REPORT OF INDEPENDENT AUDITORS AND FINANCIAL STATEMENTS WITH REQUIRED SUPPLEMENTARY INFORMATION

PALOMAR HEALTH

June 30, 2019 and 2018

MOSSADAMS

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Overview

Palomar Health (PH or District) is a public health care district and is a political subdivision of the State of California (the State) organized pursuant to Division 23 of the Health and Safety Code of the State.

This section of PH's annual financial report presents management's discussion and analysis of the financial performance for the years ended June 30, 2019 and 2018. Although the 2017 condensed statement of net position, the condensed statement of revenue, expenses, and changes in net position, and the condensed statement of cash flows are presented in this section, they are not presented in the accompanying audited financial statements and notes to the financial statements. We encourage the reader to consider the information presented here in conjunction with the audited financial statements that follow this section.

This annual financial report includes:

- Management's Discussion and Analysis.
- Report of Independent Auditors.
- Financial statements of PH, including notes that explain in more detail some of the information in the financial statements.
- Schedule of changes in total OPEB liability and related ratios.

The financial statements of PH include the financial statements of Arch Health Partners, Inc. (Arch), Pacific Accountable Management San Diego, LLC (PAM-SD), Pacific Accountable Management, LLC (PAM), and Pacific Accountable Care, LLC (PAC). In accordance with Governmental Accounting Standards Board (GASB) Codification Section 2100, *The Financial Reporting Entity,* for financial reporting purposes, PH's reporting entity includes Arch as a blended component unit as a result of the fiscal dependency of Arch on PH, and because PH is the sole corporate member of Arch. Effective August 31, 2017, PH, Arch, and U.S. Bank National Association added Arch as an additional member of the Obligated Group created pursuant to the Master Trust Indenture. PH and Arch collectively own 100% of PAC, PAM and PAM-SD. Therefore, PAC, PAM, and PAM-SD are included as blended components of PH's reporting entity. Unless otherwise indicated, amounts presented in Management's Discussion and Analysis are in thousands.

Required Financial Statements

Statements of Net Position

The statements of net position include all of PH's assets and liabilities. They also provide information about the nature and amounts of investments in resources (assets), obligations to PH's creditors (liabilities), and net position, which is the difference between assets and liabilities. The statements of net position also provide the basis for evaluating the capital structure of PH and assessing the liquidity and financial flexibility of PH.

The statement of net position as of June 30, 2017, and the related statement of revenue, expenses and changes in net position for the year ended June 30, 2017, were restated upon issuance of the June 30, 2018 financial statements, to show the impact of the adoption of GASB 75.

Table 1: Assets, Deferred Outflow of Resources, Liabilities, Deferred Inflow of Resources, and Net Position as of June 30:

ASSETS AND DEFERRED OUTFLOW OF RESOURCES	2019	2018	2017 (restated)
CURRENT ASSETS	$ 442,894	$ 423,241	$ 417,348
CAPITAL ASSETS - net	1,016,133	1,049,141	1,074,031
NONCURRENT ASSETS	101,425	115,522	70,927
Total assets	1,560,452	1,587,904	1,562,306
DEFERRED OUTFLOW OF RESOURCES	59,093	61,858	44,278
Total assets and deferred outflow of resources	$ 1,619,545	$ 1,649,762	$ 1,606,584
LIABILITIES, DEFERRED INFLOW OF RESOURCES, AND NET POSITION			
CURRENT LIABILITIES	$ 158,502	$ 152,556	$ 151,699
WORKERS' COMPENSATION - net of current portion	3,064	2,484	1,963
FAIR VALUE OF INTEREST RATE SWAP	25,541	18,971	26,473
LONG-TERM DEBT - net of current portion	1,275,903	1,282,517	1,202,333
Total liabilities	1,463,010	1,456,528	1,382,468
DEFERRED INFLOW OF RESOURCES	7,822	7,941	8,041
Total liabilities and deferred inflow of resources	1,470,832	1,464,469	1,390,509
INVESTED IN CAPITAL ASSETS - net of related debt	(135,563)	(91,703)	(56,155)
RESTRICTED, expendable for:			
Repayment of debt	21,722	22,525	21,350
Capital acquisitions	10,088	9,925	9,880
Other purposes	350	349	347
UNRESTRICTED	252,116	244,197	240,653
Total net position	148,713	185,293	216,075
Total liabilities, deferred inflow of resources and net position	$ 1,619,545	$ 1,649,762	$ 1,606,584

2019: Analysis of the Statement of Net Position from 2018 to 2019

- Current assets increased by $19,654 or 5% during the year ended June 30, 2019, primarily due to increases in estimated third-party settlements of $13,528, investments of $11,898, and current restricted cash and investments of $4,376, offset by decreases in patient accounts receivable of $12,458, and other receivables of $133. The increase in third-party settlements is due to management's improved valuation of programs in determining direction to recognize revenue when program funding is available and collectible.

- Capital assets – net decreased by $33,008 or 3% primarily due to depreciation and amortization expense of $43,727, the sale of capital assets and write-down of abandoned projects of $8,684, offset by purchases related to major building projects of $18,983.

- Noncurrent assets and deferred outflow of resources decreased by $16,862 or 10% primarily due to decreases in restricted noncurrent cash and investments of $11,403, prepaid debt insurance costs of $665, amortization of deferred outflows of resources from losses incurred in the refinancing of the Series 2007A General Obligation Bonds (G.O. Bonds) of $2,765, and loan receivable from affiliates and other assets of $2,029.

- Current liabilities increased by $5,671 or 4% primarily due to an increase in accounts payable, accrued compensation and related liabilities, current portion of G.O. Bonds and long term debt and accrued interest payable of $13,028, offset by a decrease in other accrued liabilities of $6,314 and a decrease in estimated third-party liabilities of $1,043.

- Noncurrent liabilities and long term debt increased by $811 or 1% primarily due to an increase in workers' compensation reserve of $580, and in the unrealized loss of the fair value of the interest rate swap of $6,570 offset by a decrease in the long-term debt of $6,339.

- Net position decreased by $36,580 or 20% due to net loss from operations of $5,698 and total non-operating expenses of $30,882.

2018: Analysis of the Statement of Net Position from 2017 to 2018

- Current assets increased by $5,893 or 1% during the year ended June 30, 2018, primarily due to increases in accounts receivable of $12,152, estimated third-party settlements of $11,670, and current restricted cash and investments of $1,633, offset by decreases in cash and cash equivalents of $17,058, and investments of $6,257. The increase in accounts receivable is primarily due to increased aging with certain payor classes, respective collection lags, and increased denial appeals. PH saw an increase in accounts receivable related to patients and auto liability claims, which led to a higher collection percentage but at a lagged rate. In addition, PH experienced post go-live challenges with a new insurance claim scrubber leading to a billing delay. The increase in third-party settlements is due to management's improved valuation of programs in determining direction to recognize revenue when program funding is available and collectible.

2018: Analysis of the Statement of Net Position from 2017 to 2018 (continued)

- Capital assets – net decreased by $24,890 or 2% primarily due to depreciation and amortization expense of $44,781, sale of capital assets, and write-down of abandoned projects for a total of $2,776, offset by purchases related to major building projects of $22,744.

- Noncurrent assets and deferred outflow of resources combined increased by $44,595, or 63% primarily due to increases in restricted noncurrent cash and investments of $46,341, prepaid debt insurance costs of $3,980, and deferred outflows of resources from losses incurred in the refinancing of the Series 2007A General Obligation Bonds (G.O. Bonds) of $17,580, offset by a decrease in loan receivable from affiliates of $1,745.

- Current liabilities increased by $1,132 or 1% primarily due to an increase in accounts payable, accrued compensation, and related liabilities of $11,597, offset by a decrease in current portion of general obligation bonds and long term debt, and other accrued liabilities of $8,630 and a decrease in estimated third-party liabilities of $2,085.

- Noncurrent liabilities and long-term debt increased by $72,928 or 6% primarily due to an increase in long-term debt of $79,909 resulting from the refinancing of long-term debt (See Note 9) and workers' compensation reserve of $521, offset by a decrease in the unrealized loss of the fair value of the interest rate swap of $7,502.

- Net position decreased by $30,782 or 14% due to net loss from operations of $11,861 and total non-operating expenses of $18,921.

Statements of revenue, expenses, and changes in net position – All of PH's revenue, expenses, and changes in net position are included in the statements of revenue, expenses, and changes in net position. The financial statements measure the success of PH's operations during the years presented and are used to determine if PH has successfully recovered all of its costs through its fees and other sources of revenue. It also shows profitability and creditworthiness. Over time, increases or decreases in PH's net position are one indicator of PH's financial health.

In accordance with accounting principles generally accepted in the United States of America (also known as GAAP or generally accepted accounting principles) for governmental health care providers, PH's statements of revenue, expenses, and changes in net position reflect non-operating income (expenses) including interest expense, which for nongovernment hospitals is typically grouped as an operating expense. While these GASB requirements make district hospitals conform to other governmental entities, such as cities and counties, they may be less comparable to nongovernment hospitals because of these GASB requirements. This must be a consideration of any comparison of PH to nonprofit and for-profit hospitals.

Table 2: Operating Results and Changes in Net Position for the years ended June 30:

	2019	2018	2017 (restated)
OPERATING REVENUE:			
Net patient service revenue	$ 693,446	$ 696,948	$ 691,503
Shared risk revenue	82,283	82,326	79,798
Other revenue	13,575	14,894	15,423
Total operating revenue	789,304	794,168	786,724
OPERATING EXPENSES	795,002	806,029	780,967
(LOSS) INCOME FROM OPERATIONS	(5,698)	(11,861)	5,757
NON-OPERATING INCOME (EXPENSE):			
Investment income	5,904	181	1,380
Unrealized (loss) gain on interest rate swap	(6,570)	7,502	12,267
Interest expense	(60,929)	(64,443)	(69,164)
Property tax revenue - unrestricted	17,609	16,779	15,910
Property tax revenue - restricted	20,333	19,093	20,077
Other - net	(7,229)	1,967	(4,287)
Total non-operating expense - net	(30,882)	(18,921)	(23,817)
NET LOSS BEFORE CAPITAL CONTRIBUTIONS	(36,580)	(30,782)	(18,060)
CHANGE IN NET POSITION	(36,580)	(30,782)	(18,060)
NET POSITION - Beginning of year	185,293	216,075	234,135
NET POSITION - End of year	$ 148,713	$ 185,293	$ 216,075

2019: Analysis of the Statement of Revenue, Expenses, and Changes in Net Position from 2018 to 2019

- Operating revenue decreased by $4,864 or 1% during the year ended June 30, 2019, primarily due to an increase in behavioral health volume, lower than expected surgical cases and less severe flu season than prior years. Management has implemented a number of operational initiatives which has resulted in improved billing and collections. Continued participation in government reimbursement and supplemental programs, including but not limited to: Medi-Cal Quality Assurance program, Managed Care Rate Range Plan, Public Hospital Redesign and Incentives in Medi-Cal (PRIME), and Outpatient Supplemental Program contributes to operational revenue.

- Operating expenses are those expenses related to the treatment of patients as well as overhead and administrative expenses. Operating expenses decreased by $11,027 or 1% during the year ended June 30, 2019, primarily due to decreases in salaries, wages, and benefits of $10,677 which was driven by improvements in productivity, lower utilization of contract labor and other operational improvement initiatives implemented by management, offset by increase in purchased services of $5,761. Professional fees decreased $5,335 reflecting PH's continued focus on restructuring unfavorable contracts and lower utilization of consulting services. Other direct expenses, the combination of rent, utilities, and other expense, decreased by $2,156, primarily due to a decrease in other expenses of $4,554, rental equipment of $554, offset by increases in utilities of $593, and medical office building rent of $2,359. The decrease in operating expenses included a reduction in depreciation expense of $1,054 due to fewer capital outlays than the previous year and assets reaching the end of their useful lives.

- Non-operating expenses (net) increased by $11,961 or 63% during the year ended June 30, 2019, primarily due to an increase in the unrealized loss on the interest rate swap of $14,072, offset by an increase in property tax revenue of $2,070, a decrease in interest expense of $3,514 and an increase in investment income of $5,723.

- As a result of the factors noted above, net position decreased by $36,580 or 20% during the year ended June 30, 2019.

2018: Analysis of the Statement of Revenue, Expenses, and Changes in Net Position from 2017 to 2018

- Operating revenue increased by $7,744 or 1% during the year ended June 30, 2018, primarily due to annual rate increases, improved pricing from payor contracts, increased billing and collection efficiencies augmented by continued participation in government reimbursement and supplemental programs, including but not limited to: Medi-Cal Expansion program, Managed Care Rate Range Plan, Public Hospital Redesign and Incentives in Medi-Cal (PRIME), and Outpatient Supplemental Program. Other revenue decreased $32 primarily due to the reduced bed capacity for Rady Children's Hospital (RCH) of $910. PH and RCH have an affiliation whereby PH transferred the day to day operations of the neonatal intensive care unit to RCH. This decrease is offset by an increase in the Child Abuse Program/Sexual Assault Response Team programs of $619, and an improvement of $534 in the Palomar Health Development grants program. The decrease related to RCH's capacity is driven by the move from the Palomar Medical Center Downtown Campus (PHDC) to Palomar Medical Center (PMC) Escondido.

