Report of Independent Auditors and
Consolidated Financial Statements with
Supplementary Information

Sonoma Valley Health Care District

June 30, 2014 and 2013

MOSS-ADAMS LLP

Certified Public Accountants | Business Consultants

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CONTENTS

Introduction – This management's discussion and analysis of the financial performance of Sonoma Valley Health Care District (the "District") provides an overview of the District's financial activities for the years ended June 30, 2014 and 2013. It should be read in conjunction with the accompanying consolidated financial statements and footnotes of the District.

Financial highlights

- The District's net position increased in 2014 by approximately $2,984,000 or 28% and increased in 2013 by approximately $1,959,000 or 22%.

- Cash, cash equivalents, and total investments decreased in 2014 by approximately $6,369,000 or 57% and decreased in 2013 by approximately $12,212,000 or 52%. This decrease was due to the use of the Series B General Obligation bond funds for the building of the new Emergency Room.

- Net patient accounts receivable increased in 2014 by approximately $361,000 or 6% and increased in 2013 by approximately $506,000 or 9%.

- The District reported operating losses in both 2014 ($4,036,000) and 2013 ($5,809,000). The operating loss in 2014 decreased by approximately $1,772,000 or 31% less than the operating loss reported in 2013. The decrease in the operating loss in 2014 was due to an increase in Net Patient Service Revenue. The increase in revenue was also due to an adjustment to bad debts for positive collections of old accounts receivable. The operating loss in 2013 was larger due to 2 material factors: 1) the Hospital received a large number of Recover Auditor Contractor ("RAC") audits which resulted in $1,109,000 of RAC take backs; 2) an exceptional amount of information systems training and non-capitalizable cost were incurred due to the Hospital implementing the electronic medical documentation systems, impact of $1,107,000; $757,000 for purchases services and $350,000 in salaries related to the Electronic Health Record. The 2012 operating loss included $1.2 million from the settlement of a 15 year old Medicare cost report Skilled Nursing Home appeal. There were no material positive prior year cost report settlements in 2013. The operating loss in 2013 increased by approximately $1,136,000 or 24% more than the operating loss reported in 2012.

Using this annual report – The District's consolidated financial statements consist of three statements—statement of net position, a statement of revenues, expenses and changes in net position, and a statement of cash flows. These statements provide information about the activities of the District, including resources held by the District but restricted for specific purposes by creditors, contributors, grantors or enabling legislation. The District is accounted for as a business-type activity and presents its consolidated financial statements using the economic resources measurement focus and the accrual basis of accounting.

The statement of net position and statement of revenues, expenses and changes in net position – The statement of net position and the statement of revenues, expenses, and changes in net position report information about the District's resources and its activities. One of the most important questions asked about the District's finances is, "Is the District as a whole, better or worse off as a result of the year's activities?" The statement of net position and the statement of revenues, expenses, and changes in net position report information about the District's resources and its activities in a way that helps answer this question. These statements include all restricted and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the District's net position and changes in them. You can think of the District's net position – the difference between assets and liabilities – as one way to measure the District's financial health, or financial position. Over time, increases or decreases in the District's net position are one indicator of whether its financial health is improving or deteriorating. You will need to consider other non-financial factors, such as changes in the District's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the District.

The statement of cash flows – The final required statement is the statement of cash flows. The statement reports cash receipts, cash payments, and net changes in cash and cash equivalents resulting from four defined types of activities. It provides answers to such questions as where did cash come from, what was cash used for, and what was the change in cash and cash equivalents during the reporting period.

The District's net position – The District's net position are the difference between its assets and liabilities reported in the balance sheet. The District's net position increased by $2,984,000 or 28% in 2014 over 2013 and increased by $1,959,000 or 22% in 2013 over 2012, as shown in Table 1.

The increases in net position in 2014 are largely the result of the Capital Campaign in that the District is working with the Sonoma Valley Hospital Foundation to raise funds for the building expansion.

In 2014, noncurrent investments decreased by $7,316,700 or 80% as compared to 2013. The reason for the decrease is the use of the General Obligation Bonds for renovating and retrofitting the District's existing hospital facility and to purchase equipment outlined in Note 6 to the consolidated financial statements.

In 2014, net patient accounts receivable increased by $361,000 or 6% compared to 2013. The reason for the increase was a slowdown in coding at year end due to the implementation of McKesson Intelligent Coding system. Estimated third-party payor settlements increased by $1,415,499 or 1261% compared to 2013. The reason for the increase is the recording of the Inter-Governmental Transfer of $824,000. During 2014, Napa State was paid quarterly, not yearly like in 2013, therefore the payable to Napa State in 2013 was $1,199,000, the payable is offsetting Other receivables. Property tax receivables, increased $777,000 or 16% from 2013, which is due to the increase in principal due on the General Obligation Bonds B.

Table 1: Assets, Liabilities, and Net Position

	2014	(As Restated) 2013	(As Restated) 2012
ASSETS			
Current assets			
Cash and cash equivalents	$ 2,849,986	$ 1,902,869	$ 926,083
Short-term investments	-	-	460,008
Patient accounts receivable, net of allowances for doubtful accounts of $965,414 and $1,471,799 in 2014 and 2013, respectively	6,793,990	6,433,401	5,927,300
Estimated third-party payor settlements	1,527,754	112,255	1,578,006
Property tax receivables	5,758,948	4,982,227	5,697,647
Other receivables	2,061,156	1,093,383	648,832
Pledge receivables, current	-	500,000	-
Supplies	771,028	805,424	872,171
Prepaid expenses	816,423	1,074,432	569,843
Total current assets	20,579,285	16,903,991	16,679,890
Noncurrent investments			
Board-designated funds	-	186,468	185,910
Restricted for capital acquisitions	220,748	3,474,239	16,978,806
Restricted for debt service	1,637,914	5,263,697	4,276,368
Principal of permanent endowments	-	-	36,839
Other long-term investments	23,756	274,738	449,562
	1,882,418	9,199,142	21,927,485
Capital assets, net of accumulated depreciation	56,350,250	42,476,327	25,216,306
Pledge receivables, long-term	-	1,500,000	-
Total assets	$ 78,811,953	$ 70,079,460	$ 63,823,681

LIABILITIES AND NET POSITION

Current liabilities			
Accounts payable and accrued expenses	$ 8,477,305	$ 10,400,356	$ 7,331,294
Accrued payroll and related liabilities	2,835,095	2,621,053	2,617,748
Deferred tax revenues	5,849,985	4,825,602	4,769,308
Current portion of bond payable	95,000	25,000	-
Current portion of capital lease obligations	1,697,107	832,760	832,323
Current portion of notes payable	124,814	38,795	738,924
Total current liabilities	19,079,306	18,743,566	16,289,597
Accrued workers' compensation liability	711,000	557,000	506,000
Line of credit	4,973,734	2,373,734	-
Bonds payable	35,437,000	35,282,223	35,292,111
Capital lease obligations, net of current portion	4,022,449	2,069,571	2,419,748
Notes payable, net of current portion	917,777	367,116	588,888
Total liabilities	65,141,266	59,393,210	55,096,344
Net Position			
Invested in capital assets, net of related debt	9,082,369	7,997,719	9,787,516
Restricted			
For debt service	1,637,914	1,263,697	276,368
Expendable for capital assets	3,757,072	3,858,727	2,043,087
Nonexpendable permanent endowments	-	-	36,839
Unrestricted (deficit)	(806,668)	(2,433,893)	(3,416,473)
Total net position	13,670,687	10,686,250	8,727,337
Total liabilities and net position	$ 78,811,953	$ 70,079,460	$ 63,823,681

In 2013, net patient accounts receivable increased by $506,000 or 9% compared to 2012. The reason for the increase was a slowdown in insurance payments on older patient accounts. Other receivables, property tax receivables, and pledge receivables increased $229,131 or 4% from 2012, which is due in part to a pledge receivable for the Capital Campaign. Estimated third-party payor settlements decreased $1,466,000 or 93%, which is due to a Medi-Cal 2012 settlement and the RAC reserve.

