



Report of Independent Auditors
and Financial Statements

**Public Hospital District No. 1
of Skagit County, Washington**

December 31, 2022 and 2021

Table of Contents

	Page
Management’s Discussion and Analysis	1
Report of Independent Auditors	22
Financial Statements	
Statements of Net Position	26
Statements of Revenues, Expenses, and Changes in Net Position	28
Statements of Cash Flows	29
Notes to Financial Statements	31
Report of Independent Auditors on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	59
Required Supplementary Information	
Schedule of Changes in Total Other Post-Employment Benefits and Related Ratios	62

Management's Discussion and Analysis

Public Hospital District No. 1 of Skagit County, Washington

Management's Discussion and Analysis

Years Ended December 31, 2022 and 2021

This discussion and analysis provides an overview of the financial position and financial activities of Public Hospital District No. 1 of Skagit County, Washington (the District). The District, doing business as Skagit Valley Hospital (SVH), added the clinic division on July 1, 2010. The clinic division, which is known as Skagit Regional Clinics (SRC), was acquired when SVH employed the physicians of the former Skagit Valley Medical Center (SVMC) and started operations. On January 1, 2011, the District created the system name Skagit Regional Health (SRH). This name encompasses both SVH and the SRC operations. On June 1, 2016, the District began leasing the facilities of Public Hospital District No. 3 of Snohomish County and providing hospital and clinic services under the name Cascade Valley Hospital and Clinics (CVH).

Please read this discussion and analysis in conjunction with the accompanying financial statements and accompanying notes, which follow this section.

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. 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 it. Over time, increases or decreases in the District's net position are one indicator of whether its financial health is improving or deteriorating.

Financial Highlights

- SRH's total operating revenue grew by 6.0%, or \$29.6 million, from \$494.0 million in 2021 to \$523.6 million in 2022. Over the same period, total operating expenses grew by 9.6%, or \$48.1 million, from \$501.5 million in 2021 to \$549.6 million in 2022.
- SRH ended 2022 with a net operating loss of \$26.1 million, a change of \$18.5 million from the net operating loss of \$7.5 million recognized in 2021. In 2022, SRH had net non-operating income of \$2.3 million, Capital contributions of \$0.3 million, and a Gain on transfer of assets of \$1.1 million. This resulted in a decrease in net position of \$22.3 million for the year.
- In December 2021, the District carried out the advance refunding of the outstanding Hospital Revenue Improvement and Refunding Bonds, 2013A, with the issuance of the Hospital Revenue Refunding Bond, Series 2021. The advance refunding will save the District a total of \$4.3 million and a net present value savings of \$3.4 million at the time of issuance.
- The District has made a strategic investment of approximately \$72 million for the five-year span of 2016–2020 to build a new Electronic Health Record (EHR) and selected Epic as the vendor in 2015. The new EHR is a powerful, state-of-the-art tool that provides system interoperability, connectivity with patients, access to information, and data sharing across the District's entire system, including SVH, SRC, and CVH. The EHR became operable across the system in October 2017.
- In 2022, the District issued a Request for Proposal for the replacement of the District's Enterprise Resource Planning (ERP) System with the vision of achieving clinical and business system operational efficiency and excellence through a fully integrated system. After a thorough review of the responses the District selected the Infor CloudSuite solution. Implementation of the ERP system began in 2022 and is expected to take at least three years to become fully operable. The total cost of the system including both capital and operating costs is expected to be \$11.2 million.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

- In 2022, the District adopted the Governmental Accounting Standards Board (GASB) Statement No. 87, *Leases* (Statement 87). Statement 87 changed the accounting and reporting for leases by establishing a single model for lease accounting based on the foundational principle that leases represent a financing of the right to use an underlying asset. Statement 87 applies to contracts that convey a right to use a non-financial asset in exchange or exchange-like transaction for a term exceeding 12 months. Under Statement 87, a lessee is required to recognize a lease liability and an intangible right to use asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The District has applied the new standard retroactively to the year ending December 31, 2021. Accordingly, the 2020 financial information included in management's discussion and analysis has not been adjusted for the impact of GASB 87. As a result, the District recognized \$72.4 million in assets made up of \$67.3 million in right to use assets, net of accumulated amortization, \$4.8 million in long term lease receivable, and \$0.3 million in other current assets. In addition, the District recognized \$72.4 million in liabilities and deferred outflows, made up of \$62.1 million in long-term lease liability, \$6.3 million in current portion of lease liability, \$94 thousand in accrued interest payable, and \$5.0 million in deferred lease inflows. See Note 5 in the accompanying notes to financial statements for additional information.