- Operating expenses are those expenses related to the treatment of patients as well as overhead and administrative expenses. Operating expenses increased by $25,062 or 3% during the year ended June 30, 2018, primarily due to increases in salaries, wages, and benefits of $29,202 which was driven by additional labor force and premium pay required during union negotiations, surveys and flu season, annual merit increases and increases to the annual health insurance of $4,510, and workers' compensation premiums and claims of $1,064. Professional fees increased $4,842 reflecting PH's continued focus on medical directorships and professional assistance related to the union negotiations. Other direct expenses increased by $2,492, primarily due to increased utilities usage of $1,049, medical office building rent of $821, and remaining operating expenses of $100. The increase in operating expenses was offset by a decrease in purchased services of $4,865 due to a restructuring of PH's IT service contract of $2,911, offset by the initiative to improve revenue cycle processes and cash collection efficiencies of $3,248, and $3,100 due to management's effort to identify cost saving opportunities, a reduction in repairs and maintenance of $1,534, and a reduction in depreciation expense of $6,644 from less capital outlay than the previous year and assets reaching end of their useful lives.

- Non-operating expenses (net) decreased by $4,896 or 21% during the year ended June 30, 2018, primarily due to a decrease in interest expense of $4,721, the loss on the sale of capital assets of $3,022 and other non-operating expenses of $132, offset by a decrease in the unrealized gain on the interest rate swap which was included in non-operating income of $4,765 and investment income of $1,199.

- As a result of the factors noted above, net position decreased by $30,782 or 14% during the year ended June 30, 2018.

Statements of Cash Flows

The statements of cash flows report cash receipts, cash payments, and net changes in cash resulting from operating, investing, and financing activities, which provides answers to such questions as what were the sources and uses of cash, and what was the change in the cash balance during the reporting year.

Table 3: Statement of Cash Flows for the years ended June 30:

	2019	2018	2017
CASH FLOWS FROM:			
Operating activities	$ 42,206	$ 14,798	$ 52,155
Noncapital financing activities	17,609	16,779	12,458
Capital and related financing activities	(61,397)	(5,805)	(53,449)
Investing activities	2,238	(42,830)	(4,213)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	656	(17,058)	6,951
CASH AND CASH EQUIVALENTS - Beginning of year	49,480	66,538	59,587
CASH AND CASH EQUIVALENTS - End of year	$ 50,136	$ 49,480	$ 66,538

2019: Analysis of the Statement of Cash Flows from 2018 to 2019

- Net cash inflows provided by operating activities reflected an increase of $27,408 during the year ended June 30, 2019, over the year ended June 30, 2018. This increase is primarily due to an increase in accounts receivable collections of $23,021, offset by a decrease in accrued compensation and related liabilities of $3,395.

- Net cash outflows used in capital and related financing activities increased by $55,592 primarily due to the decrease in proceeds on bond offerings of $77,339.

- Net cash inflows provided by noncapital financing activities reflected an increase of $830 during the year ended June 30, 2019, due to an increase in district tax revenue receipts.

- Net cash provided by investing activities during the year ended June 30, 2019, increased by $45,068 primarily due to a decrease in proceeds from the sale of investments of $29,675 and the decrease in purchase of investments of $73,612.

- The ending cash and cash equivalents of $50,136 at June 30, 2019, reflect the checking account and overnight investment balances held by PH. In addition, PH held investments of $162,822 at June 30, 2019, with maturities of one year or less which are classified as current assets.

2018: Analysis of the Statement of Cash Flows from 2017 to 2018

- Net cash inflows provided by operating activities reflected a decrease of $37,357 during the year ended June 30, 2018, over the year ended June 30, 2017. This decrease is primarily due to a decrease in accounts receivable collections, an increase in slow-paying programs, and an increase in payments to suppliers of $6,765 due to the increased volume in high-cost surgeries.

- Net cash outflows used in capital and related financing activities increased by $47,644 primarily due to the refinance and issuance of new debt, resulting in an increase of interest payments and cost of issuance of $5,719 and an increase in restricted property tax revenue of $1,450, offset by a decrease in repayment of long-term debt of $45,303 and a decrease in the acquisition of property, plant, and equipment of $6,740.

- Net cash inflows provided by noncapital financing activities reflected an increase of $4,321 during the year ended June 30, 2018, due to an increase in district tax revenue receipts.

- Net cash provided by investing activities during the year ended June 30, 2018, increased by $38,617 primarily due to an increase in proceeds from the sale of investments of $51,846, offset by the purchase of investments of $90,463.

- The ending cash and cash equivalents of $49,480 at June 30, 2018, reflect the checking account and overnight investment balances held by PH. In addition, PH held investments of $150,924 at June 30, 2018, with maturities of one year or less which are classified as current assets.

2019 and 2018: Capital Assets and Long-Term Debt

In 2004, the Board of Directors approved the Facilities Master Plan budgeted at $1,057,000. In November 2004, the residents of the District voted and approved to fund $496,000 of this expansion by the issuance of G.O. Bonds. Payment for these bonds was funded by an *ad valorem* property tax levied on District residents. The approximate amount of the tax levy for each taxable property was 21.0% of assessed value during the years ended June 30, 2019 and 2018, respectively. The levy was established by the Board of Directors' resolution each year in an amount sufficient to service the debt for the upcoming year along with a reserve amount.

One of the major components of the Facilities Master Plan included the construction of PMC. On August 19, 2012, PH opened the 288-bed facility, which includes critical, intermediate, and general inpatient care, surgical and interventional services, a women's center, and emergency and trauma services.

Other building projects include the renovation of existing hospital facilities at Pomerado Hospital, now known as Palomar Medical Center Poway (Poway), and construction of a medical office building, parking structure, and ambulatory and outpatient facilities at various locations in the District.

2019 and 2018: Capital Assets and Long-Term Debt (continued)

PH has four outstanding revenue bonds and five outstanding G.O. Bonds that are classified as long-term debt. The revenue bonds are comprised of the 2006 Certificates of Participation (COP), the 2017 COP, and the 2016 and 2017 Refunding Revenue Bonds. The G.O. Bonds are comprised of the Series 2007A, 2009A, 2010A, and 2016 A and B bonds. Principal payments of $12,290 and $169,690 during the years ended June 30, 2019 and 2018, respectively, reduced the revenue bonds' principal to $596,235 and $608,525 as of June 30, 2019 and 2018, respectively. As of June 30, 2018, the outstanding principal balance of the 2010 COP that was advance refunded during fiscal year 2018 was $158,705. The 2010 COP are considered to be defeased and the liability for these bonds has been removed from the statement of net position. Principal payments of $5,234 and $7,107 during the years ended June 30, 2019 and 2018, respectively, reduced the G.O. Bonds' principal to $431,124 and $436,359 as of June 30, 2019 and 2018, respectively. All debt payments have been made timely. See Note 9 for long-term debt on a consolidated basis.

In July 2005, PH issued its first series of G.O. Bonds authorized by voter approval in 2004 (measure BB) in the amount of $80,000 for use in funding the building expansion project. In December 2007, PH issued its second series of G.O. Bonds totaling $241,083. In March 2009, PH issued its third series of G.O. Bonds in the amount $110,000. In November 2010, PH issued the final series of G.O. Bonds in the amount of $64,917.

In July 2016, the Board of Directors authorized management to commence the due diligence associated with the refunding of the 2005 and 2007 General Obligation Bonds and the 2009 Revenue Bonds.

In October 2016, the $246,750 Refunding Revenue Bonds Series 2016 were issued with the purpose of refunding the 2009 Certificates of Participation, funding a reserve account and paying the costs of issuance of the Series 2016 Revenue Bonds.

On October 27, 2016, the $48,520 General Obligation Refunding Bonds Series 2016A were issued with the purpose of refunding the General Obligations Bonds, Election of 2004, Series 2005A and paying a portion of the costs of issuance of the Series 2016 G.O. Bonds.

On October 27, 2016, the $164,450 General Obligation Refunding Bonds Series 2016B were issued with the purpose of refunding a portion of the General Obligation Bonds, Election of 2004, Series 2007A, funding a reserve account and paying a portion of the costs of issuance of the Series 2016 G.O. Bonds.

On December 11, 2017, the Board of Directors authorized the issuance of the $151,460 Refunding Revenue Bonds, Series 2017 with the purpose to advance refund the refunding 2010 COP, fund a reserve account for the Refunding Bonds, and pay the costs of issuing the Series 2017 Revenue Bonds. This refunding served to lower interest costs and generate savings creating capacity for a new bond issuance.

In conjunction with the above refunding, the Board of Directors authorized management to commence the due diligence associated with issuing the $60,100 Series 2017 COP. Proceeds in the related Project Fund will finance the construction, improvement, renovation, and equipping of hospital and related health care facilities.

2019 and 2018: Capital Assets and Long-Term Debt (continued)

The collective advance refunding as described above resulted in an overall economic gain of $44,973.

Liquidity and Capital Resources

PH's unrestricted liquid assets as of June 30, 2019, were $212,958, including $50,136 in operating cash, and $162,822 in unrestricted investments stated at fair market value. The current liquidity position represents a $12,554 increase from the $200,404 in available liquidity as of June 30, 2018, and equaled 33% of the total outstanding debt as of June 30, 2019 (excluding the existing G.O. Bonds, which are paid from *ad valorem* property taxes), as compared to available liquidity representing 31% of total outstanding debt as of June 30, 2018.

PH's days cash and investments on hand as of June 30, 2019 and 2018, was 103.3 and 96.1, respectively.

Economic and Other Factors

On June 24, 2015, PH's Board of Directors voted to transfer all services from PHDC to other PH-owned facilities. Due to failing infrastructure and absent a seismic retrofit, the Board also voted to close the facility. The sale of the PHDC remained in escrow at the end of June 30, 2019. The sales contract specifies the transaction must close no later than the third quarter of the calendar year ended December 31, 2020. The remaining downtown services will be relocated as new facilities are completed.

The challenge of meeting constant capital needs and consumer demands becomes more difficult as the health care industry is highly dependent upon a number of factors that could have a significant effect on the operations and financial condition of PH. The healthcare industry is moving towards value-based care which requires improved efficiency and quality measures. As PH shifts towards these patient-centric drivers, inpatient utilization rates will lower with the decrease of readmission rates and improved continuum of care management.

Government payors continue to present reimbursement challenges for healthcare districts as the reimbursement rates are set annually with no ability for negotiation on rates and terms. In addition to the 2% sequestration cuts that were put in place in 2013, Medicare continues to look for additional ways to cut medical costs by way of reimbursement modeling. Quality-based reimbursement methods incentivize health care providers to improve quality outcomes and patient experiences and penalize those who are not able to meet these measures. Contractually negotiated commercial payments, while based on an agreed-upon reimbursement methodology, are susceptible to shifts in demand, patterns of patient services, and sensitive to a more competitive market.

Union Contract

PH and two unions, the California Nurses Association (CNA) and the Caregivers Healthcare Employees Union (CHEU) reached agreements on December 27, 2017. Both contracts are now in effect and valid through May 31, 2021.

Finance contact – PH's financial statements are designed to present users with a general overview of PH's finances and to demonstrate PH's accountability. If you have any questions about the report or need additional financial information, please contact the Chief Financial Officer, PH, 456 E. Grand Avenue, Escondido, California 92025.

Report of Independent Auditors

To the Audit Committee of
Palomar Health

Report on Financial Statements

We have audited the accompanying financial statements of Palomar Health, which comprise the statements of net position as of June 30, 2019 and 2018, and the related statements of revenue, expenses, and changes in net position, and cash flows for the years 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the California Code of Regulations, Title 2, Section 1131.2, *State 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Palomar Health as of June 30, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Required Supplementary Information

Accounting standards generally accepted in the United States of America require that the management's discussion and analysis, and schedule of changes in total OPEB liability and related ratios, as listed in the table of contents, 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, and 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.