Operating results and changes in the District's net position – In 2014 the District's operating loss decreased by $1,772,400 or 31% from 2013. In 2013 the operating loss increased by $1,136,000 or 24% from 2012, as shown in Table 2 below:

Table 2: Operating results and changes in net position

	2014	(As Restated) 2013	(As Restated) 2012
Operating revenues			
Net patient service revenue, net of provision for bad debts of $1,458,255 and $2,901,255 in 2014 and 2013, respectively	$ 47,416,961	$ 43,247,566	$ 44,906,433
Capitation revenue	2,055,548	2,111,726	2,223,114
Other revenue	1,103,166	1,647,768	48,820
Total operating revenues	50,575,675	47,007,060	47,178,367
Operating expenses			
Salaries and wages	26,219,974	25,702,558	24,601,200
Purchased services	6,507,171	6,874,543	6,363,019
Supplies	5,889,441	6,119,299	6,277,110
Employee benefits	5,986,866	5,949,821	5,393,819
Medical fees	4,288,169	3,692,868	4,127,471
Other	2,191,737	1,180,790	2,042,418
Depreciation	2,339,876	2,132,706	1,970,238
Utilities	961,882	899,466	845,029
Insurance	226,650	243,608	230,967
Total operating expenses	54,611,766	52,795,659	51,851,271
Operating loss	(4,036,091)	(5,788,599)	(4,672,904)
Non operating revenues and (expenses)			
Property tax revenues	4,938,955	4,797,081	4,757,571
Investment income	32,714	32,614	32,190
Non capital grants and gifts	18,333	232,596	576,711
Interest expense	(1,088,851)	(721,567)	(736,084)
Bond issuance cost	(180,605)	-	-
Contribution to Prima Medical Foundation	(604,413)	(787,560)	(782,817)
Other	147,323	335,621	190,417
Total non operating revenues and (expenses)	3,263,456	3,888,785	4,037,988
(Deficit) excess of revenues over expenses before capital grants and contributions	(772,635)	(1,899,814)	(634,916)
Capital grants and contributions	3,757,072	3,858,727	2,043,087
Increase in net position	2,984,437	1,958,913	1,408,171
Cumulative effect of restatement	-	-	(241,990)
Total net position, beginning of year	10,686,250	8,727,337	7,561,156
Total net position, end of year	$ 13,670,687	$ 10,686,250	$ 8,727,337

The District's net patient revenue is comprised of comprehensive services that span the continuum of healthcare services: inpatient and outpatient hospital patient care services, emergency services, skilled nursing facility services, and home health care services. The following is the District's payer mix based upon net revenue. Net revenue represents payments made by insurance companies and patients and not based upon the gross billed charges.

The following chart shows, the percentage of Government programs (Medicare, Medicare HMO, Medi-Cal and Medi-Cal Managed Care) and commercial insurance has been decreasing. Government programs generally do not cover the cost of providing patient care services and therefore are supplemented by commercial insurance payments. The District's payer mix is the reason that the parcel tax is so critical to the ongoing operations of the District.

	2014	2013	2012
Medicare	38.9%	40.6%	45.3%
Medicare HMO	4.6%	4.4%	0.5%
Medi-Cal	9.8%	6.7%	7.7%
Medi-Cal Managed Care	5.9%	5.4%	5.5%
Commercial Insurance	31.8%	31.4%	33.0%
Workers Compensation	3.2%	3.9%	3.2%
Capitated	1.6%	0.1%	0.1%
Self-pay - Other	4.2%	7.5%	4.7%
	100%	100%	100%

Over the period, the District has experienced a shift from inpatient to outpatient care. The District's experience with this shift in patient care services is consistent across all hospitals in the United States. Many payors, including Medicare, the District's largest payor, are more frequently requiring services to be provided in the outpatient setting.

Operating losses – The first component of the overall change in the District's net position is its operating income or loss; generally, the difference between net patient services and other operating revenues and the expenses incurred to perform those services. In each of the past three years, the District has reported an operating loss. This is consistent with the District's recent operating history as the District was formed and operates primarily to serve residents of Sonoma Valley, regardless of their ability to pay. The District levies property taxes to provide sufficient resources to enable the facility to serve lower income and other residents. The decrease in the operating loss for 2014 was due to 2013 RAC audits and the cost of implementation of information technology during the fiscal year.

The operating loss for 2014 decreased by $1,772,400 or 31% as compared to 2013 and increased by $1,136,000 or 24% as compared to 2012. The major components of those changes in operating loss are:

- Total operating revenues increased by $3,569,000 or 8% in 2014. This is primarily due to the recording of the two IGT's during the year for $1,817,000 and the Medicare legal settlement of $488,000, and the reduction of the Bad Debt reserve of $572,000. In 2013 RAC audits for $1,109,000 reduced operating revenues. The increase in operating revenues in 2012 was primarily due to a Medicare settlement for $1,032,000.

- Salaries, wages, and benefits increased in 2014 by $517,400 or 2% due to an across the board salary increase of 3% in January 2014. Workers' compensation expense, a component of employee benefits, increased in 2014 as compared to 2013 due to increases in open claims and claim reserves required for payments made on outstanding claims. Salaries, wages, and benefits increased in 2013 by $1,101,000 or 4% due to an across the board salary increase of 3% in January 2013 and adjusting employees' salaries to market.

- Medical fees increased in 2014 by $595,300 or 16% compared to 2013 and decreased by $435,000 or 11% in 2013 compared to 2012. The increase in 2014 is due to the surgery call to Prima Medical Foundation. The decrease in 2013 is due to the elimination of the Certified Registered Nurse Anesthetists ("CRNA").

- Purchased services decreased in 2014 by $367,000 or 5% compared to 2013 and increased in 2013 by $512,000 or 8% compared to 2012. Decrease in 2014 is due to the cancellation of Sodexo contract in Plant Operations and Environmental Services of $214,000 and the decreased in Repair & Maintenance of $166,000 . Decreased use of outside consultants of $410,000 offset with an increase use of information technologies for $757,000, accounted for the increase in 2013.

- Depreciation expense increased in 2014 by $207,000 or 10% as compared to 2013 and increased $162,000 or 8% in 2013 as compared to 2012. During 2014 the new Emergency Room went into service.

- Other expenses increase in 2014 by $990,000 or 83% as compared to 2013 and decrease by $842,000 or 41% in 2013 compared to 2012. The increase in 2014 is due to the two Inter Governmental Transfers ("ITG"), for $645,000. And in 2014 there were more equipment leases by $121,000 than in 2013. The decrease in 2013 is due to the decrease in shared IT costs with Palm Drive Hospital of approximately $717,000.