- The District entered into an agreement to construct the Station Square facility, a three-story 30,000 square foot medical office building in downtown Mount Vernon, less than a mile west of SVH's main campus. The construction began in August 2021 and was completed on time and on budget, opening to patients January 9, 2023. The building was constructed and owned by a real estate developer, and leased by SRH. The Station Square facility helps address the need for additional medical office space, as well as the need for primary care services in the community, by offering services including primary care, urgent care, lab and imaging, all operated as departments of SRH. The District has an option to purchase this building in 2024.

- On June 30, 2022, construction broke ground on a three-story 60,000 square foot outpatient surgery center and medical office building, located just northwest of SVH in Mount Vernon. The addition of the Mount Vernon Surgery Center will help meet the need of our surgical patients with a facility and environment that is designed specifically for outpatient procedures and relieve pressure on the six operating rooms at SVH, where the focus will remain with patients who will need to receive hospital care following surgery and emergent procedures. The Mount Vernon Surgery Center has a December 2023 target opening and will contain four operating rooms, three endoscopy suites, one procedure room, diagnostic imaging, lab and several specialty clinics, including Gastroenterology; Ear, Nose and Throat; and Orthopedics and Sports Medicine. Other surgical specialties that will provide services in the new surgical center include, but is not limited to, urology, general surgery, podiatry, plastic surgery, gynecology, pain management and orthopedic spine surgery. The building is being constructed and will be owned by a real estate developer, and leased by SRH.

Public Hospital District No. 1 of Skagit County, Washington

Management's Discussion and Analysis

Years Ended December 31, 2022 and 2021

- Tamara Ceseña, MBA was promoted to Regional Vice President and Chief Financial Officer (CFO) in January 2023 after serving in a variety of finance roles in the organization since 1994. Ceseña takes on the role held by CFO Paul Ishizuka who retired in the end of January 2023 after serving the District for 5 years. Ceseña started with Skagit Regional Health (then known as Affiliated Health Services) in 1994, departing for a brief stint with Providence Medical Center in 2000 before returning to the organization. Her roles at Skagit Regional Health have spanned titles including Reimbursement Manager, Revenue Cycle Director and Vice President of Finance. She was the leader in the 2016 consolidation of the revenue cycle structure at Skagit Regional Health in addition to having oversight of value-based initiatives, payer contracting and governmental reporting functions. Ceseña holds a Bachelor of Arts from Western Washington University and a Master's in Business Administration in Healthcare Administration from City University.

COVID-19

On February 29, 2020, the Governor of the State of Washington, Jay Inslee, declared a state of emergency after the first known death attributed to COVID-19 in the State of Washington occurred in the Seattle metropolitan area. Shortly thereafter, the World Health Organization declared the COVID-19 outbreak a global pandemic. On March 13, 2020, President Trump declared a national state of emergency with respect to the COVID-19 pandemic, ordering all states to establish emergency operations and authorizing the use of federal funds. On March 18, 2020 pursuant to direction from the State of Washington, SRH began canceling or postponing non-urgent and elective procedures.

On March 23, 2020, Governor Inslee issued a "Stay Home, Stay Healthy" proclamation, which included an order to halt certain elective procedures including surgeries, outpatient procedures and dental services to preserve the availability of critical equipment for health care workers caring for COVID-19 positive patients. Gov. Inslee issued a proclamation on May 18, 2020 defining the state's plan for the resumption of non-urgent medical and dental procedures. The plan requires an assessment of the organization's readiness as well as the current COVID-19 activity in the community to determine the appropriateness of reopening. As part of the assessment, the proclamation requires specific criteria related to screening, personal protective equipment (PPE), social distancing and hygiene, surge capacity, telemedicine, and others, to be met in order to resume non-urgent procedures. SRH met the requirements defined in the proclamation and resumed non-urgent procedures the week of May 18, 2020.

In response to a surge of COVID-19 related hospitalizations in November of 2020, SRH postponed elective surgical procedures that required an inpatient stay through the end of the year.

The Food and Drug Administration issued emergency use authorization of the Pfizer-BioNTech and Moderna COVID-19 Vaccines for use in individuals 18 years of age or older in the fall and winter of 2020. The District began operating vaccination clinics to administer the vaccines to those eligible according to the risk based rollout plan defined by the State of Washington. The District continued to operate the vaccination clinics as supplies increased through the first half of 2021, including the addition of a third vaccine approved for emergency use authorization developed by Johnson & Johnson, and more individuals became eligible. SRH adapted operations to include access to Covid-19 vaccine booster shots as they became available in 2021.