Moss Adams LLP

Irvine, California
October 17, 2019

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(Dollars in Thousands)

ASSETS AND DEFERRED OUTFLOW OF RESOURCES

	June 30, 2019	June 30, 2018
CURRENT ASSETS		
Cash and cash equivalents	$ 50,136	$ 49,480
Investments	162,822	150,924
Patient accounts receivable - net of allowances for uncollectible accounts of $43,305 in 2019 and $27,720 in 2018	123,761	136,219
Other receivables	10,050	10,183
Supplies and inventories	12,239	11,547
Prepaid expenses and other	5,552	4,458
Estimated third-party payor settlements receivable	42,141	28,613
Restricted cash and investments, current	36,193	31,817
Total current assets	442,894	423,241
RESTRICTED NONCURRENT CASH AND INVESTMENTS		
Held by trustee under indenture agreements	78,352	90,031
Held by trustee under general obligation bonds indenture	36,041	31,553
Held in escrow for street improvements	10,088	9,925
Restricted by donor and other	350	349
Total restricted cash and investments	124,831	131,858
Less amounts required to meet current obligations	36,193	31,817
Total restricted noncurrent cash and investments	88,638	100,041
CAPITAL ASSETS - net	1,016,133	1,049,141
OTHER ASSETS		
Prepaid debt insurance costs	9,371	10,036
Investment in and amounts due from affiliated entities	2,170	2,816
Other	1,246	2,629
Total other assets	12,787	15,481
Total assets	1,560,452	1,587,904
DEFERRED OUTFLOW OF RESOURCES - loss on refunding of debt	59,093	61,858
Total assets and deferred outflow of resources	$ 1,619,545	$ 1,649,762

Palomar Health
Statements of Net Position (Continued)
(Dollars in Thousands)

LIABILITIES. DEFERRED INFLOWS OF RESOURCES, AND NET POSITION

	June 30, 2019	June 30, 2018
CURRENT LIABILITIES		
Accounts payable	$ 45,137	$ 47,692
Accrued compensation and related liabilities	45,047	44,183
Current portion of general obligation bonds	9,100	5,234
Current portion of long-term debt - other	12,915	12,376
Estimated third-party payor settlements liability	768	1,811
Other accrued liabilities	31,064	31,904
Accrued interest payable	14,471	9,356
Total current liabilities	158,502	152,556
WORKERS' COMPENSATION - net of current portion	3,064	2,484
LONG-TERM DEBT - general obligation bonds - net of current portion	647,451	638,852
LONG-TERM DEBT - other - net of current portion	628,452	643,665
FAIR VALUE OF INTEREST RATE SWAP	25,541	18,971
Total liabilities	1,463,010	1,456,528
DEFERRED INFLOW OF RESOURCES	7,822	7,941
Total liabilities and deferred inflow of resources	1,470,832	1,464,469
COMMITMENTS AND CONTINGENCIES (Note 15)		
NET POSITION		
Net investment in capital assets	(135,563)	(91,703)
Restricted, expendable for:		
Repayment of debt	21,722	22,525
Capital acquisitions	10,088	9,925
Other purposes	350	349
Unrestricted	252,116	244,197
Total net position	148,713	185,293
Total liabilities, deferred inflow of resources, and net position	$ 1,619,545	$ 1,649,762

See accompanying notes.

(Dollars in Thousands)

	Year Ended June 30, 2019	2018
OPERATING REVENUE		
Patient service revenue, net of provision for uncollectible accounts of $60,747 in 2019 and $59,158 in 2018	$ 693,446	$ 696,948
Shared risk revenue	82,283	82,326
Other revenue	13,575	14,894
Total operating revenue	789,304	794,168
OPERATING EXPENSES		
Salaries, wages, and benefits	464,625	475,302
Professional fees	41,034	46,369
Supplies	109,255	106,821
Purchased services	87,229	81,468
Depreciation and amortization	43,727	44,781
Rent expense	20,587	18,782
Utilities	11,476	10,883
Other	17,069	21,623
Total operating expenses	795,002	806,029
LOSS FROM OPERATIONS	(5,698)	(11,861)
NON-OPERATING INCOME (EXPENSES)		
Investment income	5,904	181
Unrealized (loss) gain on interest rate swap	(6,570)	7,502
Interest expense	(60,929)	(64,443)
Property tax revenue - unrestricted	17,609	16,779
Property tax revenue - restricted	20,333	19,093
Other - net	(7,229)	1,967
Total non-operating expenses - net	(30,882)	(18,921)
CHANGE IN NET POSITION	(36,580)	(30,782)
NET POSITION - beginning of year	185,293	216,075
NET POSITION - end of year	$ 148,713	$ 185,293

Palomar Health
Statements of Cash Flows
(Dollars in Thousands)

	Year Ended June 30, 2019	Year Ended June 30, 2018
CASH FROM OPERATING ACTIVITIES		
Receipts from:		
Patients, insurers, and other third-party payors	$ 828,752	$ 807,441
Other sources	16,881	18,409
Payments to:		
Employees	(463,180)	(470,739)
Suppliers	(340,247)	(340,313)
Net cash provided by operating activities	42,206	14,798
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Receipt of district taxes	17,609	16,779
Net cash provided by noncapital financing activities	17,609	16,779
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	(18,702)	(21,037)
Interest payments on long-term debt	(37,918)	(42,335)
Proceeds from issuance of long-term debt	-	230,034
Defeasance of debt	-	(174,176)
Principal repayment on long-term debt	(17,880)	(20,681)
Proceeds from sale of capital assets	-	1,255
Receipt of property taxes restricted for debt service on general obligation bonds	20,333	19,093
Other	(7,230)	2,042
Net cash used in capital and related financing activities	(61,397)	(5,805)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(165,696)	(239,309)
Proceeds from sale of investments	166,622	196,297
Interest received on investments and notes receivable	1,312	182
Net cash provided by (used in) investing activities	2,238	(42,830)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	656	(17,058)
CASH AND CASH EQUIVALENTS - beginning of year	49,480	66,538
CASH AND CASH EQUIVALENTS - end of year	$ 50,136	$ 49,480

See accompanying notes.

(Dollars in Thousands)

	Year Ended June 30, 2019	Year Ended June 30, 2018
RECONCILIATION OF LOSS FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Loss from operations	$ (5,698)	$ (11,861)
Adjustments to reconcile loss from operations to net cash provided by operating activities:		
Depreciation and amortization	43,727	44,781
Provision for bad debts	60,747	59,158
Equity in losses of affiliates	646	1,745
Loss on disposal of fixed assets	8,083	1,521
Changes in assets and liabilities:		
Patient accounts receivable	(48,289)	(71,310)
Other receivables	133	(2,513)
Supplies and inventories	(692)	(991)
Prepaid expenses and other	(1,454)	(249)
Estimated third-party payor settlements	(14,571)	(13,755)
Other - net	1,383	3,981
Accounts payable	(2,294)	98
Accrued compensation and related liabilities	1,444	4,839
Other accrued liabilities	(840)	(546)
Deferred inflow of resources	(119)	(100)
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 42,206	$ 14,798
NONCASH INVESTING AND CAPITAL AND FINANCING ACTIVITIES		
Capital expenditures included in accounts payable	$ 2,329	$ 2,590
Premium related to issuance of 2017 Revenue Bonds	$ -	$ 18,829
Settlement of future interest payments and fees related to defeasance of debt	$ -	$ 23,567

Note 1 – Operations and Reporting Entity

Organization – Palomar Health (PH or District), a public health care district, is organized under the provisions of the Health and Safety Code of the State of California to provide and operate health care facilities. The accompanying financial statements include the accounts of the following commonly controlled divisions and related entities of PH. Unless otherwise indicated the following are divisions of PH:

- Palomar Medical Center Escondido (Escondido), located in west Escondido, California, includes a 288-bed general acute care hospital, including tertiary services, trauma services, cardiovascular surgery, women's services, and retail pharmacy.

- Palomar Medical Center Poway (Poway), located in Poway, California, includes a 107-bed general acute care hospital, and Villa Pomerado, a distinct part skilled nursing facility and sub-acute facility.

- Palomar Medical Center Downtown Campus (PHDC), located in east Escondido, California, includes acute rehab, Center for Behavioral Health, radiation therapy, and a crisis stabilization unit.

- Palomar Home Health Services, located in Escondido, California.

- San Marcos Ambulatory Care Center located in San Marcos, California, includes outpatient therapy.

- Jean McLaughlin Women's Center for Health and Healing, located on the Poway campus.

- Palomar Outpatient Behavioral Health, located in San Marcos, California.

- PH Development, a charitable tax exempt organization created to provide assistance and support for PH by obtaining grant funding from federal, state, local, and private sources.

- Arch Health Partners, Inc. (Arch), a tax exempt medical foundation established under Section 1206(l) of the California Health and Safety Code, with fifteen clinics located in Poway, Escondido, Ramona, and San Marcos, California, that provide primary and specialty care medical services, and add another component in effective health care delivery to residents within PH's community. In accordance with Governmental Accounting Standards Board (GASB) Codification Section 2100, *The Financial Reporting Entity*, for financial reporting purposes, PH's reporting entity includes Arch as a blended component unit as a result of the fiscal dependency of Arch on PH, and because PH is the sole corporate member of Arch.

- Pacific Accountable Care, LLC (PAC), a Medicare approved Accountable Care Organization (ACO) that has contracted with Centers for Medicare & Medicaid Services (CMS) as a participant in a Track 1 Medicare Shared Savings Program (MSSP) to provide coordinated high-quality care to Medicare patients at reduced cost. Arch's reporting entity includes PAC as a blended component unit because Arch is the sole member of PAC. See Note 8.

Note 1 – Operations and Reporting Entity (continued)

- Pacific Accountable Management, LLC (PAM) and Pacific Accountable Management San Diego (PAM-SD) operated as management service organizations (MSO), and provided administrative and billing services to Arch during the year ended June 30, 2018. Operations for PAM and PAM-SD ceased in July 2018 when the MSO services were assumed by Arch. Revenue and expenses of PAM and PAM-SD were minimal during the year ended June 30, 2019. See Note 8.

Arch membership of obligated group – On August 31, 2017, PH, Arch, and U.S. Bank National Association, as Master Trustee, entered into a Supplemental Master Indenture agreement providing for addition of Arch as a member of the Obligated Group created pursuant to the Master Indenture of Trust Dated December 1, 2006. As such, Arch becomes jointly and severally liable for the repayment of PH's revenue obligations and places its collateral under control of a master trustee for the benefit of lenders and bondholders. In consideration of the agreement of Arch to become an Obligated Group Member, PH has agreed to the extinguishment of Arch Obligations. Related eliminations can be found in Note 16.

Note 2 – 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, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Basis of accounting and presentation – The accompanying financial statements have been prepared using the economic resource measurement focus and the accrual basis of accounting, in accordance with U.S. generally accepted accounting principles for healthcare organizations and the State Controller's Minimum Audit Requirements and Reporting Guidelines, and are presented in accordance with the reporting model as prescribed in GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. PH follows the business-type activities requirements of GASB Statement No. 34 and No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*.

Fiscal year – PH has adopted a fiscal year ending June 30. All references to years herein refer to the respective fiscal year.

Reclassifications – Certain prior year amounts were reclassified to conform to current year presentation.

Cash and cash equivalents – Cash and cash equivalents include highly liquid debt instruments with original maturities of three months or less and are intended for use in daily operations.

Investments – Investments in debt, equity, and fixed income securities are carried at fair value, as determined by quoted market prices in the statements of net position. Investment income or loss is included in non-operating income, unless the income or loss is restricted by donor or law.

Note 2 – Summary of Significant Accounting Policies (continued)

Supplies and inventories – Supplies and inventories are stated at the lower of cost (first-in, first-out) or market value.

Restricted cash and investments – Restricted cash and investments primarily includes assets held by trustees under indenture agreements and designated assets set aside by the Board of Directors for future capital improvements over which the Board of Directors retains control and may, at its discretion, subsequently use for other purposes. Amounts required to meet current liabilities of PH have been classified as current assets in the accompanying statements of net position.

PH has entered into an agreement with the City of Escondido (the City) to financially participate in street improvements near the site of Escondido. Under the agreement, PH was required to deposit $13,000 into an account jointly managed by PH and the City. PH's financial obligation is limited to the deposited amount plus any earned interest on the deposited funds. The balance of $10,088 and $9,925 as of June 30, 2019 and 2018, respectively, was included in restricted cash and investments in the accompanying statements of net position.

Capital assets – Capital asset acquisitions are recorded at cost. The capitalization threshold for individual item cost is $5 or greater and similar items that have cost less than $5 but have an aggregate cost of $20 or greater. Depreciation is computed using the straight-line method over the estimated useful life of each class of depreciable asset (the shorter of the estimated useful life or the lease term for leasehold improvements) as follows:

	Years
Land improvements	10-40
Buildings and building improvements	10-40
Leasehold improvements	3-15
Equipment	3-20

Gifts of long-lived assets, such as land, buildings, or equipment, are recorded at their fair market value and are reported in non-operating income. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted for other purposes in net position. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated, or acquired long-lived assets are placed in service.

Note 2 – Summary of Significant Accounting Policies (continued)

Capital assets are reviewed for impairment when events or changes in circumstances suggest that the service utility of the capital asset may have significantly and unexpectedly declined. Capital assets are considered impaired if both the decline in service utility of the capital asset is large in magnitude and the event or change in circumstance is outside the normal life cycle of the capital asset. Such events or changes in circumstances that may be indicative of impairment include evidence of physical damage, enactment, or approval of laws or regulations or other changes in environmental factors; technological changes or evidence of obsolescence; changes in the manner or duration of use of a capital asset; and construction stoppage. The determination of the impairment loss is dependent upon the event or circumstance in which the impairment occurred. Impairment losses are recorded in the statements of revenue, expenses, and changes in net position. During the year ended June 30, 2019, an impairment charge of $6,100 was recorded. During the year ended June 30, 2018, no impairment charges were recorded.

Compensated absences – PH policies permit most employees to accumulate vacation and sick leave benefits that may be realized as paid time off or, in limited circumstances, as a cash payment. Expense and the related liability are recognized as vacation benefits and are earned whether the employee is expected to realize the benefit as time off or in cash. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the statement of net position date plus an additional amount for compensation-related payments such as Social Security and Medicare taxes computed using rates in effect at that date.

Debt discounts, debt premiums, and debt issuance costs – Debt discounts and debt premiums are amortized by the effective interest method over the life of the related bonds. Debt issuance costs, except prepaid insurance costs, are expensed as incurred. Prepaid insurance costs are reported as an asset and recognized as an expense over the duration of the related debt.