Nonoperating revenues and expenses – Nonoperating revenues and expenses consist of property taxes levied by the District, investment income, interest expense and noncapital grants and gifts. Parcel taxes remained relatively unchanged in 2014 as compared to 2013. Tax assessments for the general obligation bonds increased by $133,000 over 2013. Interest expense increased by $367,000 or 51% in 2014. The increase in interest was due to our new building being completed in February 2014 and GO Bond interest was no longer being capitalized to the project. Investment income increased by $100 in 2014 and increased by $500 in 2013. Noncapital grants and gifts decreased by $214,000 in 2014 and decreased by $344,000 in 2013.

Capital grants and gifts – The District received gifts of $3,757,000 from a foundation and various individuals to purchase capital assets in 2014 and $3,859,000 in 2013, a decrease of $102,000 from 2014 to 2013 and an increase of $1,816,000, from 2013 and 2012, respectively.

The District's cash flows – Changes in the District's cash flows are consistent with changes in operating losses and non-operating revenues and expenses, as discussed earlier.

Capital assets – At the end of 2014 and 2013, the District had $56,350,000 and $42,476,000, respectively, invested in capital assets, net of accumulated depreciation, as detailed in Note 6 to the consolidated financial statements. In 2014 and 2013, the District purchased new equipment and made capital improvements costing $16,200,000 and $19,452,000, respectively. The majority of the 2014 improvements and new equipment related to the preparation of a master plan, detailed planning, acquisition of equipment, and installation of the information systems wiring for the District's renovation project.

Debt – At June 30, 2014 and 2013, the District had $47,268,000 and $40,989,000, respectively, in bonds, equipment notes payable, and notes payable outstanding as detailed in Note 10 to the financial statements. In 2014, the District entered into leases and a note totaling $4,466,000 for purchases of an Electronic Health Record system and equipment for the new building. The implementation of the Electronic Health Record system is a multiyear project. The new building opened in February of 2014.

Future plans –The District has historically provided salary and practice supports for recruitment and retention of new physicians whose services meet the needs of our community. In the past, certain of these arrangements have been provided via contractual agreements with Prima Medical Group, a regional physician organization. The District has implemented plans to convert and consolidate these arrangements to a master agreement with Prima Medical Foundation. The District has made capital contributions to Prima Medical Foundation, which is a non-profit medical care, research, and community benefit organization. This is a more cost effective and longer term vehicle for physician support.

Contacting the District's financial management – This financial report is designed to provide our patients, suppliers, taxpayers and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. Questions about this report and requests for additional financial information should be directed to the Chief Financial Officer by telephoning (707) 935-5003.

MOSS-ADAMS LLP
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REPORT OF INDEPENDENT AUDITORS

To the Board of Directors
Sonoma Valley Health Care District

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Sonoma Valley Health Care District, (the "District") which comprise the consolidated statements of net position as of June 30, 2014 and 2013, and the related statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Sonoma Valley Health Care District as of June 30, 2014 and 2013, and the consolidated changes in financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the Government Accounting Standard Board ("GASB") issued Statement No. 65, *Items Previously Reported as Assets and Liabilities* ("GASB No. 65"), which is effective for financial statements for periods beginning after December 15, 2012. GASB No. 65 establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. It also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term deferred in financial statement presentations. The District has adopted this statement for the fiscal year ended June 30, 2014, and as a result, the consolidated financial statements presented herein have been restated retrospectively.

Other Matters

Required Supplementary Information

The accompanying Management's Discussion and Analysis on pages 1 through 6 are not required parts of the consolidated financial statements but are supplementary information required by the Governmental Accounting Standards Board who considers them to be an essential part of financial reporting for placing the consolidated financial statements in an appropriate operational economic, or historical context. This supplementary information is the responsibility of Sonoma Valley Health Care District's management. We have applied certain limited procedures in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the consolidated financial statements, and other knowledge we obtained during our audit of the consolidated financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

The accompanying supplementary information related to community support on page 27 is presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of Sonoma Valley Health Care District's management. The information has not been subjected to the auditing procedures applied in the audit of the consolidated financial statements and accordingly, we do not express an opinion or provide any assurance on it.

San Francisco, California
October 22, 2014

CONSOLIDATED FINANCIAL STATEMENTS

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SONOMA VALLEY HEALTH CARE DISTRICT
CONSOLIDATED STATEMENTS OF NET POSITION
Years Ended June 30, 2014 and 2013 (AS RESTATED)

	2014	(As Restated) 2013
ASSETS		
Current assets		
Cash and cash equivalents	$ 2,849,986	$ 1,902,869
Patient accounts receivable, net of allowances for doubtful accounts of $965,414 and $1,471,799 in 2014 and 2013, respectively	6,793,990	6,433,401
Estimated third-party payor settlements (net)	1,527,754	112,255
Property tax receivables	5,758,948	4,982,227
Other receivables	2,061,156	1,093,383
Pledge receivables, current	-	500,000
Supplies	771,028	805,424
Prepaid expenses	816,423	1,074,432
Total current assets	20,579,285	16,903,991
Noncurrent investments		
Board-designated funds	-	186,468
Restricted for capital acquisitions	220,748	3,474,239
Restricted for debt service	1,637,914	5,263,697
Other long-term investments	23,756	274,738
	1,882,418	9,199,142
Capital assets, net of accumulated depreciation	56,350,250	42,476,327
Pledge receivables, long-term	-	1,500,000
Total assets	$ 78,811,953	$ 70,079,460

See accompanying notes.

LIABILITIES AND NET POSITION

Current liabilities		
Accounts payable and accrued expenses	$ 8,477,305	$ 10,400,356
Accrued payroll and related liabilities	2,835,095	2,621,053
Deferred tax revenues	5,849,985	4,825,602
Current portion of bond payable	95,000	25,000
Current portion of capital lease obligations	1,697,107	832,760
Current portion of notes payable	124,814	38,795
Total current liabilities	19,079,306	18,743,566
Accrued workers' compensation liability	711,000	557,000
Line of credit	4,973,734	2,373,734
Bonds payable, net of current portion	35,437,000	35,282,223
Capital lease obligations, net of current portion	4,022,449	2,069,571
Notes payable, net of current portion	917,777	367,116
Total liabilities	65,141,266	59,393,210
Net Position		
Invested in capital assets, net of related debt	9,082,369	7,997,719
Restricted		
For debt service	1,637,914	1,263,697
Expendable for capital assets	3,757,072	3,858,727
Nonexpendable permanent endowments	-	-
Unrestricted (deficit)	(806,668)	(2,433,893)
Total net position	13,670,687	10,686,250
Total liabilities and net position	$ 78,811,953	$ 70,079,460

See accompanying notes.

SONOMA VALLEY HEALTH CARE DISTRICT
CONSOLIDATED STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
Years Ended June 30, 2014 and 2013 (AS RESTATED)

	2014	(As Restated) 2013
Operating revenues		
Net patient service revenue, net of provision for bad debts of $1,458,255 and $2,901,255 in 2014 and 2013, respectively	$ 47,416,961	$ 43,247,566
Capitation revenue	2,055,548	2,111,726
Other revenue	1,103,166	1,647,768
Total operating revenues	50,575,675	47,007,060
Operating expenses		
Salaries and wages	26,219,974	25,702,558
Purchased services	6,507,171	6,874,543
Supplies	5,889,441	6,119,299
Employee benefits	5,986,866	5,949,821
Medical fees	4,288,169	3,692,868
Other	2,191,737	1,180,790
Depreciation	2,339,876	2,132,706
Utilities	961,882	899,466
Insurance	226,650	243,608
Total operating expenses	54,611,766	52,795,659
Operating loss	(4,036,091)	(5,788,599)
Nonoperating revenues and (expenses)		
Property tax revenues	4,938,955	4,797,081
Investment income	32,714	32,614
Noncapital grants and contributions	18,333	232,596
Interest expense	(1,088,851)	(721,567)
Bond issuance cost	(180,605)	-
Contribution to Prima Medical Foundation	(604,413)	(787,560)
Other	147,323	335,621
Total nonoperating revenues and (expenses)	3,263,456	3,888,785
Deficit of revenues over expenses before capital grants and contributions	(772,635)	(1,899,814)
Capital grants and contributions	3,757,072	3,858,727
Increase in net position	2,984,437	1,958,913
Total net position, beginning of year, as restated (Note 1)	10,686,250	8,727,337
Total net position, end of year	$ 13,670,687	$ 10,686,250

See accompanying notes.

