Hi-Desert Memorial Health Care District
doing business as Hi-Desert Medical Center
Summary Schedule of Prior Audit Findings
Year Ended June 30, 2015

2014-001 Auditor Detected Journal Entries

[ ] Compliance Finding [X] Significant Deficiency [ ] Material Weakness

Condition Various journal entries were proposed by the audit team to achieve accurate account balances. Adjustments were made to 340b contract pharmacy revenue, grant revenue, and net position.

Status Repeated as 2015-001.

2014-002 Application of Sliding Fee Discounts

Program Information:

Federal Agency U.S. Department of Health and Human Services
CFDA 93.537 Health Centers Cluster
Award Numbers H80CS26610 – November 1, 2013 – January 31, 2016

[X] Compliance Finding [ ] Significant Deficiency [X] Material Weakness

Condition During our testing of sliding fee discounts for Health Centers Cluster patients qualifying for reduced charge visits, we identified seven incidents of no income verification being performed.

Status Repeated as 2015-002.