Deferred outflows of resources – Deferred outflows of resources represent a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until that time. The deferred outflows of resources reported in the financial statements is loss on refunding of debt which is amortized over the shorter of the remaining life of the refunded bonds or the refunding debt as a component of interest expense. See Note 9.

Deferred inflows of resources – Deferred inflows of resources represent an increase in net position that applies to future periods and so will not be recognized as an inflow of resources (revenue) until that time. The deferred outflows of resources reported in the financial statements are unearned rental income that will be recognized as revenue over the life of the rental agreement and the change in assumptions and other inputs related to Other Post-Employment Benefits (OPEB). See Note 14.

Note 2 – Summary of Significant Accounting Policies (continued)

Interest rate swaps – PH has entered into variable-to-fixed interest rate swaps, which are reflected at fair value in the statements of net position. The fair value of the interest rate swaps will fluctuate based generally on changes in market rates of interest. Unrealized gains or losses resulting from changes in fair value are reported as interest expense in non-operating income (expenses) in the statements of revenue, expenses, and changes in net position. Interest cost on variable interest rate debt is reported based on the fixed interest rate paid by PH under the interest rate swaps and is also recorded as interest expense. As of June 30, 2019 and 2018, the interest rate swaps were recorded as a liability of $25,541 and $18,971, respectively.

Net position – Net position of PH is classified in three broad components: net investment in capital assets, restricted (distinguishing between major categories of restrictions), and unrestricted. Net investment in capital assets consists of capital assets, net of accumulated depreciation, and reduced by the outstanding balances of borrowings used to finance the purchase or construction of those assets. Net position restricted for repayment of debt includes amounts deposited with trustees as required by bond indentures, as described in Note 9. Net position restricted for capital acquisitions relates to amounts restricted to acquire capital assets. Net position restricted for other purposes relates to noncapital net position that must be used for a particular purpose, as specified by contributors or others external to PH. Unrestricted net position represents the remaining net position that does not meet the definition of net investment in capital assets, or restricted.

Risk management – PH 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 other than medical malpractice and workers' compensation claims. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

PH is self-insured for a portion of its exposure to risk of loss from workers' compensation and malpractice claims. Annual estimated provisions are accrued based on actuarially determined amounts or management's estimate, and includes an estimate of the ultimate costs for both reported claims, and claims incurred but not yet reported.

Statements of revenue, expenses, and changes in net position – All revenue and expenses directly related to the delivery of health care services are included in operating revenue and expenses in the statements of revenue, expenses, and changes in net position. Non-operating income (expenses) consist of those revenue and expenses that result from non-exchange transactions, financing (interest expense and changes in the fair value of interest rate swaps), and investment income.

Note 2 – Summary of Significant Accounting Policies (continued)

Net patient service revenue – PH has agreements with third-party payors that provide for payments to PH at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and daily rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including a provision for bad debts and estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis during the year the related services are rendered and adjusted in future years, as final settlements are determined.

Shared risk revenue – PH and its affiliated medical groups have agreements with various third-party payors to provide medical services to subscribing participants. Under some of these agreements, PH and its affiliated medical groups receive monthly capitation payments based on the number of members for each payor, regardless of services actually performed by PH. Under these agreements, after deduction of costs incurred by providers outside these agreements for care provided to subscribing participants, PH participates in shared risk pools with medical groups, through which it earns reimbursement or pays additional amounts to the medical groups. In conjunction with the shared risk pools, PH estimates incurred but not reported (IBNR) claims for medical services provided to patients. IBNR of $8,467 and $8,176 are included in other accrued liabilities in the accompanying statements of net position as of June 30, 2019 and 2018, respectively.

Activity in PH's liability for IBNR claims for medical services provided to patients as of and for the years ended June 30, 2019 and 2018, is summarized as follows (in thousands):

	2019	2018
BALANCE, beginning of the year	$ 8,176	$ 10,966
Current year claims incurred and changes in estimates	44,378	41,547
Claims and expenses paid	(44,087)	(44,337)
BALANCE, end of the year	$ 8,467	$ 8,176

Charity care – PH provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Amounts determined to qualify as charity care are not reported as revenue in the accompanying financial statements.

Note 2 – Summary of Significant Accounting Policies (continued)

Property taxes – PH receives financial support from property taxes. Property taxes are levied by the County of San Diego on behalf of PH to finance PH's activities. Amounts levied for General Obligation Bonds (G.O. Bonds) are based on assessed property values and are set annually by the Board of Directors. Property tax revenue for the years ended June 30, 2019 and 2018, consists of the following (in thousands):

	2019	2018
To support operations - unrestricted use	$ 17,609	$ 16,779
For debt service on G.O. Bonds - restricted use	20,333	19,093
	$ 37,942	$ 35,872

Income taxes – PH is a governmental subdivision of the State of California and is exempt from federal income and state franchise taxes. Arch and PAC are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code (IRC) and Section 23701(d) of the California Revenue and Taxation Code. PAM and PAM-SD, which are limited liability companies (LLC) are classified as partnerships for federal and state income tax purposes, and, as such, are exempt from federal income and state franchise taxes.

Accordingly, no provision for income taxes has been included in the accompanying financial statements.

Recent accounting pronouncements – In January 2017, the GASB issued Statement No. 84, *Fiduciary Activities.* This statement establishes fiduciary criteria and requires PH to report separate fiduciary funds financial statements within the District's financial statements. This statement is effective July 1, 2019. PH is evaluating the impact of adopting this statement on the financial statements.

In June 2017, the GASB issued Statement No.87, *Leases*, establishing a single approach to the accounting for and reporting of leases by state and local governments requiring that all leases be considered as financing. Under the new guidance, PH must recognize a lease liability and an intangible asset in the financial statements. The statement is effective July 1, 2020. PH is evaluating the impact of adopting this statement on the financial statements.

In June 2018, the GASB issued Statement No. 89, *Accounting for Interest Cost Before the End of a Construction Period.* This statement requires that interest costs incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest costs incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type activity or enterprise fund. This statement is effective July 1, 2019. PH is evaluating the impact of adopting this statement on the financial statements.

Note 3 – Net Patient Service Revenue, Third-Party Reimbursement Programs, and Non-Operating Revenue

Net patient service revenue – PH renders services to certain patients under contractual arrangements with the Medicare and Medi-Cal programs and various health maintenance and preferred provider organizations. The Medicare program generally pays a prospectively determined fee for services rendered to Medicare patients. Additionally, Medicare reimburses PH for certain inpatient services (primarily mental health unit services) on the basis of costs incurred. The Medi-Cal program provides for payment on a prospectively negotiated contractual rate per day, percentage of charges for services rendered, or capitated payment arrangement.

Revenue from the Medicare and Medi-Cal programs inclusive of risk (capitated) and non-risk managed care programs, accounted for approximately 52% and 54% of PH's net patient service revenue for the years ended June 30, 2019 and 2018, respectively.

Third-party cost reports for the Medicare program have been settled through the year ended June 30, 2015, with the exception of PMC Escondido's fiscal years 2011 and 2013 reports which are pending administrative review by Centers for Medicare & Medicaid Services (CMS). The cost reports for the Medi-Cal program have been settled through the year ended June 30, 2015 for Escondido, and through the year ended June 30, 2017 for Poway. Results of cost report settlements as well as estimates for settlements of all years through 2019 have been reflected in the accompanying financial statements.

As of June 30, 2019 and 2018, estimated third-party settlements resulted in a receivable of $42,141 and $28,613, respectively, and a liability of $768 and $1,811, respectively.

Laws and regulations governing Medicare and Medi-Cal programs are 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. During the years ended June 30, 2019 and 2018, PH settled various prior-year cost reports and appeal issues. These settlements and normal estimation differences between subsequent cash collections on patient accounts receivable resulted in approximately $3,901 and $9,140 of additional revenues for the years ended June 30, 2019 and 2018, respectively, which was included in net patient service revenue in the accompanying statements of revenue, expenses, and changes in net position.

Third-party reimbursement programs – *Public hospital redesign and incentives in Medi-Cal program (PRIME or the Program)* – The program was approved via the California's Section 1115(a) demonstration waiver, titled "California's Medi-Cal 2020 Demonstration." The PRIME program intends to close the gap by incentivizing hospitals to identify critical objectives to improve delivery of care for Medi-Cal beneficiaries. The Program is effective beginning January 1, 2016, and is a five-year program. The program has both reporting metrics as well as performance metrics. Revenue is recognized based on approval from CMS for the achievement of reporting metrics and when metrics are achieved for the performance metrics component.

Note 3 – Net Patient Service Revenue, Third-Party Reimbursement Programs, and Non-Operating Revenue (continued)

Medi-Cal managed care rate range intergovernmental transfer (IGT) – The Affordable Care Act (ACA) recognized the formation and maintenance of a network of primary care providers to service Medi-Cal Managed Care plans would require funding assistance. IGT is a payment methodology to partially fund the gap between what Medi-Cal Managed Care plans pay and the full cost of providing the service.

Senate Bill 239 quality assurance fee (QAF) supplemental payment – A state-legislated supplemental program that distributed funds to hospitals based on the volume of care to Medi-Cal funded patients. The intention is to strengthen the ability of hospitals to meet the increased demand resulting from implementing programs, service, and capital required by ACA.

QAF managed care funds – part of the hospital QAF – Under the California Hospital Fee Program, PH receives net supplemental funds under a managed care methodology.

Assembly Bill 113 Medi-Cal rate stabilization – A state-legislated program which provides a cost supplement for Medi-Cal Managed Care Seniors and Persons with Disabilities.

Assembly Bill 915 outpatient supplement payment – This bill provides for the payment of a supplemental reimbursement to acute care hospitals owned by certain public entities that provide outpatient services to Medi-Cal beneficiaries. The state legislated a supplemental reimbursement for uncompensated Medi-Cal Fee-For-Service (FFS) outpatients. PH receives 50% of reported uncompensated costs.

The following table summarizes amounts recognized as net patient service revenue from the various state supplemental funding programs and transfer agreements available to PH for the years ended June 30, 2019 and 2018, respectively, (in thousands):

	2019	2018
PRIME	$ 8,265	$ 10,168
Managed care rate range IGT	24,277	22,302
Quality assurance fee (QAF)	32,661	9,327
Medi-Cal rate stabilization	2,951	5,173
Outpatient supplemental payment	3,854	9,197
Totals	$ 72,008	$ 56,167

With respect to the above described programs, revenue is recognized when management is reasonably assured all performance and satisfaction of obligations have been met, the amount of revenue is available, and has been considered in estimating the amount of revenue to be recognized.

Note 4 – Cash and Cash Equivalents and Investments

The State of California Government Code (the Government Code) authorizes PH to invest unrestricted and board-designated assets in obligations of the U.S. Treasury and certain U.S. government agencies, obligations of the State of California and local government entities bankers' acceptances, commercial paper, certificates of deposit, repurchase agreements, and mortgage securities. Certain of these investments may be purchased only in limited amounts and limited maturity dates, as defined in the Government Code.

PH's bond indenture agreements authorize trustee-held assets to be invested in obligations of the U.S. Treasury and certain U.S. government agencies, repurchase agreements, and obligations of financial institutions meeting certain criteria defined in the indentures.

The California State Treasury makes available the Local Agency Investment Fund (LAIF) through which local governments may pool investments. Each governmental entity may invest up to $65,000 of unrestricted monies in the fund and an unlimited amount of qualified bond proceeds. PH had invested $63,464 and $63,172 of unrestricted funds in this fund as of June 30, 2019 and 2018, respectively. PH also had invested $10,088 and $9,925 in jointly managed funds under an escrow agreement with the City of Escondido as of June 30, 2019 and 2018, respectively. Investments in the LAIF are highly liquid, as deposits can be converted to cash within 24 hours without loss of interest. PH is a voluntary participant in the LAIF. The fair value of PH's investment in this pool is reported in the accompanying statements of net position at amounts based upon PH's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis and therefore is excluded from the fair value hierarchy.

As of June 30, 2019 and 2018, PH had the following investments (in thousands):

	2019	2018
Investments - current	$ 162,822	$ 150,924
Restricted cash and investments - current	36,193	31,817
Restricted cash and investments - noncurrent	88,638	100,041
Total	$ 287,653	$ 282,782

Note 4 – Cash and Cash Equivalents and Investments (continued)

As of June 30, 2019 and 2018, PH had investments by type and maturity as follows (in thousands):

	2019		
		Investment Maturities (in Years)	
Investment Type	Fair Value	Less Than 1	1-5
External investment pool - LAIF	$ 73,552	$ 73,552	$ -
U.S. government bonds	15,041	7,746	7,295
U.S. treasury bills	22,564	3,944	18,620
Corporate bonds	15,658	2,594	13,064
Money market mutual funds	160,838	160,838	-
Total	$ 287,653	$ 248,674	$ 38,979

	2018		
		Investment Maturities (in Years)	
Investment Type	Fair Value	Less Than 1	1-5
External investment pool - LAIF	$ 73,095	$ 73,095	$ -
U.S. government bonds	17,127	4,027	13,100
U.S. treasury bills	19,726	1,843	17,883
Corporate bonds	15,029	3,376	11,653
Money market mutual funds	157,805	157,805	-
Total	$ 282,782	$ 240,146	$ 42,636

GASB Statement No. 72, *Fair Value Measurement and Application,* defines fair value as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability.

The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk.