	2014	(As Restated) 2013
Cash flows from operating activities:		
Receipts from patients and third-party payors	$ 47,806,587	$ 47,966,710
Payments to employees for services	(31,992,798)	(31,598,074)
Payments to physicians, suppliers, and contractors	(17,800,429)	(16,643,626)
Net cash (used in) operating activities	(1,986,640)	(274,990)
Cash flows from noncapital financing activities:		
Noncapital grants, contributions, and other	110,326	742,349
Contribution to Prima Medical Foundation	(604,413)	(787,560)
Parcel taxes supporting operations	3,075,631	3,058,550
Net cash from noncapital financing activities	2,581,544	3,013,339
Cash flows from capital and related financing activities:		
Purchases of capital assets	(12,204,010)	(18,958,018)
Principal payments on capital lease obligations	(1,192,564)	(843,514)
Principal payments on notes payable	(38,772)	(921,901)
Payment of line of credit	-	(128,000)
Principal payments on bond payable	(11,905,000)	-
Interest paid on long-term debt	(1,775,601)	(1,334,388)
Proceeds from issuance of notes payable	675,452	-
Proceeds from issuance of bonds	12,437,000	-
Proceeds from line of credit	2,600,000	2,501,734
Tax revenue related to general obligation bonds	2,112,351	2,701,559
Capital grants and gifts	2,293,919	2,858,727
Net cash from capital and related financing activities	(6,997,225)	(14,123,801)
Cash flows from investing activities:		
Proceeds from sale of investments	7,316,724	12,329,624
Interest and dividends on investments	32,714	32,614
Net cash from investing activities	7,349,438	12,362,238
Net change in cash and cash equivalents	947,117	976,786
Cash and cash equivalents at beginning of year	1,902,869	926,083
Cash and cash equivalents at end of year	$ 2,849,986	$ 1,902,869

See accompanying notes.

Reconciliation of operating loss to net cash from operating activities		
Operating loss	$ (4,036,091)	$ (5,788,599)
Adjustments to reconcile operating loss to net cash from operating activities		
Depreciation	2,339,876	2,132,706
Provision for bad debts	1,458,255	2,901,255
Loss on disposal of fixed assets	-	59,065
Changes in assets and liabilities		
Patient accounts receivable	(1,818,844)	(3,407,356)
Estimated amounts due from and to third-party payors (net)	(1,415,499)	1,465,751
Accounts payable and accrued expenses	(147,450)	4,403,450
Other assets and liabilities	1,633,113	(2,021,336)
Net cash from operating activities	$ (1,986,640)	$ (255,064)
Supplemental disclosure of noncash transactions		
Acquisition of capital assets financed with long-term debt	$ 4,009,789	$ 493,774

See accompanying notes.

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization – Sonoma Valley Health Care District (the "Health Care District") is a political subdivision of the State of California organized under the State of California Local Health Care District Law as set forth in the Health and Safety Code of the State of California. The Health Care District is governed by an elected Board of Directors and is considered the primary government for financial reporting purposes.

The Health Care District owns and operates Sonoma Valley Hospital (the "Hospital"). The Hospital is located in Sonoma, California, and is licensed for 56 general acute care beds and 27 skilled nursing beds. It also provides 24-hour basic emergency care, outpatient diagnostic and therapeutic services, and operates a home health agency. The Hospital derives a significant portion of its revenues from third-party payors, including Medicare, Medi-Cal, and commercial insurance organizations.

Sonoma Valley Hospital Auxiliary (the "Auxiliary") was formed to render non-medical services on a volunteer basis to Sonoma Valley Hospital. The Auxiliary also raises monies for the benefit of the Hospital and its activities. As the sole purpose of the Auxiliary is to support the Hospital, the Auxiliary has been consolidated with the Hospital's financial statements.

Principles of consolidation – The accompanying consolidated financial statements include the accounts of the Hospital and the Auxiliary (collectively referred to as the "District"). All significant inter-company accounts and transactions have been eliminated in the consolidated financial statements.

Accounting standards – Pursuant to Government Accounting Standard Board ("GASB") Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 Financial Accounting Standards Board ("FASB") and AICPA Pronouncements*, the District's proprietary fund accounting and financial reporting practices are based on all applicable GASB pronouncements as well as codified pronouncements issued on or before November 30, 1989.

Proprietary fund accounting – The District utilizes the proprietary fund method of accounting whereby revenues and expenses are recognized on the accrual basis and consolidated financial statements are prepared using the economic resources measurement focus.

Use of estimates – The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents – Cash and cash equivalents include deposits with financial institutions and investments in highly liquid debt instruments with an original maturity of three months or less. Cash and cash equivalents exclude amounts whose use is limited by board designation or by legal restriction.

Investments – The District maintains some of its cash in the State of California Local Agency Investment Fund ("LAIF") pooled investment. The funds deposited in LAIF are invested in accordance with Government Code Sections 16340 and 16480, the stated investment authority for the Pooled Money Investment Account. Balances are stated at fair market value.

Noncurrent investments consist of Board-designated and restricted funds set aside by the board for future capital improvements and other operational reserves, over which the board retains control and may at its discretion, use for other purposes; assets set aside for qualified capital outlay projects in compliance with state law and assets restricted by donors or grantors.

Investment income, realized gains and losses, and unrealized gains and losses on investments are reflected as nonoperating income or expense.

Pledges Receivable – Pledges have been recorded at their present value net of applicable discounts of $0 and $2,000,000 as of June 30, 2014 and 2013, respectively. An allowance for estimated uncollectible pledges receivable is recorded based on past experience and an analysis of current pledges receivable balances. There was no allowance recorded as of June 30, 2014 and 2013, as the pledges are deemed collectible.

Funds held by trustee – According to the terms of the General Obligation Bond indenture agreements, these certain amounts are held by the bond trustee and paying agent and are maintained and managed by the trustee and are invested in noncurrent investments. These assets are available for the settlement of future current bond obligations.

Capital assets – Capital asset acquisitions over $500 are capitalized and recorded at cost. Donated property is recorded at its fair-market value on the date of donation. Equipment under capital lease is amortized on the straight-line basis over the shorter of the lease term or the estimated useful life of the equipment. Leasehold improvements are amortized using the straight-line method over the shorter of the lease term or the estimated useful life of the related assets. Depreciation is computed using the straight-line method over the estimated useful lives of the following asset groups:

Land Improvements	10 - 20 years
Buildings and fixtures	20 - 40 years
Equipment	2 - 10 years
Software	5 - 7 years

The District evaluates prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. Impairment losses on capital assets are measured using the method that best reflects the diminished service utility of the capital asset.

Costs of borrowing – Except for capital assets acquired through gifts, contributions or capital grants, interest cost on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

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

Workers' Compensation and Medical Malpractice Liabilities – The District maintains professional liability insurance on a claims-made basis, with liability limits of $15,000,000 in aggregate, which is subject to a $5,000 deductible.

The District purchases a Workers' Compensation Excess Policy that insures claims with no limits in the amounts and a $500,000 deductible. Actuarial estimates of uninsured losses for workers' compensation have been accrued as liabilities in the accompanying consolidated financial statements.

Net position – Net position of the District are classified as invested in capital assets, net of related debt, restricted net position, and unrestricted net position.

Invested in capital assets, net of related debt – Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted net position – Restricted net position consists of net position with limits on their use that are externally imposed by creditors (such as through debt covenants), grantors, contributors or by laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position – Unrestricted net position are remaining net position that do not meet the definition of invested in capital assets, net of related debt or restricted.

Statements of revenues, expenses, and changes in net position – For purposes of display, transactions deemed by management to be ongoing, major, or central to the provisions of health care services are reported as revenues and expenses. Peripheral or incidental transactions are reported as gains and losses. These peripheral activities include investment income, property tax revenue, gifts and contributions, grants and bequests, and change in net unrealized gains and losses on investments in marketable securities and are reported as nonoperating.

Net patient service revenue and patient accounts receivable – Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered, and adjusted in future periods as final settlements are determined. At June 30, 2014 and 2013, the District provided allowances for losses on amounts receivable directly from patients totaling $965,414 and $1,471,799, respectively. The distribution of gross patient accounts receivable by payor at June 30, 2014 and 2013, is as follows:

	2014	2013
Medicare	38.9%	40.6%
Medicare HMO	4.6%	4.4%
Medi-Cal	9.8%	6.7%
Medi-Cal Managed Care	5.9%	5.4%
Commercial Insurance	31.8%	31.4%
Workers Compensation	3.2%	3.9%
Capitated	1.6%	0.1%
Self-pay - Other	4.2%	7.5%
	100%	100%

Uncollectible accounts – The District provides care to patients without requiring collateral or other security. Patient charges not covered by a third-party payor are billed directly to the patient if it is determined that the patient has the ability to pay. A provision for uncollectible accounts is recognized based on management's estimate of amounts that ultimately may be uncollectible.

Capitation revenues – The District, in association with Meritage Medical Network (formerly Marin Independent Practice Association) ("Meritage") has agreements with various health maintenance organizations ("HMOs") to provide medical services to subscribing participants. Under two of these agreements, the District receives monthly capitation payments based on the number of each HMO's participants, regardless of the services actually performed by the District. The District is not responsible for the cost of services provided to subscribing participants by other healthcare providers. The District reassesses the profitability of the agreements for exposure risks in the event future medical costs to provide medical services exceed the related future capitation payments.

Property tax revenues – Taxes for District operations and for debt service payments related to District General Obligation Bonds are levied annually on the taxable property within the District.

In March 2002, the District voters adopted a special tax on each taxable parcel of land within the District at an annual rate of up to $130 per parcel for five years. In March 2007, the District voters extended the special tax at an annual rate of up to $195 per parcel through June 30, 2014. The purpose of the special parcel tax is to ensure continued local access to emergency room and acute hospital care and other medical services for residents of the District and for visitors to the area. The parcel tax extension was approved for 2013 – 2018 by the District's voters.

The District received approximately 165% in 2014 and 245% in 2013 of its total increase in net position from property taxes.

These funds were designated as follows:

	2014	2013
Designated for hospital operations	$ 2,963,353	$ 2,967,983
Levied for hospital operations and debt service payments	1,975,602	1,829,098
Property Tax Revenue	$ 4,938,955	$ 4,797,081

The District recognizes property taxes receivable when the enforceable legal claim arises (January 1) and recognizes revenues over the period for which the taxes are levied (July 1 to June 30). Property taxes are considered delinquent on the day following each payment due date. Property tax revenues are nonexchange transactions that are reported as nonoperating revenues.

Charity care – The District provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the District does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Grants and contributions – The District receives grants as well as contributions from individuals and private organizations. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as nonoperating revenues.

Compensated absences – District policies permit most employees to accumulate paid time-off benefits that may be realized as paid time-off or as a cash payment upon termination. Expense and the related liability are recognized as paid time-off benefits when earned. Compensated absence liabilities are computed using the regular pay and termination pay rates in effect at the balance sheet date plus an additional amount for compensation-related payments, such as social security and Medicare taxes computed using rates in effect at the date of computation.

Income taxes – The District operates under the purview of the Internal Revenue Code, Section 115, and corresponding California Revenue and Taxation Code provisions. As such, it is not subject to state or federal taxes on income. However, income from the unrelated business activities of the District and the Auxiliary may be subject to income taxes.

Restatement, **Change in Accounting Principle**–GASB issued GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* ("GASB No. 65"), which is effective for financial statements for periods beginning after December 15, 2012. GASB No. 65 establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. It also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term deferred in financial statement presentations.

The District has adopted this statement for the fiscal year ended June 30, 2014, and as a result, the consolidated financial statements presented herein have been restated retrospectively as follows:

	As previously Reported	Adjustment	As Adjusted
Unrestricted net position, end of year	$ (2,211,829)	$ (222,064)	$ (2,433,893)
Total net position, beginning of year	$ 8,969,327	$ (241,990)	$ 8,727,337
Total net position, end of year	$ 10,908,314	$ (222,064)	$ 10,686,250
Other assets	$ 222,064	$ (222,064)	$ -
Depreciation and amortization expense	$ -	$ -	$ -
Total operating expenses	$ 52,815,585	$ (19,926)	$ 52,795,659
Increase in net position	$ 1,938,987	$ 19,926	$ 1,958,913

New accounting pronouncements – GASB issued GASB Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27* ("GASB No. 68"), which is effective for financial statements for periods beginning after June 15, 2014. GASB No. 68 replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of Statement No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 27 and 50 remain applicable for pensions that are not covered by the scope of this Statement. It establishes standards for measuring and recognizing liabilities, deferred outflows of resources, and deferred inflows of resources, and expense/expenditures. For defined benefit pensions, this Statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about pensions also are addressed. The District is currently evaluating the impact of the adoption of GASB No. 68 for the fiscal year ending June 30, 2015.

GASB also issued GASB Statement No. 69, *Government Combinations and Disposals of Government Operations* ("GASB No. 69"), which is effective for financial statements for periods beginning after December 15, 2013. GASB No. 69 requires the use of carrying values to measure the assets and liabilities in a government merger. Conversely, government acquisitions are transactions in which a government acquires another entity, or its operations, in exchange for significant consideration. This Statement requires measurements of assets acquired and liabilities assumed generally to be based upon their acquisition values. It also provides guidance for transfers of operations that do not constitute entire legally separate entities and in which no significant consideration is exchanged. It defines the term operations for purposes of determining the applicability of this Statement and requires the use of carrying values to measure the assets and liabilities in a transfer of operations, and provides accounting and financial reporting guidance for disposals of government operations that have been transferred or sold. The District is currently evaluating the impact of the adoption of GASB No. 69 for the fiscal year ending June 30, 2015.