Note 4 – Cash and Cash Equivalents and Investments (continued)

In addition to defining fair value, this guidance expands the disclosure requirements around fair value and establishes a fair value hierarchy for valuation inputs. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which are determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the measurement date.

Level 2 – Pricing inputs are based on quoted market prices for similar instruments in active markets, quoted prices for identical or similar instruments in inactive markets, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Financial assets and liabilities in this category generally include asset-backed securities, corporate bonds and loans, municipal bonds, and interest rate swap instruments.

Level 3 – Pricing inputs are generally unobservable for the assets or liabilities and include situations where there is little, if any, market activity for the investment. The inputs into the determination of the fair value require management's judgment or estimation of assumptions that market participants would use in pricing the assets or liabilities. The fair values are therefore determined using factors that involve considerable judgment and interpretations, including but not limited to private and public comparables, third party appraisals, discounted cash flow models, and fund manager estimates.

Marketable securities and financial instruments – Where quoted market prices are available in an active market, securities or instruments are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated using pricing models, quoted prices of securities or instruments with similar characteristics, or discounted cash flows. These securities or instruments are classified within Level 2 of the valuation hierarchy. In certain cases, where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the valuation hierarchy.

Note 4 – Cash and Cash Equivalents and Investments (continued)

The following table summarizes PH's assets and liabilities measured at fair value on a recurring basis as of June 30, 2019 and 2018, (in thousands):

	2019			
	Total	Level 1	Level 2	Level 3
Investments				
Money market mutual funds	$ 160,838	$ 160,838	$ -	$ -
U.S. government bonds	15,041	-	15,041	-
U.S. treasury bills	22,564	22,564	-	-
Corporate bonds	15,658	-	15,658	-
	214,101	$ 183,402	$ 30,699	$ -
Investments not subject to the fair value hierarchy:				
State investment pool - LAIF	73,552			
Total investments	$ 287,653			
Liabilities				
Interest rate swap	$ (25,541)	$ -	$ (25,541)	$ -

	2018			
	Total	Level 1	Level 2	Level 3
Investments				
Money market mutual funds	$ 157,805	$ 157,805	$ -	$ -
U.S. government bonds	17,127	-	17,127	-
U.S. treasury bills	19,726	19,726	-	-
Corporate bonds	15,029	-	15,029	-
	209,687	$ 177,531	$ 32,156	$ -
Investments not subject to the fair value hierarchy:				
State investment pool - LAIF	73,095			
Total investments	$ 282,782			
Liabilities				
Interest rate swap	$ (18,971)	$ -	$ (18,971)	$ -

There are many factors affecting the value of investments. Some, such as interest rate risk, credit risk, concentration of credit risk, and custodial credit risk, may affect both equity and fixed income securities.

Equity and debt securities respond to such factors as economic conditions, individual company earnings performance, and market liquidity while fixed income securities are particularly sensitive to credit risks and changes in interest rates.

Note 4 – Cash and Cash Equivalents and Investments (continued)

Interest rate risk – Interest rate risk is the risk that the value of fixed income securities will decline due to increasing interest rates. The terms of a debt investment may cause its fair value to be highly sensitive to interest rate changes. As a means of limiting exposure to fair value losses arising from increasing interest rates, PH's investment policy, as per statutory requirements, limits the term of any investment to a maturity not exceeding five years.

Credit risk – Fixed income securities are subject to credit risk, which is the chance that an issuer will fail to pay interest or principal in a timely manner or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. Certain fixed income securities, including obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have credit risk. State law limits PH's investment in commercial paper, corporate bonds, and bond mutual funds with an "A" rating issued by nationally recognized statistical rating organizations. PH has no investment policy that would further limit investment choices. As of June 30, 2019 and 2018, PH's investments, excluding U.S. government obligations, consisted of the following: corporate bond investments rated "A" or better by Standard & Poor's (S&P) and Moody's Investors Service (Moody's), U.S. Government Agency investments rated "AA+" by S&P and "AAA" by Moody's, and PH's investments in the LAIF, which were not rated.

Concentration of credit risk – Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers, thereby exposing PH to greater risks resulting from adverse economic, political, regulatory, geographic, or credit developments, such as the LAIF, are not considered subject to concentration of credit risk. In accordance with state law, no more than 5% of total investments may be invested in the securities of any one issuer, except obligations of the U.S. government, no more than 10% may be invested in any one mutual fund, and no more than 30% may be invested in bankers' acceptances of any one commercial bank.

Investments in any one issuer (other than U.S. treasury securities and external investment pools) that represent 5% or more of the total investments as of June 30, 2019 and 2018, was as follows (in thousands):

		2019		2018	
Investment	Investment Type	Fair Value	Percentage of Total Investments	Fair Value	Percentage of Total Investments
U.S. Bank, Trustee	First American Govt Oblig Fund CL D	$ 65,746	23%	$ 77,331	27%
Wells Fargo Advantage Government Money Market	U.S. Government Money Market Funds	36,042	13%	31,555	11%
Fidelity Investments	FIMM-Treasury Port Instl CL 2644	45,756	16%	36,146	13%

Custodial credit risk – investments – All of PH's investments are insured or registered or held by PH's agent in the agent's nominee name, with subsidiary records listing PH as the legal owner. For these reasons, PH is not exposed to custodial credit risk for its investments.

Note 4 – Cash and Cash Equivalents and Investments (continued)

Custodial credit risk – deposits – Custodial credit risk is the risk that in the event of a bank failure, PH's deposits may not be returned to it. PH does not have a policy for custodial credit risk. As of June 30, 2019 and 2018, PH's bank balances totaled $52,250 and $50,449, respectively, and were not exposed to custodial credit risk, as the uninsured deposits are with financial institutions that are individually required by state law to have government deposits collateralized at a rate of 110% of the deposits. Such collateral is considered to be held in PH's name. Arch maintains bank deposit accounts that are insured by the Federal Deposit Insurance Corporation (FDIC) up to a limit of $250 per depositor. Arch had cash balances of $1,671 and $1,330 that were above the insured limit at June 30, 2019 and 2018, respectively.

Investment income – Investment income for the years ended June 30 consisted of the following (in thousands):

	2019	2018
Interest, dividends, and realized gains on sale of investments	$ 4,700	$ 1,475
Net increase (decrease) in fair value of investments	1,204	(1,294)
Total	$ 5,904	$ 181

Note 5 – Concentrations of Credit Risk

PH grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of gross receivables from patients and third-party payors as of June 30, 2019 and 2018, was as follows:

	2019	2018
Medicare	16%	19%
Medi-Cal	13%	9%
HMO/PPO/commercial*	62%	62%
Patient	6%	5%
Others	3%	5%
Total	100%	100%

* In addition to various commercial insurance plans, this category includes Medi-Cal HMOs and Medicare Advantage HMOs

Note 6 – Capital Assets

A summary of changes in capital assets for the years ended June 30, 2019 and 2018, was as follows (in thousands):

	Balance as of June 30, 2018	Additions	Disposals	Transfers	Balance as of June 30, 2019
Land improvements	$ 80,342	$ -	$ -	$ -	$ 80,342
Buildings and leasehold improvements	1,125,540	165	(423)	2,912	1,128,194
Equipment	294,935	11,306	(6,401)	812	300,652
Land	60,715	-	-	-	60,715
Construction in progress	44,014	7,512	(7,220)	(3,724)	40,582
	1,605,546	18,983	(14,044)	-	1,610,485
Less accumulated depreciation and amortization	(556,405)	(43,726)	5,779	-	(594,352)
Capital assets - net	$ 1,049,141	$ (24,743)	$ (8,265)	$ -	$ 1,016,133

	Balance as of June 30, 2017	Additions	Disposals	Transfers	Balance as of June 30, 2018
Land improvements	$ 80,342	$ -	$ -	$ -	$ 80,342
Buildings and leasehold improvements	1,122,495	147	(47)	2,945	1,125,540
Equipment	295,163	6,473	(9,274)	2,573	294,935
Land	61,912	-	(1,197)	-	60,715
Construction in progress	33,408	16,124	-	(5,518)	44,014
	1,593,320	22,744	(10,518)	-	1,605,546
Less accumulated depreciation and amortization	(519,289)	(44,781)	7,665	-	(556,405)
Capital assets - net	$ 1,074,031	$ (22,037)	$ (2,853)	$ -	$ 1,049,141

Construction commitments outstanding as of June 30, 2019, were $273.

Note 7 – Investment in and Amounts Due from Affiliated Entities

During fiscal year 2007, PH entered into a partnership agreement with PDP Pomerado, LLC in exchange for a ground lease agreement. During fiscal year 2010, the partnership with PDP Pomerado, LLC was terminated and the ground lease agreement was transferred to NHP/PMP Pomerado, LLC. In conjunction with the termination of the partnership, PDP Pomerado, LLC was dissolved and its assets were liquidated. PH received proceeds of $6,279 for its interest in PDP Pomerado, LLC, which was recorded as unearned revenue as it was attributed to the difference in contractual lease payments and the fair value of lease payments. Unamortized unearned revenue of $7,009 and $7,115 included in deferred inflow of resources in the accompanying statements of net position as of June 30, 2019 and 2018, respectively, is recognized as income over the remaining term of the ground lease agreement, which expires in April 2061, and has two ten-year options to renew at $1 per year. The renewal is considered inevitable.

Note 7 – Investment in and Amounts Due from Affiliated Entities (continued)

In October 2017, PH entered into an Investment Interests Purchase Agreement, whereby Arch conveyed 100% of its interest in PHS-PAM Holdings, Inc. (PHS-PAM) to PH. PH purchased 1,000 or 100% of the issued and outstanding shares of PHS-PAM Holdings, Inc. which owns 50% of PAM and 50% of PAM-SD. The remaining 50% ownership interests in PAM and PAM-SD are held by Arch and or its subsidiaries. PH paid $2,500 via PHS-PAM for its 50% interest in PAM-SD. This investment was eliminated in the financial statements.

PH's investment in affiliated entities, which are generally accounted for under the equity method because PH does not control the entities, was $5,870 and $5,961 at June 30, 2019 and 2018, respectively. The total income from PH's investment in affiliates was $908 and $1,273 for the years ended June 30, 2019 and 2018, respectively.

Note 8 – Related Organizations

Palomar Health Foundation – Palomar Health Foundation (the Foundation) is a charitable nonprofit organization created to provide assistance and support for PH. The Foundation is a separately governed organization. Its financial position, results of operations and cash flows are not included in the accompanying financial statements.

The Foundation provides a funding source for various programs on behalf of PH. Funding for these programs provided by the Foundation totaled $1,310 and $4,448 for the years ended June 30, 2019 and 2018, respectively.

PH has entered into a management services agreement (MSA) with the Foundation, whereby PH provides administrative support to the Foundation. Support provided to the Foundation totaled $1,651 and $1,490 for the years ended June 30, 2019 and 2018, respectively.

MSA renewed on December 31, 2016, and expiring on June 30, 2017, PH provided a line of credit to the Foundation with a $5,000 limit with interest at 2.5% above LIBOR. The Ninth Amendment to the MSA was signed on June 30, 2017, extending the LOC through June 30, 2018, and increasing the credit limit to $8,000. There were no amounts outstanding on the line of credit as of June 30, 2019 or 2018. The Tenth Amendment to the MSA was signed on December 19, 2018, to extend the LOC through June 30, 2019. The Eleventh Amendment to the MSA is expected to be signed in fiscal year 2020 to extend the LOC through June 30, 2020, with no change in the $8,000 credit limit.

Note 8 – Related Organizations (continued)

An unaudited summary of the Foundation's assets, liabilities, and net assets as of June 30, 2019 and 2018, was as follows:

	2019	2018
Assets	$ 7,595	$ 7,702
Liabilities	$ 1,274	$ 1,145
Net assets	6,321	6,557
Total liabilities and net assets	$ 7,595	$ 7,702

PIMG, Inc. – In April 2010, Arch entered into a 25-year professional services agreement with PIMG, Inc. (PIMG) under which PIMG provides professional medical services to patients seeking services from and enrolled with Arch. For the years ended June 30, 2019 and 2018, PIMG provided professional services to Arch in the amounts of $11,967 and $11,855, respectively. Any amounts advanced are to be repaid upon Arch's request and do not bear interest. There are no outstanding amounts at June 30, 2019 and 2018, respectively.

Pacific Accountable Care, LLC – In April, 2016, Arch formed PAC, a partnership with Medicare FFS participants, to develop an ACO with the intent to manage, coordinate, and promote accountability for the quality, patient safety, cost and overall care of 12,000 Medicare patients with Arch as the sole member. In January 2017, CMS awarded PAC a Track 1 MSSP contract for calendar years January 1, 2017 through December 31, 2019. PAC is eligible for payments from CMS if able to achieve medical cost savings as compared to predetermined benchmarks. As a Track 1 MSSP, PAC has no risk with CMS for any increase in medical cost. For FY18, PAC recorded a receivable of $3,946 for its share of the 2017/2018 plan year savings with a related payable of $921 due to the CMS approved physicians participating in the PAC ACO. There are no outstanding amounts at June 30, 2019.

Pacific Accountable Management, LLC and Pacific Accountable Management San Diego, LLC – PAM and PAM-SD operated as management service organizations (MSO) and provided administrative and billing services to Arch during the year ended June 30, 2018. PH and Arch collectively hold 100% of PAM and PAM-SD and closed operations of both entities in July 2018.