NOTE 2 – NET PATIENT SERVICE REVENUES

The District has agreements with third-party payors that provide for payments to the District at amounts different from its established rates. Medicare and Medi-Cal settlements are estimated and recorded in the consolidated financial statements in the year services are provided. Laws and regulations governing the Medicare and Medi-Cal programs are complex and subject to interpretation. The District believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrongdoing. While no such regulatory inquires have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as significant regulatory action, including fines, penalties, and exclusion from the Medicare and Medi-Cal programs. Changes in Medicare, Medi-Cal, or other programs or the reduction of program funding could have an adverse impact on future net patient service revenues. A summary of the payment arrangements with major third-party payors is as follows:

Medicare – Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge for the District. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. The District's classification of inpatients under the Medicare program and the appropriateness of their admissions are subject to an independent review by a peer review organization under contract with the District. Most outpatient services at District provided to Medicare beneficiaries are paid at prospectively determined rates per encounter that vary according to procedures performed. Medicare cost reports have been audited and final settled by the fiscal intermediary through 2013 for the District.

Medi-Cal – Prior to July 1, 2013, inpatient acute care services rendered to Medi-Cal program beneficiaries are were reimbursed under a cost reimbursement methodology; however, the District is also subject to per discharge limits. The District was paid for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports and audits thereof by Medi-Cal. Medi-Cal cost reports have been audited through June 30, 2011. Per discharge limits have been determined by Medi-Cal through June 30, 2009, for the District. Beginning July 1, 2013, inpatient acute care services rendered to Medi-Cal program beneficiaries under a diagnostic related group (DRG) methodology. Under this methodology, similar to Medicare, services are paid at prospectively determined rates per discharge according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient skilled nursing care services rendered to Medi-Cal program beneficiaries are reimbursed at prospectively determined per diem rates. Outpatient services rendered to Medi-Cal program beneficiaries are reimbursed based on prospectively determined fee schedules.

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

Net patient service revenues for the years ended June 30, 2014 and 2013, were as follows:

	2014	2013
Patient service revenues at established charge rates		
Services provided to Medicare patients	$ 102,613,658	$ 92,776,198
Services provided to Medi-Cal patients	30,692,700	27,374,856
Services provided to other patients	70,953,915	71,230,691
Gross patient service revenues	204,260,273	191,381,745
Less contractual adjustments and provision for bad debts	(156,843,312)	(148,134,179)
Net patient service revenues	$ 47,416,961	$ 43,247,566

NOTE 3 – CASH DEPOSITS

At June 30, 2014 and 2013, the District cash accounts are recorded of $2,849,986 and $1,902,869, respectively. Bank balances were $2,925,164 and $1,737,128, respectively. All of the bank balances at June 30, 2014 and 2013 were covered by federal depository insurance.

NOTE 4 – BOARD - DESIGNATED, RESTRICTED FUNDS, AND OTHER LONG-TERM INVESTMENTS

District investment balances and average maturities were as follows at June 30, 2014 and 2013, respectively:

	2014		
		Investment Maturities (in years)	
Investment Type	Fair-Value	Less than 1	1 to 5
Short-term money market funds	$ 1,637,914	$ 1,637,914	$ -
Interest in irrevocable trust held in LAIF	-	-	-
LAIF (State Pool Demand Deposits)	244,504	244,504	-
Total fair-value	$ 1,882,418	$ 1,882,418	$ -

	2013		
		Investment Maturities (in years)	
Investment Type	Fair-Value	Less than 1	1 to 5
Short-term money market funds	$ 5,263,697	$ 5,263,697	$ -
LAIF (State Pool Demand Deposits)	3,935,445	3,935,445	-
Total fair-value	$ 9,199,142	$ 9,199,142	$ -

Except for the investment of unexpended funds borrowed for construction, the District's investment policy limits the first $5,000,000 of investments to the LAIF. Once investments exceed $5,000,000, the policy (California Government Code) limits investments to bonds and other obligations of the US Treasury, US agencies or instrumentalities, or the state of California; bonds of any city, county, school district, or special road district of the state of California; bonds of banks for cooperatives, federal land banks, federal intermediate credit banks, federal home loan banks, Federal Home Loan Bank, Tennessee Valley Authority, and the National Mortgage Association or certificates of deposit.

The investment policy does not specifically address interest rate risk, credit risk, custodial credit risk, concentration of credit risk or foreign currency risk.

Interest rate risk – Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest. The money market funds are presented as an investment with a maturity of less than one year because they are redeemable in full immediately.

Credit risk – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2014 and 2013, the District's investments in money market mutual funds were rated AAA by Standard and Poor's and AAA by Moody's Investors Service and the District's investments in LAIF were not rated.

Custodial credit risk – For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The District's investments in US agency securities, LAIF, and money market mutual funds are held by the broker or by the bank's trust department in other than the District's name.

Concentration of credit risk – This risk relates to the risk of loss attributed to the magnitude of the District's investment in a single issuer. The District had the following investments in a single issuer in excess of 5% of total investments as of June 30, 2014 and 2013:

	2014		2013	
LAIF (State Pool Demand Deposits)	$ 244,504	13.0%	$ 3,935,445	42.8%

NOTE 5 – PROPERTY TAX RECEIVABLES

Property tax receivables consisted of the following as of June 30, 2014 and 2013:

	2014	2013
Property tax receivables		
Special parcel tax	$ 3,078,743	$ 3,039,656
Tax for general obligation bond debt service payments	2,680,205	1,942,571
	5,758,948	4,982,227
Total property tax receivables	$ 5,758,948	$ 4,982,227

NOTE 6 – CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2014, is as follows:

	Balance June 30, 2013	Increases	Decreases, Transfers, and Retirements	Balance June 30, 2014
Nondepreciable capital assets				
Land	$ 197,659	$ -	$ -	$ 197,659
Construction in progress	32,772,060	13,211,854	(43,416,608)	2,567,306
Total nondepreciable capital assets	32,969,719	13,211,854	(43,416,608)	2,764,965
Depreciable capital assets				
Land improvements	805,238	-	-	805,238
Buildings and improvements	22,446,088	1,037	42,095,243	64,542,368
Equipment	18,948,817	3,000,908	1,321,365	23,271,090
	42,200,143	3,001,945	43,416,608	88,618,696
Less accumulated depreciation	(32,693,535)	(2,339,876)	-	(35,033,411)
Total depreciable capital assets, net	9,506,608	662,069	43,416,608	53,585,285
Total capital assets, net	$ 42,476,327	$ 13,873,923	$ -	$ 56,350,250

Capital assets activity for the year ended June 30, 2013, is as follows:

	Balance June 30, 2012	Increases	Decreases, Transfers, and Retirements	Balance June 30, 2013
Nondepreciable capital assets				
Land	$ 197,659	$ -	$ -	$ 197,659
Construction in progress	17,586,721	18,870,019	(3,684,680)	32,772,060
Total nondepreciable capital assets	17,784,380	18,870,019	(3,684,680)	32,969,719
Depreciable capital assets				
Land improvements	838,336	-	(33,098)	805,238
Buildings and improvements	22,729,315	11,462	(294,689)	22,446,088
Equipment	16,875,798	570,311	1,502,708	18,948,817
	40,443,449	581,773	1,174,921	42,200,143
Less accumulated depreciation	(33,011,523)	(2,132,706)	2,450,694	(32,693,535)
Total depreciable capital assets, net	7,431,926	(1,550,933)	3,625,615	9,506,608
Total capital assets, net	$ 25,216,306	$ 17,319,086	$ (59,065)	$ 42,476,327

NOTE 7 – EMPLOYEE BENEFIT PLANS

Defined contribution plan – The District contributes to a defined contribution retirement plan (the "Plan") covering substantially all employees. Expense is recorded for the amount of the District's required contributions, determined in accordance with the terms of the Plan. The Plan is administered by the District's Board of Directors. The Plan provides retirement benefits to plan members and death benefits to beneficiaries of plan members. Benefit provisions are contained in the plan document and are established and can be amended by action of the District's governing body. Contribution rates for plan members and the District, expressed as a percentage of covered payroll, were 3.42% for 2014 and 2013.