Note 9 – Long-Term Debt

The following is a summary of long-term debt transactions for PH for the years ended June 30, 2019 and 2018, (in thousands):

	Balance June 30, 2018	Additions	Reductions	Balance June 30, 2019	Amounts Due within One Year
Bonds payable:					
Series 2017 Refunding Revenue Bonds	$ 168,646	$ -	$ (658)	$ 167,988	$ -
Series 2017 Certificates of Participation	61,378	-	(1,005)	60,373	985
Series 2016 Refunding Revenue Bonds	269,770	-	(6,860)	262,910	5,755
Series 2016A&B General Obligation Bonds	236,862	-	(3,114)	233,748	1,610
Series 2010A General Obligation Bonds	65,566	-	(31)	65,535	-
Series 2009A General Obligation Bonds	113,292	-	(222)	113,070	3,400
Series 2007A General Obligation Bonds	52,973	-	(3,845)	49,128	4,090
Series 2006 Certificates of Participation	155,475	-	(5,795)	149,680	6,050
Accrued interest on capital appreciation bonds	175,394	19,677	-	195,071	7,150
Note payable	339	-	(289)	50	14
Capital leases	432	-	(67)	365	111
Total long-term debt	$ 1,300,127	$ 19,677	$ (21,886)	$ 1,297,918	$ 29,165

	Balance June 30, 2017	Additions	Reductions	Balance June 30, 2018	Amounts Due within One Year
Bonds payable:					
Series 2017 Refunding Revenue Bonds	$ -	$ 168,646	$ -	$ 168,646	$ -
Series 2017 Certificates of Participation	-	61,378	-	61,378	935
Series 2016 Refunding Revenue Bonds	276,460	-	(6,690)	269,770	5,530
Series 2016A&B General Obligation Bonds	242,245	-	(5,383)	236,862	1,520
Series 2010 Certificates of Participation	155,571	-	(155,571)	-	-
Series 2010A General Obligation Bonds	65,597	-	(31)	65,566	-
Series 2009A General Obligation Bonds	113,514	-	(222)	113,292	-
Series 2007A General Obligation Bonds	56,431	-	(3,458)	52,973	3,714
Series 2006 Certificates of Participation	161,065	-	(5,590)	155,475	5,825
Accrued interest on capital appreciation bonds	152,001	23,393	-	175,394	1,971
Note payable	76	263	-	339	13
Capital leases	141	291	-	432	73
Total long-term debt	$ 1,223,101	$ 253,971	$ (176,945)	$ 1,300,127	$ 19,581

Note 9 – Long-Term Debt (continued)

The terms and due dates of PH's long-term debt as of June 30, 2019 and 2018, are as follows:

- Series 2017 Refunding Revenue Bonds (Series 2017 Bonds) bear interest at 5.00%, with interest payments due semi-annually. Principal payments are due in annual amounts ranging from $15,785 in fiscal year 2041 to $22,405 in fiscal year 2048. The Series 2017 Bonds are net of unamortized original issue premium of $16,527 and $17,186 at June 30, 2019 and 2018, respectively, and are collateralized by PH revenues as defined in the indenture agreement. The net unamortized loss on refunding is $18,843 and $19,594 at June 30, 2019 and 2018, respectively, and is included as deferred outflow of resources and amortized.

- Series 2017 Certificates of Participation (2017 COP) bear interest at rates between 4.00% to 5.00%, with interest payments due semiannually. Principal payments are due in annual amounts ranging from $935 in fiscal year 2019 to $3,450 in fiscal year 2048. The 2017 COP are net of unamortized original issue premium of $1,208 and $1,278 at June 30, 2019 and 2018, respectively, and are collateralized by PH revenues as defined in the indenture agreement.

- Series 2016 Refunding Revenue Bonds (Series 2016 Revenue Bonds) bear interest at rates between 3.00% to 5.00%, with interest payments due semiannually. Principal payments are due in annual amounts ranging from $5,360 in fiscal year 2018 to $27,440 in fiscal year 2040. The Series 2016 Revenue Bonds are net of unamortized original issue premium of $27,050 and $28,380 at June 30, 2019 and 2018, respectively, and are collateralized by PH revenues as defined in the indenture agreement. The net unamortized loss on refunding is $36,589 and $38,388 at June 30, 2019 and 2018, respectively, and is included as deferred outflow of resources and amortized.

- Series 2016A General Obligation Bonds (Series 2016A G.O. Bonds) bear interest at rates between 2.00% to 5.00%, with interest payments due semiannually. Principal payments are due in annual amounts ranging from $1,520 in fiscal year 2019 to $4,345 in fiscal year 2035. The Series 2016A G.O. Bonds are net of unamortized original issue premium of $8,633 and $9,205 at June 30, 2019 and 2018, respectively.

- Series 2016B General Obligation Bonds (Series 2016B G.O. Bonds) bear interest at rates between 2.00% to 5.00%, with interest payments due semiannually. Principal payments are due in annual amounts ranging from $1,615 in fiscal year 2018 to $19,305 in fiscal year 2038. The Series 2016B G.O. Bonds are net of unamortized original issue premium of $17,453 and $18,475 at June 30, 2019 and 2018, respectively. The net unamortized loss on refunding is $3,661 and $3,876 at June 30, 2019 and 2018, respectively, and is included as deferred outflow of resources and amortized.

- Series 2010 Certificates of Participation (2010 COP) were advance refunded on December 11, 2017, with proceeds from the issuance of the Series 2017 Bonds. Additional 2010 COP reserves were deposited in an escrow trust account held with the escrow agent to provide for all future debt service payments. As a result, the 2010 COP are considered to be defeased and the liability for these bonds has been removed from the statements of net position. PH refunded the Series 2010 COP to reduce its total debt service payments over the next 16 years and to obtain an economic gain of $16,678.

Note 9 – Long-Term Debt (continued)

- Series 2010A General Obligation Bonds (Series 2010A G.O. Bonds), accreted interest compounded at rates between 6.84% to 7.85% on $64,917 Capital Appreciation Bonds (CABs) with the first payment to bondholders due on August 1, 2034. Accreted interest compounds at 6.75% on $49,999 Convertible CABs with the first payment to bondholders also due on August 1, 2034. Principal payments are due in annual amounts ranging from $1,476 in fiscal year 2038 to $33,159 in fiscal year 2041. The Series 2010A G.O. Bonds are net of unamortized premium of $619 and $649 at June 30, 2019 and 2018, respectively.

- Series 2009 Certificates of Participation (2009 COP) were advance refunded on October 20, 2016, with proceeds from the issuance of the Series 2016 Revenue Bonds. Additional 2009 COP reserves were deposited in an escrow trust account held with the escrow agent to provide for all future debt service payments. As a result, the 2009 COP is considered to be defeased and the liability for these bonds has been removed from the statements of net position. PH refunded the Series 2009 COP to reduce its total debt service payments over the next 23 years by $48,600 and to obtain an economic gain of $33,200.

- Series 2009A General Obligation Bonds (Series 2009 G.O. Bonds), accreted interest compounded at rates between 6.84% to 9.00% on $50,001 CABs with the first payment to bondholders on August 1, 2019. Accreted interest compounded at 7% on $59,999 Convertible CABs with the first payment to bondholders on August 1, 2033. Principal payments are due in annual amounts ranging from $327 in fiscal year 2021 to $18,868 in fiscal year 2039. The Series 2009 G.O. Bonds are net of unamortized premium of $3,071 and $3,293 at June 30, 2019 and 2018, respectively.

- Series 2007A General Obligation Bonds (Series 2007A G.O. Bonds), $66,083 CABs are compounded at interest rates between 3.67% to 4.92% with the first payment paid to bondholders on August 1, 2011. Principal payments are due in annual amounts ranging from $557 in fiscal 2012 to $6,585 in fiscal 2027. The Series 2007A G.O. Bonds are net of unamortized premium of $580 and $711 at June 30, 2019 and 2018, respectively. A portion of the Series 2007A G.O. Bonds, the current interest bonds, was advance refunded on October 27, 2016, with proceeds from the issuance of the Series 2016B G.O. Bonds. As a result, the Series 2007A G.O. current interest bonds are considered to be defeased and the liability for these bonds has been removed from the statements of net position. PH refunded the 2007A G.O. Bonds to reduce its total debt service payments over the next 21 years by $50,200 and to obtain an economic gain of $38,200.

- Series 2006 Certificates of Participation (2006 COP), were issued as auction rate securities, whereby the interest rate for each series is generally determined during successive seven-day auction periods (a portion of the Series 20016 COP refunded the Series 1993 Insured Refunding Revenue Bonds). In addition, PH entered into an interest rate swap agreement with Citibank, N.A., New York, with respect to the 2006 COP in a notional amount of $180,000 (the Swap Agreement) (see Note 10). Interest on the 2006 COP is accrued at 3.22%, which is the fixed rate to be paid by PH under the Swap Agreement; interest payments are due semiannually and principal payments are due annually in amounts ranging from $5,500 in fiscal year 2017 to $12,350 in fiscal year 2037. The 2006 COP are net of unamortized loss on refunding of $70 and $100 at June 30, 2019 and 2018, respectively, and are collateralized by PH revenues as defined in the indenture agreement.

Note 9 – Long-Term Debt (continued)

- The 2005A General Obligation Bonds (2005A G.O. Bonds), were redeemed on October 27, 2016, with proceeds from the issuance of the Series 2016B G.O. Bonds. The liability for these bonds has been removed from the statement of net position as of June 30, 2018.

All the G.O. Bonds represent the general obligation of PH, in an amount sufficient to service the obligation, and PH has the power and is obligated to cause to be levied and collected by the County of San Diego annual *ad valorem* taxes upon all property within PH's boundaries subject to taxation by PH for payment of the principal of and interest on the bonds when due. However, PH is legally required to repay the G.O. Bonds if collected *ad valorem* taxes are insufficient.

PH is required to maintain certain debt covenants (Days Cash on Hand, Maximum Annual Debt Service Coverage, and Cushion Ratio) under its indenture agreements for the COP. The covenants stipulate that in the event of underachievement, the Insurers may require PH to call in mutually agreed-upon consultants to perform mutually agreed-upon scope of services to assist PH in achieving the covenants.

At June 30, 2019 and 2018, long-term capital leases, net of current portion, amounted to $255 and $359, respectively. Related net book value of leased equipment totaled $387 and $478, and depreciation expense totaled $81 and $100 for the years ended June 30, 2019 and 2018, respectively.

The estimated fair value of PH's long-term debt was approximately $1,482,767 and $1,431,066 as of June 30, 2019 and 2018, respectively, based on quotations from independent third parties.

Estimated future principal and interest payments on long-term debt, including capital leases, as of June 30, 2019, are as follows (in thousands):

	Principal	Interest	Total
Years ending June 30			
2020	$ 22,015	$ 47,222	$ 69,237
2021	19,884	50,275	70,159
2022	21,222	54,330	75,552
2023	22,533	55,314	77,847
2024	23,873	56,536	80,409
2025 - 2029	149,216	296,675	445,891
2030 - 2034	235,339	308,576	543,915
2035 - 2039	275,018	240,239	515,257
2040 - 2044	162,386	114,352	276,738
2045 - 2048	96,289	9,655	105,944
Sub-total	1,027,775	1,233,174	2,260,949
Net premium on bonds	75,072	-	75,072
Accrued interest on capital appreciation bonds	195,071	-	195,071
Total	$ 1,297,918	$ 1,233,174	$ 2,531,092

Note 10 – Interest Rate Swap

In 2006, PH entered into the Swap Agreement as a means to lower its borrowing costs on the 2006 COP (see Note 9) when compared against fixed-rate bonds at the time of issuance. The Swap Agreement was effective December 28, 2006, with an initial notional amount of $180,000 for the 2006 COP and terminates on November 1, 2036, simultaneously with the maturity of the 2006 COP.

Under the Swap Agreement, PH pays the swap provider amounts based on a fixed interest rate of 3.218%, and the swap provider pays to PH amounts based on 56% of the British Banker's Association 30-day London Interbank Offered Rate, LIBOR, plus 0.23% (1.57% and 1.40% at June 30, 2019 and 2018, respectively).

The significant terms of the Swap Agreement are as follows:

Corresponding bond series	Series 2006 Certificate of Participation bonds
Swap type	Fixed income
Initial notional amount	$ 180,000
Notional amount as of June 30, 2019	$ 149,750
Notional amount as of June 30, 2018	$ 155,575
Effective date	December 28, 2006
Termination date	November 1, 2036
Final bond maturity	November 1, 2036
PH pays	3.218 %
Cash payments remitted by PH for year ended June 30, 2019	$ 2,531
PH receives	56% of 30-day LIBOR + 0.23%
Swap fair value as of June 30, 2019	$ (25,541)
Change in fair value for the year ended June 30, 2019	$ (6,570)
Classification	Liability

Fair value – As of June 30, 2019 and 2018, the swap had a negative fair value of $25,541 and $18,971, respectively, developed by a mark-to-market pricing service using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement of the swap. The negative fair value of the swap is reported in the accompanying statements of net position as a long-term liability. The change in the fair value of the swap is reported in the accompanying statements of revenue, expenses, and changes in net position as unrealized gain (loss) on interest rate swap.