Deferred compensation plan – The District offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The deferred compensation plan is available to all employees and permits them to defer a portion of their salary. An employer match is also provided and is vested at the rate of 16.7% per year.

The District's contributions to the defined contribution retirement plan and deferred compensation plan totaled $557,148 and $521,163 during 2014 and 2013, respectively.

NOTE 8 – MEDICAL MALPRACTICE COVERAGE AND CLAIMS

The District has joined together with other providers of health care services to form Beta Healthcare Group ("Beta"), a public entity risk pool (the "Pool") currently operating as a common risk management and insurance program for its members. The District purchases medical malpractice insurance from the Pool under a claims-made policy. The District pays an annual premium to the Pool for its torts insurance coverage. The District purchases excess liability insurance through a commercial insurer for amounts in excess of the coverage provided under Beta. The Pool's governing agreements specifies that the Pool will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of stop-loss amounts. Accounting principles generally accepted in the United States of America require a health care provider to accrue the expense of its share of malpractice claim costs, if any, for any reported and unreported incidents of potential improper professional service occurring during the year which will not be covered by an existing claims made insurance policy by estimating the probable ultimate costs of the incidents. Based upon the District's claims experiences, an estimated accrual of $0 and $15,000, as of June 30, 2014 and 2013, respectively, for malpractice costs was recorded and is included in accounts payable and accrued expenses in the consolidated statements of net position.

NOTE 9 – WORKERS' COMPENSATION CLAIMS

The District is self-insured for workers' compensation claims of its employees up to $500,000, with commercial stop-loss insurance coverage purchased for claims in excess of these amounts through. A provision is accrued for self-insured workers' compensation claims, including both claims reported and claims incurred but not yet reported of $711,000 and $557,000 as of June 30, 2014 and 2013, respectively. The District utilizes an actuary to estimate the ultimate costs to settle such claims. Estimated future payments related to workers' compensation claims have been discounted at a rate of 1% at June 30, 2014 and 2013. It is reasonably possible that the District's estimate will change by a material amount in the near term.

NOTE 10 – LONG-TERM DEBT

The following is a summary of the District's long-term debt transactions for the years ended June 30, 2014 and 2013:

	Balance June 30, 2013	Additions	Decreases/ Amortization	Balance June 30, 2014
General obligation bonds payable				
Principal	$ 35,000,000	$ 12,437,000	$ (11,905,000)	$ 35,532,000
Original issue premium	342,212	-	(307,223)	34,989
Deferred loss on early retirement of revenue bonds	(34,989)	-	-	(34,989)
	35,307,223	12,437,000	(12,212,223)	35,532,000
Notes payable	405,911	675,452	(38,772)	1,042,591
Total long-term debt	$ 35,713,134	$ 13,112,452	$ (12,250,995)	$ 36,574,591

	Balance June 30, 2012	Additions	Decreases/ Amortization	Balance June 30, 2013
General obligation bonds payable				
Principal	$ 35,000,000	$ -	$ -	$ 35,000,000
Original issue premium	373,866	-	(31,654)	342,212
Deferred loss on early retirement of revenue bonds	(81,756)	-	46,767	(34,989)
	35,292,110	-	15,113	35,307,223
Notes payable	1,327,812	-	(921,901)	405,911
Total long-term debt	$ 36,619,922	$ -	$ (906,788)	$ 35,713,134

General obligation bonds payable – On November 4, 2008, the District electorate approved the authorization to issue a total of $35,000,000 in general obligation bonds. On April 1, 2009, the District issued $12,000,000 principal amount of general obligation bonds (Sonoma Valley Health Care District General Obligation Bonds, Election of 2008, Series A 2009). Bond proceeds were to be used to pay for a portion of the costs of renovating and retrofitting the District's existing hospital facility, to purchase equipment, to refund outstanding indebtedness, to pay costs of issuance and to pay bond interest due August 1, 2009. $4,000,000 of the proceeds were used to refund all of the then outstanding Revenue Bonds. $8,000,000 of the proceeds and the proceeds from all future bonds authorized by the election were used to construct a new central utility plant, improve utility infrastructure, make all necessary seismic upgrades to existing facilities, and purchase additional medical equipment and install information systems wiring (the "Project").

Interest on the Bonds is payable semi-annually at rates ranging from 5.375% to 8.750% with principal payments due annually beginning August 1, 2013.

Bonds maturing on or before August 1, 2014, are not subject to redemption prior to their respective stated maturity dates. Bonds maturing on or after August 1, 2015, may be redeemed prior to maturity at the District's option at redemption prices equal to the par amount of Bonds redeemed. The Bonds are general obligations of the District payable from ad valorem taxes. In the event the District fails to provide sufficient funds for payment of principal and interest when due, a commercial insurance company has guaranteed to pay that portion of principal and interest for which funds are not available.

In the first phase of the Project, the District prepared a master plan, completed the detailed planning for the Project, acquired some equipment, installed the information systems wiring, and began construction.

In August 2010, the District issued $23,000,000 of additional general obligation bonds (Sonoma Valley Health Care District General Obligation Bonds, Election of 2008, Series B 2010) in order to finance the second and final phase of the Project. During this phase, which the District expects to complete in fiscal year 2013, the District will complete all construction and improvement aspects of the Project and finish purchasing the equipment budgeted in the Project. The Project was completed in March 2014.

In February 2014, the District issued $12,437,000 of additional general obligation bond (Sonoma Valley Health Care District 2014 General Obligation Refunding Bond) to refund all of the outstanding Sonoma Valley Health Care District General Obligation Bonds, Election of 2008, Series A 2009. The 2009 General Obligations Bonds were refunded in February 2014 and the funds were transferred to an escrow account held by a trustee until the bonds were fully called in August 2014. As of June 30, 2014, the District did not have a liability for these funds.

Interest on the Bonds is payable semi-annually at 3.780% with principal payments due annually beginning August 1, 2015.

Line of credit – The District entered into a line of credit agreement with a bank for $7,000,000, with an interest rate of 2.5% and maturing on January 31, 2017. The District is required to comply with certain restrictive covenants, including maintaining a total debt to EBIDA ratio of 2.0 to 1.0 and maintaining a minimum tangible net worth of not less than $9,000,000. The District had an unused credit of $2,026,265 as of June 30, 2014.