Note 10 – Interest Rate Swap (continued)

Credit risk – PH seeks to limit its counterparty risk by contracting only with highly rated entities. As of June 30, 2019, the counterparty of the interest rate swap was rated “Aa3” by Moody’s, “A+” by S&P, and “A+” by Fitch Ratings (Fitch). To mitigate the potential for credit risk, under the terms of the Swap Agreement, if the counterparty’s credit quality falls below (1) Moody’s rating of Baa2, (2) S&P’s rating of BBB, or (3) Fitch’s rating of BBB, the fair value of the swap will be collateralized by the counterparty with cash and/or treasury securities.

Basis risk – PH is exposed to basis risk on its Swap Agreement because the variable rate payments received by PH on the instruments are based on a rate or index other than the interest rate paid on its variable rate debt.

Termination risk – The swap uses the International Swaps & Derivatives Association Master Agreement (the Master Agreement), which includes standard termination events such as failure to pay and bankruptcy. The Master Agreement also includes an “additional termination event.” The Master Agreement can be terminated if, at any time, a relevant credit rating with respect to a party declines below the termination level or is withdrawn, or if any party has no relevant rating but was previously rated by such rating agency. The termination levels are (1) Moody’s rating of Baa2, (2) S&P rating of BBB, and (3) Fitch rating of BBB.

The negative swap fair value in the accompanying statements of net position approximates the termination payment that would be owed by PH to the swap counterparty if the swap was terminated. The payments from PH to the swap counterparty are insured by Assured Guaranty. This insurance provides protection to the swap counterparty in the event PH fails to make payments due under the swap. Under the terms of the Swap Agreement, an “insurer event” will occur if both Moody’s and S&P’s ratings for Assured Guaranty fall below the A category. If an insurer event happens, PH would be required to post collateral by a first priority perfected security interest in the gross revenues of PH. Assured Guaranty was rated A2 by Moody’s with a stable outlook effective August 2019.

Note 11 – Operating Leases

PH leases certain office space and equipment under operating leases. Lease expense on all such leases for the years ended June 30, 2019 and 2018, totaled $20,883 (including $67 in non-operating expense) and $19,319 (including $387 in non-operating expense), respectively. PH also leases office space to others which qualify as operating leases. Future minimum lease payments and receipts under office space and equipment leases as of June 30, 2019, were as follows (in thousands):

	Lease Payments	Lease Receipts
Years ending June 30		
2020	$ 13,360	$ 1,024
2021	13,235	1,026
2022	11,726	1,039
2023	7,375	611
2024	6,988	512
2025-2029	26,579	1,641
2030-2034	17,399	1,510
2035-2039	17,397	1,250
2040-2081	31,664	625
Total	$ 145,723	$ 9,238

Note 12 – Deferred Annuity Contracts

PH offers its employees a deferred compensation plan, which has an employer-match component created in accordance with Internal Revenue Code (IRC) Section 457. Employees who elect to participate in the plan make contributions through a reduction in salary. All participating employees manage their contribution and investment choices through a funding agency selected by PH.

The investments of PH's IRC Section 457 plan and earnings thereon are held in trust for the exclusive benefit of the plan participants and their beneficiaries. The IRC Section 457 plan and earnings are not subject to claims of PH's general creditors. Accordingly, the accompanying statements of net position do not include the funds deposited with financial institutions pursuant to deferred annuity contracts.

Note 13 – Retirement Plan

PH sponsors a defined contribution retirement plan under which benefits are limited to amounts accumulated from total contributions by PH and by participating employees, plus earnings thereon. Generally, all employees with one year of service are eligible to participate. For the years ended June 30, 2019 and 2018, contributions under the retirement plan by PH were 6% of covered employees' basic compensation. Contributions are funded as accrued. Total PH contributions expensed for the years ended June 30, 2019 and 2018, were $18,966 and $18,333, respectively.

Note 14 – Postemployment Healthcare Plan

The Company accounts for its postemployment healthcare plan under GASB Codification Section P50, *Postemployment Benefits Other Than Pensions-Employer Reporting*.

Plan description and funding policy – PH's Postemployment Healthcare Plan (the Plan) is a single-employer defined benefit healthcare plan administered by Discovery Benefits. The Plan provides medical and dental insurance benefits to qualified postemployment participants on a gap coverage basis. Coverage is limited to those employees who have provided 10 years of consecutive service, are below the age of 65, and do not receive coverage from other sources. The contribution requirements of the Plan members and PH are established and may be amended by the Board of Directors. The required contribution is based on estimated pay-as-you-go financing requirements.

Employees covered by benefit terms – As of the current and prior valuation dates, the following employees were covered by the Plan:

	July 1, 2018	July 1, 2016
Inactive employees currently receiving benefit payments	8	12
Active employees	3,634	3,617
Total	3,642	3,629

Total OPEB liability – PH's total OPEB liability of $1,230 was measured as of June 30, 2019, and was determined by an actuarial valuation as of that date.

Actuarial assumptions and other inputs – The total OPEB liability in the June 30, 2019 actuarial valuation, is determined using the following actuarial assumptions and other inputs, applied to all periods included in the measurement, unless otherwise specified. The actuarial assumptions used in the June 30, 2019 valuation, were based on the results of an actuarial experience study for the period June 30, 2018 to June 30, 2019.

Inflation	2.50%
Salary Increases	3.00% - 18.50%, including inflation
Discount Rate	3.48%
Healthcare Cost Trend Rates	7% for 2019, 6.75% for 2020, 6.50% for 2021 and decreasing to an ultimate rate of 4% in 2031

The discount rate was based on Bond Buyer 20-Bond General Obligation Index. Mortality rates were based on the RP-2000. Combined mortality table rates projected with mortality improvement scale BB.

Note 14 – Postemployment Healthcare Plan (continued)

Changes in the total OPEB liability (in thousands):

	Year Ended June 30, 2019		Year Ended June 30, 2018	
Total OPEB liability - prior measurement date	$	1,193	$	1,176
Changes in total OPEB liability				
(a) Service cost		69		60
(b) Interest on the total OPEB liability		46		43
(c) Changes on benefit terms		(48)		-
(d) Differences between expected and actual experience		-		-
(e) Changes of assumptions or other inputs		34		(24)
(f) Benefit payments		(64)		(62)
Total OPEB liability - current measurement date	$	1,230	$	1,193
Covered-employee payroll	$	258,493	$	209,718
Total OPEB liability as a % of covered-employee payroll		0.48%		0.57%
Key information				
Valuation date		July 1, 2018		July 1, 2016
Reporting date		June 30, 2019		June 30, 2018
Measurement date		June 30, 2019		June 30, 2018
Discount rate as of the measurement date		3.48%		3.87%
Municipal bond index rate		3.48%		3.87%
Municipal bond index date		June 11, 2019		June 30, 2018

Sensitivity of the net OPEB liability to changes in the discount rate – The following presents PH's total OPEB liability using the final discount rate of 3.48%, and preliminary discount rate of 3.87% for June 30, 2019 and 2018 measurement dates, respectively, as well as what the total OPEB liabilities would be they were calculated using a discount rate that is one-percentage-point lower or one-percentage-point higher that the current rate (in thousands).

	June 30, 2019			June 30, 2018		
	1% Decrease 2.48%	Discount Rate 3.48%	1% Increase 4.48%	1% Decrease 2.87%	Discount Rate 3.87%	1% Increase 4.87%
Net OPEB liability	$ 1,323	$ 1,230	$ 1,145	$ 1,278	$ 1,193	$ 1,115

Note 14 – Postemployment Healthcare Plan (continued)

Sensitivity of the net OPEB liability to changes in the healthcare trend rates – The following presents PH's total OPEB liability using the current health trend rates, as well as what the total OPEB liability would be if it were calculated using healthcare trend rates that are one-percentage-point lower or one-percentage-point higher that the current healthcare trend rates (in thousands).

	June 30, 2019			June 30, 2018		
	1% Decrease 6.0% to 3.0%	Current 7.0% to 4.0%	1% Increase 8.0% to 5.0%	1% Decrease 5.5% to 3.0%	Current 6.5% to 4.0%	1% Increase 7.5% to 5.0%
Net OPEB liability	$ 1,114	$ 1,230	$ 1,364	$ 1,076	$ 1,193	$ 1,327

OPEB expense and deferred outflows of resources and deferred inflows of resources related to OPEB – For the fiscal year ended June 30, 2019, PH recognized OPEB expense of $42. At June 30, 2019, the deferred outflows of resources and deferred inflows of resources related to OPEB are as follows (in thousands):

	June 30, 2019			June 30, 2018		
	Deferred Outflows of Resources	Deferred Inflows of Resources	Net Amount	Deferred Outflows of Resources	Deferred Inflows of Resources	Net Amount
Differences between expected and actual experience	$ -	$ -	$ -	$ -	$ -	$ -
Changes of assumptions and other inputs	26	49	(23)	-	(18)	(18)
Total	$ 26	$ 49	$ (23)	$ -	$ (18)	$ (18)

Amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows (in thousands):

	Amount
Years ending June 30,	
2020	$ (9)
2021	(9)
2022	(4)
2023	(1)
2024	-
Thereafter	-
	$ (23)

Note 15 – Commitments and Contingencies

Legal matters – The health care industry is subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations, specifically those relating to the Medicare and Medi-Cal programs is subject to government review and interpretation, as well as regulatory actions. Claims for payment for services rendered to Medicare and Medi-Cal beneficiaries must meet applicable billing laws and regulations, which, among other things, require that the services are medically necessary, accurately coded, and sufficiently documented in the beneficiaries' medical records. Allegations concerning possible violations of regulations can result in the imposition of significant fines and penalties, as well as significant repayment of previously billed and collected revenues for patient services.

PH has ongoing efforts to comply with laws and regulations, to assess its prior compliance, and the potential impact of noncompliance. PH with its ongoing compliance program will continue to monitor, investigate, and correct any potential areas of noncompliance. No regulatory action has been asserted against PH to date, although such action could occur in the future.

PH is a party to certain other legal actions arising in the ordinary course of business. In the opinion of PH management, the liability, if any, under these claims is adequately covered by insurance. PH is insured for medical malpractice under a claims-made and reported policy.

PH is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; natural disasters; and employee health and accident benefits. Commercial insurance coverage is purchased for claims arising from such matters.

Workers' compensation program – Effective July 1, 2016, PH has contracted with Safety National Casualty Corporation to provide workers' compensation insurance coverage. PH is self-insured for the first $1,000 of each occurrence with a maximum limit of indemnity per occurrence of $1,000. At June 30, 2019 and 2018, estimated claims liabilities for workers' compensation recorded were $5,441 and $4,491, respectively.

Activity in PH's workers' compensation claims liability during the years ended June 30, 2019 and 2018, is summarized as follows (in thousands):

	2019	2018
BALANCE, beginning of the year	$ 4,491	$ 2,704
Current year claims incurred and changes in estimates for claims incurred in the prior year	4,223	4,873
Claims and expenses paid	(3,273)	(3,086)
BALANCE, end of year	5,441	4,491
Less current portion, included in other accrued liabilities	(2,377)	(2,007)
BALANCE, end of year, less current portion	$ 3,064	$ 2,484

Note 15 – Commitments and Contingencies (continued)

Comprehensive liability insurance coverage – PH is insured for comprehensive liability (professional liability, bodily injury and property damage liability, personal injury, advertising injury and discrimination liability, and employee benefit liability) under a claims-made policy, which covers asserted claims and incidents reported to the insurance carrier, and has a per-claim deductible of $100 for professional liability. PH's comprehensive liability insurance was renewed effective July 1, 2019, and the current policy expires on June 30, 2020. PH has reserved for estimated claims through 2015, including an estimate of IBNR. Such reserves remained unchanged at $2,463 from previous year and are recorded as other accrued liabilities in the accompanying statements of net position.

Effective July 1, 2019, PH withdrew its membership from its insurance carrier and has contracted with C.N.A. to provide comprehensive liability insurance. PH is self-insured for the first $1,000 for each claim and $10,000 in aggregate.

Activity in PH's comprehensive liability insurance coverage liability during the years ended June 30, 2019 and 2018, is summarized as follows (in thousands):

	2019	2018
BALANCE, beginning of the year	$ 2,463	$ 2,463
Current year claims incurred and changes in estimates	377	487
Claims and expenses paid	(377)	(487)
BALANCE, end of the year	$ 2,463	$ 2,463

Medicare Recovery Audit Contractor (RAC) program – PH is subject to the Medicare RAC Program, which is a program designed to identify improper Medicare payments-both underpayments and overpayments. RAC auditors are contracted by the CMS on a contingent fee basis, receiving a percentage of the improper overpayments and underpayments they recover from or return to providers. RAC audits resulted in recoupments of $0 and $30 for the years ended June 30, 2019 and 2018, respectively. There are currently no RAC audits in process nor are any reserves recorded at June 30, 2019, or 2018.

Seismic compliance – California Senate Bill (SB) 1953 requires hospital acute care buildings to meet more stringent seismic guidelines by 2020. PH's buildings are compliant with an SPC-2 rating and are eligible to render acute inpatient care until 2030.

Note 16 – Condensed Combining Information

A summary of the condensed combining information for PH and Arch as of June 30, 2019, is as follows (in thousands):

ASSETS AND DEFERRED OUTFLOW OF RESOURCES

CONDENSED COMBINING STATEMENT OF NET POSITION AS OF JUNE 30, 2019

	PH	Arch	PAM	PAM-SD	PAC	Eliminations	Total
Current assets	$ 437,978	$ 7,066	$ 404	$ 1,895	$ 126	$ (4,575)	$ 442,894
Capital assets - net	1,013,355	2,696	-	82	-	-	1,016,133
Noncurrent assets	104,974	1,110	-	-	-	(4,659)	101,425
Total assets	1,556,307	10,872	404	1,977	126	(9,234)	1,560,452
Deferred outflow of resources	59,093	-	-	-	-	-	59,093
Total assets and deferred outflow of resources	$ 1,615,400	$ 10,872	$ 404	$ 1,977	$ 126	$ (9,234)	$ 1,619,545
LIABILITIES, DERERRED INFLOW OF RESOURCES, AND NET POSITION							
Current liabilities	$ 149,624	$ 10,368	$ 2,308	$ -	$ 1,181	$ (4,979)	$ 158,502
Long-term liabilities	1,304,472	36	-	-	-	-	1,304,508
Total liabilities	1,454,096	10,404	2,308	-	1,181	(4,979)	1,463,010
Deferred inflow of resources - deferred revenue	7,822	-	-	-	-	-	7,822
Total liabilities and deferred inflow of resources	1,461,918	10,404	2,308	-	1,181	(4,979)	1,470,832
Invested in capital assets - net of related debt	(138,291)	2,646	-	82	-	-	(135,563)
Restricted	32,160	-	-	-	-	-	32,160
Unrestricted	259,613	(2,178)	(1,904)	1,895	(1,055)	(4,255)	252,116
Total net position	153,482	468	(1,904)	1,977	(1,055)	(4,255)	148,713
Total liabilities, deferred inflow of resources, and net position	$ 1,615,400	$ 10,872	$ 404	$ 1,977	$ 126	$ (9,234)	$ 1,619,545

Note 16 – Condensed Combining Information (continued)

PH is the sole corporate member of Arch and Arch is dependent upon PH for financial support. Arch received $16,382 and $20,640 in financial support for years ending June 30, 2019 and 2018, respectively.

Subsequent to June 30, 2019, Arch has received an additional $4,400 of financial support.

CONDENSED COMBINING STATEMENT OF REVENUE, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2019

	PH	Arch	PAM	PAM-SD	PAC	Elimination	Total
OPERATING REVENUE							
Net patient service revenue	$ 667,103	$ 27,658	$ -	$ -	$ (1,315)	$ -	$ 693,446
Shared risk revenue	70,901	11,432	-	-	-	(50)	82,283
Other revenue	11,477	2,098	(647)	-	-	647	13,575
PH Program revenue	-	1,936	-	-	-	(1,936)	-
Total operating revenue	749,481	43,124	(647)	-	(1,315)	(1,339)	789,304
OPERATING EXPENSES	690,057	62,678	518	(3)	(636)	(1,339)	751,275
DEPRECIATION AND AMORTIZATION	42,340	1,328	-	59	-	-	43,727
Total operating expenses	732,397	64,006	518	56	(636)	(1,339)	795,002
INCOME (LOSS) FROM OPERATIONS	17,084	(20,882)	(1,165)	(56)	(679)	-	(5,698)
NON-OPERATING INCOME (EXPENSE):							
Investment income	5,833	71	-	-	-	-	5,904
Unrealized gain on interest rate swap	(6,570)	-	-	-	-	-	(6,570)
Interest expense	(60,857)	(5)	(67)	-	-	-	(60,929)
Property tax revenue	37,942	-	-	-	-	-	37,942
Other - net	(6,663)	(4,641)	1,350	368	-	2,357	(7,229)
Total nonoperating expense - net	(30,315)	(4,575)	1,283	368	-	2,357	(30,882)
CHANGE IN NET POSITION	(13,231)	(25,457)	118	312	(679)	2,357	(36,580)
INTERFUND - ARCH HEALTH PARTNERS	(16,569)	16,569	-	-	-	-	-
NET POSITION - Beginning of year	183,281	9,358	(2,023)	1,666	(376)	(6,613)	185,293
NET POSITION - End of year	$ 153,481	$ 470	$ (1,905)	$ 1,978	$ (1,055)	$ (4,256)	$ 148,713

CONDENSED COMBINING STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2019 (dollars in thousands)

	PH	Arch	PAM	PAM-SD	PAC	Elimination	Total
CASH FLOWS FROM:							
Operating activities	$ 57,908	$ (14,428)	$ 1,126	$ (286)	$ 110	$ (2,224)	$ 42,206
Noncapital financing activities	17,609	-	(1,836)	-	-	1,836	17,609
Capital and related financing activities	(76,511)	14,507	(67)	286	-	388	(61,397)
Investing activities	2,167	71	-	-	-	-	2,238
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,173	150	(777)	-	110	-	656
CASH AND CASH EQUIVALENTS - Beginning of year	47,761	942	777	-	-	-	49,480
CASH AND CASH EQUIVALENTS - End of year	$ 48,934	$ 1,092	$ -	$ -	$ 110	$ -	$ 50,136

Note 16 – Condensed Combining Information (continued)

ASSETS AND DEFERRED OUTFLOW OF RESOURCES

CONDENSED COMBINING STATEMENT OF NET POSITION AS OF JUNE 30, 2018

	PH	Arch	PAM	PAM-SD	PAC	Eliminations	Total
Current assets	$ 412,667	$ 13,750	$ 3,026	$ 2,559	$ 3,947	$ (12,708)	$ 423,241
Capital assets - net	1,045,505	3,435	-	601	-	(400)	1,049,141
Noncurrent assets	116,766	2,456	2,512	-	-	(6,212)	115,522
Total assets	1,574,938	19,641	5,538	3,160	3,947	(19,320)	1,587,904
Deferred outflow of resources	61,858	-	-	-	-	-	61,858
Total assets and deferred outflow of resources	$ 1,636,796	$ 19,641	$ 5,538	$ 3,160	$ 3,947	$ (19,320)	$ 1,649,762
LIABILITIES, DERERRED INFLOW OF RESOURCES, AND NET POSITION							
Current liabilities	$ 141,653	$ 10,232	$ 5,844	$ 1,494	$ 4,323	$ (10,990)	$ 152,556
Long-term liabilities	1,303,921	51	1,717	-	-	(1,717)	1,303,972
Total liabilities	1,445,574	10,283	7,561	1,494	4,323	(12,707)	1,456,528
Deferred inflow of resources - deferred revenue	7,941	-	-	-	-	-	7,941
Total liabilities and inflow of resources	1,453,515	10,283	7,561	1,494	4,323	(12,707)	1,464,469
Invested in capital assets - net of related debt	(95,275)	3,372	-	601	-	(401)	(91,703)
Restricted	32,799	-	-	-	-	-	32,799
Unrestricted	245,757	5,986	(2,023)	1,065	(376)	(6,212)	244,197
Total net position	183,281	9,358	(2,023)	1,666	(376)	(6,613)	185,293
Total liabilities, deferred inflow of resources, and net position	$ 1,636,796	$ 19,641	$ 5,538	$ 3,160	$ 3,947	$ (19,320)	$ 1,649,762

CONDENSED COMBINING STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2018

	PH	**Arch**	**PAM**	**PAM-SD**	**PAC**	**Elimination**	**Total**
OPERATING REVENUE							
Net patient service revenue	$ 665,630	$ 27,371	$ -	$ -	$ 3,947	$ -	$ 696,948
Shared risk revenue	70,148	12,178	-	-	-	-	82,326
Other revenue	11,996	3,019	9,356	8,011	-	(17,488)	14,894
PH Program revenue	-	2,057	-	-	-	(2,057)	-
Total operating revenue	747,774	44,625	9,356	8,011	3,947	(19,545)	794,168
OPERATING EXPENSES	694,271	61,570	13,839	6,947	4,321	(19,700)	761,248
DEPRECIATION AND AMORTIZATION	43,205	1,150	-	426	-	-	44,781
Total operating expenses	737,476	62,720	13,839	7,373	4,321	(19,700)	806,029
INCOME (LOSS) FROM OPERATIONS	10,298	(18,095)	(4,483)	638	(374)	155	(11,861)
NON-OPERATING INCOME (EXPENSE):							
Investment income	131	50	-	-	-	-	181
Unrealized loss on interest rate swap	7,502	-	-	-	-	-	7,502
Interest expense	(64,386)	(6)	(51)	-	-	-	(64,443)
Property tax revenue	35,872	-	-	-	-	-	35,872
Other - net	(110,478)	14,779	(1)	1	(2)	97,668	1,967
Total nonoperating expense - net	(131,359)	14,823	(52)	1	(2)	97,668	(18,921)
NET (LOSS) INCOME BEFORE CAPITAL CONTRIBUTIONS	(121,061)	(3,272)	(4,535)	639	(376)	97,823	(30,782)
CAPITAL CONTRIBUTIONS	-	-	2,512	1,027	-	(3,539)	-
CHANGE IN NET POSITION	(121,061)	(3,272)	(2,023)	1,666	(376)	94,284	(30,782)
NET POSITION - Beginning of year	304,342	3,272	-	-	-	(91,539)	216,075
NET POSITION - End of year	$ 183,281	$ -	$ (2,023)	$ 1,666	$ (376)	$ 2,745	$ 185,293

Note 16 – Condensed Combining Information (continued)

CONDENSED COMBINING STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2018 (dollars in thousands)

	PH	Arch	PAM	PAM-SD	PAC	Elimination	Total
CASH FLOWS FROM:							
Operating activities	$ 126,246	$ (24,583)	$ (1,007)	$ -	$ -	$ (85,858)	$ 14,798
Noncapital financing activities	(92,680)	-	1,834	-	-	107,625	16,779
Capital and related financing activities	(9,001)	25,013	(50)	-	-	(21,767)	(5,805)
Investing activities	(42,882)	52	-	-	-	-	(42,830)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(18,317)	482	777	-	-	-	(17,058)
CASH AND CASH EQUIVALENTS - Beginning of year	66,078	460	-	-	-	-	66,538
CASH AND CASH EQUIVALENTS - End of year	$ 47,761	$ 942	$ 777	$ -	$ -	$ -	$ 49,480

Required Supplementary Information

Palomar Health

Schedule of Changes in the Net OPEB Liability and Related Ratios – Last 10 Fiscal Years (Shown in Thousands)

	Fiscal Year End Reporting Periods									
	2019 *	2018 *	2017 *	2016	2015	2014	2013	2012	2011	2010
1. Total OPEB liability - prior measurement date	$ 1,193	$ 1,176	$ 1,190	n/a	n/a	n/a	n/a	n/a	n/a	n/a
2. Changes in total OPEB liability										
(a) Service cost	69	60	72	n/a	n/a	n/a	n/a	n/a	n/a	n/a
(b) Interest on the total OPEB liability	46	43	35	n/a	n/a	n/a	n/a	n/a	n/a	n/a
(c) Changes on benefit terms	(48)	-	-	n/a	n/a	n/a	n/a	n/a	n/a	n/a
(d) Differences between expected and actual experience	-	-	-	n/a	n/a	n/a	n/a	n/a	n/a	n/a
(e) Changes of assumptions or other inputs	34	(24)	(63)	n/a	n/a	n/a	n/a	n/a	n/a	n/a
(f) Benefit payments	(64)	(62)	(58)	n/a	n/a	n/a	n/a	n/a	n/a	n/a
(g) Total	$ 1,230	$ 1,193	$ 1,176	$ -	$ -	$ -	$ -	$ -	$ -	$ -
3. Total OPEB liability - current measurement date	$ 1,230	$ 1,193	$ 1,176	$ 1,190	$ -	$ -	$ -	$ -	$ -	$ -
4. Estimated covered-employee payroll	$ 258,493	$ 209,718	$ 240,492	n/a	n/a	n/a	n/a	n/a	n/a	n/a
5. Total OPEB liability as a % of covered-employee payroll	0.48%	0.60%	0.50%	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Key information										
Valuation date	July 1, 2018	July 1, 2016	July 1, 2016	July 1, 2016	n/a	n/a	n/a	n/a	n/a	n/a
Reporting date	June 30, 2019	June 30, 2018	June 30, 2017	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Measurement date	June 30, 2019	June 30, 2018	June 30, 2017	June 30, 2016	n/a	n/a	n/a	n/a	n/a	n/a
Discount rate as of the measurement date	3.48%	3.87%	3.58%	2.85%	n/a	n/a	n/a	n/a	n/a	n/a
Bond index rate	3.48%	3.87%	3.58%	2.85%	n/a	n/a	n/a	n/a	n/a	n/a
Bond index date	June 11, 2019	June 30, 2018	June 30, 2017	June 30, 2016	n/a	n/a	n/a	n/a	n/a	n/a

* June 30, 2017 measurement date results use a final discount rate of 3.58% which is the municipal bond rate as of June 30, 2017.

* June 30, 2018 measurement date results use a final discount rate of 3.87% which is the municipal bond rate as of June 30, 2018.

* June 30, 2019 measurement date results use a final discount rate of 3.48% which is the municipal bond rate as of June 11, 2019.

Notes: PH has no assets that are accumulated in a trust to pay related benefits that meet the criteria in paragraph 4 of Statement 75.