Debt service requirements – Debt service requirements for long-term debt are as follows at June 30, 2014:

	General Obligation Bonds		Note Payable	
Year Ending June 30,	**Principal**	**Interest**	**Principal**	**Interest**
2015	$ 95,000	$ 1,328,536	$ 124,814	$ 11,497
2016	1,236,000	1,149,770	127,013	9,297
2017	1,339,000	1,110,233	128,312	7,999
2018	1,433,000	1,065,791	129,597	6,713
2019 - 2023	8,754,000	4,523,669	532,855	4,758
2024 - 2028	12,448,000	2,849,409	-	2,523
2029 - 2033	10,227,000	618,897	-	-
	$ 35,532,000	$ 12,646,305	$ 1,042,591	$ 42,787

Interest costs – Interest costs incurred during the years ended June 30, 2014 and 2013, are summarized as follows:

	2014	**2013**
Interest cost		
Paid	$ 1,775,601	$ 1,334,388
Accrued	329,844	714,262
Total incurred	2,105,445	2,048,650
Amortization of deferred financing costs, original issue premium and deferred loss on early retirement of revenue bonds	31,573	15,112
Interest capitalized	(1,048,167)	(1,342,195)
Total interest expense	$ 1,088,851	$ 721,567

NOTE 11 – CAPITAL LEASE OBLIGATIONS

Capital lease obligations outstanding as of June 30, 2014, are as follows:

Description	**Maturity**	**Interest Rates**	**Original Issue**	**June 30, 2014**
Capital leases - equipment net of interest	October 2011 - July 2017	4.37% - 7.54%	$ 10,155,120	$ 5,719,556
Less current portion				(1,697,107)
				$ 4,022,449

Description	**June 30, 2013**	**Increases**	**Decreases**	**Outstanding June 30, 2014**
Capital lease - equipment	$ 2,902,331	$ 4,009,789	$ (1,192,564)	$ 5,719,556

Description	**June 30, 2012**	**Increases**	**Decreases**	**Outstanding June 30, 2013**
Capital lease - equipment	$ 3,252,071	$ 493,774	$ (843,514)	$ 2,902,331

Debt service requirements for capital lease obligations are as follows:

Year Ending June 30,		
2015	$	1,697,107
2016		1,427,895
2017		973,990
2018		984,185
2019		510,355
Thereafter		126,024
Less interest		-
		5,719,556
Less current portion		(1,697,107)
	$	4,022,449

NOTE 12 – TRANSACTIONS WITH SONOMA VALLEY HOSPITAL FOUNDATION

Sonoma Valley Hospital Foundation, Inc. (the "Foundation") is authorized by the District to solicit contributions on behalf of the Hospital. In the absence of donor restrictions, the Foundation has discretionary control over the amounts, timing, and use of their distributions. The District recorded contributions from the Foundation of $3,757,072 in 2014 and $858,727 in 2013. At June 30, 2014 and 2013, the Foundation's unaudited cash basis financial statements reported net position of $286,841 and $61,591, respectively. The Foundation is not considered a component unit of the District because the Foundation is not controlled by the District.

NOTE 13 – RELATED PARTY TRANSACTIONS

During 2010, the District contributed $100,000 to Meritage for the development of Prima Medical Foundation ("PMF"), a joint venture with Meritage, Marin Healthcare District ("MHD"), and Marin Medical Practice Concepts, Inc. ("MMPC"). The PMF's purpose is establishing, operating, and maintaining multi-specialty medical clinics. The successful establishment and operation of PMF in Marin and Sonoma Counties is expected to be a cornerstone in the District's plans to ensure adequate health care services to the greater Sonoma Area. The District's contribution to PMF totaled $604,413 and $787,560 for the years ended June 30, 2014 and 2013, respectively.

NOTE 14 – COMMITMENTS AND CONTINGENCIES

Litigation – The District is a defendant in various legal proceedings arising out of the normal conduct of its business. In the opinion of management and its legal representatives, the District has valid and substantial defenses, and settlements or awards arising from legal proceedings, if any, will not exceed existing insurance coverage, nor will they have a material adverse effect on the financial position, results of operations, or liquidity of the District.

Operating leases – The District leases certain facilities and equipment under long-term, noncancelable operating lease agreements. Total rental expense for all operating leases amounted to $746,000 and $686,944 in 2014 and 2013, respectively, and is included in other expenses in the consolidated statements of revenues, expenses, and changes in net position. The following is a schedule by year of future minimum lease payments under operating leases that have initial or remaining terms in excess of one year:

Year Ending June 30,	
2015	$ 1,276,899
2016	581,142
2017	492,037
2018	401,679
2019	401,679
	$ 3,153,436

Regulatory environment – The health care industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. The District is subject to routine surveys and reviews by federal, state, and local regulatory authorities. The District has also received inquiries from health care regulatory authorities regarding its compliance with laws and regulations. Although the District's management is not aware of any violations of laws and regulations, it has received corrective action requests as a result of completed and on-going surveys from applicable regulatory authorities. Management continually works in a timely manner to implement operational changes and procedures to address all corrective action requests from regulatory authorities. Breaches of these laws and regulations and non-compliance with survey corrective action requests could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

NOTE 15 – CHARITY CARE

During the years ended June 30, 2014 and 2013, the District provided in estimated costs of $296,250 and $724,137, respectively, for free or discounted services for the poor and underserved. This includes services provided to persons who have health care needs and are uninsured, under-insured, and ineligible for a government program and are otherwise unable to pay for medically necessary care based on their individual financial situation. Costs are computed based on a relationship of costs to charges similar to a Medicare cost to charge ratio. During the year ended June 30, 2014, there were approximately 157 patient cases under this policy. During the year ended June 30, 2013, there were approximately 93 patient cases under this policy.

SUPPLEMENTARY INFORMATION

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UNCOMPENSATED CARE AND COMMUNITY SUPPORT

Uncompensated care – In September 2004, the District adopted a formal community benefits policy, developed under guidelines provided by the California Hospital Association, and began to identify those patients who are medically indigent. The District's policy is to provide service to all who require it, regardless of their ability to pay. As such, it provides substantial amounts of uncompensated care. When this care is provided to patients who lack financial resources (and therefore are deemed medically indigent), it is classified as community benefits. When it is provided to patients who have the means to pay but decline to do so, it is classified as a provision for uncollectible accounts. Neither community benefits nor the provision for uncollectible accounts is reflected in net patient service revenues.

In addition, the District provides services to other medically indigent patients under certain government-reimbursed public aid programs. Such programs pay providers amounts that are less than established charges for the services provided to the recipients and frequently the payments are less than the cost of rendering the services. Finally, some undetermined portion of the provision for uncollectible accounts represents care to indigent patients who the District has been unable to identify.

Uncompensated charges relating to these services are as follows:

	2014	2013
Community benefits (charity care) allowances	$ 269,201	$ 186,468
State Medi-Cal and other public aid programs	25,003,025	21,942,805
Provision for uncollectible accounts	1,458,255	2,901,255
Total	$ 26,730,481	$ 25,030,528

The District's estimated costs of providing uncompensated care and community benefits to the poor and the broader community for 2014 and 2013 are as follows:

	2014	2013
Uncompensated costs of community benefits and uncollectible accounts	$ 51,363	$ 201,586
Medi-Cal and other public aid programs	2,776,415	2,359,502
	2,827,778	2,561,088
Benefits for the broader community	9,747,878	8,706,914
Total estimated community benefit costs	$ 12,575,656	$ 11,268,002

Benefits for the broader community include the unpaid costs of providing service to the elderly, providing health screenings and other health-related services, training health professionals, educating the community with various seminars and classes, and the costs associated with providing free clinics and other community service programs.

Community support – The District also commits significant time and resources to endeavors and critical services that meet otherwise unfilled community needs. Many of these activities are sponsored with the knowledge that they will not be self-supporting or financially viable. Such programs include recruitment of physicians, health screening and assessments, prenatal education and care, community educational services, and various support groups.

During 2014 and 2013, the District recorded the following amounts related to community support:

	2014	2013
Noncapital gifts and grants included in non operating revenues	$ 18,333	$ 232,596
Capital grants and contributions from		
Sonoma Valley Hospital Foundation	3,757,072	858,727
Others	-	3,000,000
	3,757,072	3,858,727
Total community support	$ 3,775,405	$ 4,091,323
Fundraising expenses included in operating expenses	$ 136,466	$ 417,691