Public Hospital District No. 1 of Skagit County, Washington

Management's Discussion and Analysis

Years Ended December 31, 2022 and 2021

Coinciding with the vaccine rollout, the COVID-19 pandemic continued to evolve throughout 2021 mutating into several new variants, resulting in surges in infections and hospitalizations. These surges, along with nationwide labor shortages, global supply chain challenges, and inflationary pressures strained operations and increased costs.

In January of 2022, as a result of the emergence of the "Omicron" variant, Governor Inslee issued a proclamation restricting non-urgent medical procedures from January 17, 2022 through February 17, 2022. In addition, increased inflationary pressures on drugs and supplies along with worsening labor disruption and costs continued to negatively impact costs resulting in a \$26.1 million operating loss for the District in 2022.

Major federal and state stimulus and liquidity support came in in several forms described below:

- **Medicare Accelerated and Advance Payment Program:** SRH applied for expedited Medicare payments through the Centers for Medicare and Medicaid Services Medicare Accelerated and Advance Payment Program. SRH received approximately \$8 million in funds through the program in June of 2020 and a second advance of approximately \$35 million in September of 2020. At the time of receipt, repayment of the funds was set to begin 120 days after the funds were received. SRH repaid the \$8 million advance in September 2020. In October, the Continuing Appropriations Act, 2021 and Other Extensions Act amended the repayment terms to begin one year after funds were received. At December 31, 2020, SRH had a current liability of \$35,247,911 related to these funds. In September 2021, SRH repaid the \$35 million advance in full.
- **CARES Act Provider Relief Funds:** The Coronavirus Aid, Relief, and Economic Security (CARES) Act provided more than \$170 billion to be distributed to health care providers to address, in part, the loss of revenue resulting from reduced elective procedures and the cost incurred in caring for COVID-19 patients. The distribution of these funds began in April 2020 and continued through November 2021 in several general and targeted distributions. SRH has received approximately \$25 million in funds through December 2021. SRH has recognized all of these funds as non-operating revenues on the Statements of Revenues, Expenses, and Changes in Net Position in the years ended December 31, 2021 and 2020.
- **CARES Act FICA Deferral:** The CARES Act also provided for interest free payment deferral of the employer's portion of Social Security taxes that would otherwise be required to be paid during the period beginning March 27, 2020, and ending December 31, 2020. This deferred payment is to be repaid in two installments, SRH repaid 50% of the deferred amount in December 2021, and the remaining 50% was paid in December 2022. As a result, SRH had a liability of \$7,727,975 and \$3,863,987 related to this deferral at December 31, 2020 and December 31, 2021, respectively.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

- **FEMA Public Assistance Program:** SRH applied for a \$2.0 million expedited funding grant from the Federal Emergency Management Agency (FEMA) Public Assistance Program, covering the timeframe of March 1 to September 22, 2020. Meant to offset incremental expenses incurred as a result of the COVID-19 pandemic. This funding channel allows for an organization to receive 50% of estimated expenses prior to project close (after removing a 25% state cost share requirement). As of December 31, 2021, SRH received approximately \$1.2 million through this funding source. Of this \$1.2 million, SRH recognized \$972 thousand in 2020 and \$270 thousand in 2021 as non-operating revenue on the Statements of Revenues, Expenses, and Changes in Net Position. SRH continues to submit claims to FEMA for expenses incurred across 2021. In 2022, covering the time period up to June 30, 2022, SRH submitted an additional \$5.7 million in pandemic related expenses. Of this total, \$1.5 million has been funded or obligated to date with the remainder under active review.

- **Other federal, state, and other expense grants:** SRH received additional funding from several sources, including funds made available through the CARES Act and passed through the State of Washington, PPE grants made available through the Washington State Hospital Association, as well as other federal, state and other organization grants. These funds totaled approximately \$0.5 million and \$1.0 million and were recognized in 2021 and 2020 on the Statements of Revenues, Expenses, and Changes in Net Position, respectively.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Operating Statistics

Following are key operating statistics for the years ended December 31, 2022, 2021, and 2020:

Statistical Volumes and Definitions ⁽¹⁾

VOLUME	2022	2021	2020
Skagit Valley Hospital			
Admissions (excludes Newborns)			
Medical/Surgical	5,599	5,828	6,018
Obstetrics	1,101	944	872
Behavioral Health	371	395	308
Total Admissions	<u>7,071</u>	<u>7,167</u>	<u>7,198</u>
Discharges (excludes Newborns)			
Medical/Surgical	5,582	5,741	5,926
Obstetrics	1,053	918	866
Behavioral Health	383	402	335
Total Discharges	<u>7,018</u>	<u>7,061</u>	<u>7,127</u>
Patient Days (excludes Newborns)			
Medical/Surgical	34,441	31,935	29,570
Obstetrics	1,767	1,696	1,613
Behavioral Health	3,653	3,904	3,972
Total Patient Days	<u>39,861</u>	<u>37,535</u>	<u>35,155</u>
Average Length of Stay (excludes Newborns)			
Medical/Surgical	6.17	5.56	4.99
Obstetrics	1.68	1.85	1.86
Behavioral Health	9.54	9.71	11.86
Total Overall Average Length of Stay	5.68	5.32	4.93
Inpatient Occupancy (excludes Newborns)	79.7%	75.1%	70.1%
Surgical Cases			
Inpatient Cases	1,073	1,050	1,394
Outpatient Cases	5,829	5,586	4,333
Total Surgical Cases	<u>6,902</u>	<u>6,636</u>	<u>5,727</u>
Endoscopy Cases	6,792	6,763	5,850
Deliveries	888	861	810
Emergency Department Visits ⁽²⁾	33,733	31,895	29,306
Oncology Visits			
Medical Visits	21,708	19,851	18,392
Radiation Therapy Visits	10,466	10,708	11,130
Total Oncology Visits	<u>32,174</u>	<u>30,559</u>	<u>29,522</u>
Diagnostic Imaging Procedures			
CT	25,051	21,938	20,254
MRI	9,786	9,206	8,275
X-Ray	74,823	68,199	57,639
Other Diagnostic Imaging	41,079	37,861	34,386
Total Diagnostic Imaging Procedures	<u>150,739</u>	<u>137,204</u>	<u>120,554</u>
Cath Lab Procedures	3,543	3,611	3,328

⁽¹⁾ Volumes include all patients unless otherwise noted.

⁽²⁾ Includes those patients who are later admitted.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Statistical Volumes and Definitions ⁽¹⁾

VOLUME	2022	2021	2020
Cascade Valley Hospital			
Admissions (excludes Newborns)			
Medical/Surgical	1,429	1,166	1,187
Obstetrics	211	144	141
Total Admissions	1,640	1,310	1,328
Discharges (excludes Newborns)			
Medical/Surgical	1,422	1,152	1,176
Obstetrics	203	140	138
Total Discharges	1,625	1,292	1,314
Patient Days (excludes Newborns)			
Medical/Surgical	8,010	5,042	4,909
Obstetrics	389	246	238
Total Patient Days	8,399	5,288	5,147
Average Length of Stay (excludes Newborns)			
Medical/Surgical	5.63	4.38	4.17
Obstetrics	1.92	1.76	1.72
Total Overall Average Length of Stay	5.17	4.09	3.92
Inpatient Occupancy (excludes Newborns)	47.9%	30.2%	29.3%
Surgical Cases			
Inpatient Cases	446	470	517
Outpatient Cases	1,375	1,385	1,079
Total Surgical Cases	1,821	1,855	1,596
Endoscopy Cases	1,409	1,207	822
Deliveries	186	129	127
Emergency Department Visits ⁽²⁾	22,218	18,937	17,102
Diagnostic Imaging Procedures			
CT	9,186	7,854	6,833
MRI	1,466	1,245	1,243
X-Ray	12,694	11,797	11,347
Other Diagnostic Imaging	11,589	10,720	8,543
Total Diagnostic Imaging Procedures	34,935	31,616	27,966
Skagit Regional Health - Clinics			
Provider Clinic Visits			
Primary Care Clinic Visits	207,046	191,696	171,050
Specialty Care Clinic Visits	203,877	187,755	149,862
Total Provider Clinic Visits	410,923	379,451	320,912

⁽¹⁾ Volumes include all patients unless otherwise noted.

⁽²⁾ Includes those patients who are later admitted.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Performance Overview

The following is a comparison of 2022 actual revenues, expenses, and changes in net position results to 2021 and 2020 results (in thousands):

	<u>2022</u>	<u>2021 ⁽¹⁾</u>	<u>2020</u>
Operating revenues			
Net patient service revenue	\$ 492,083	\$ 463,178	\$ 397,012
Other operating revenues	<u>31,486</u>	<u>30,792</u>	<u>31,189</u>
Total operating revenues	<u>523,569</u>	<u>493,970</u>	<u>428,201</u>
Operating expenses			
Salaries and wages	240,993	227,549	197,389
Employee benefits	53,225	55,817	50,463
Professional fees	41,672	22,326	19,748
Supplies	95,054	83,177	70,851
Purchased services and other	87,189	80,127	76,663
Depreciation and amortization	25,440	25,208	18,061
Interest and amortization	<u>6,052</u>	<u>7,294</u>	<u>5,669</u>
Total operating expenses	<u>549,625</u>	<u>501,498</u>	<u>438,844</u>
Operating loss	(26,056)	(7,528)	(10,643)
CARES Act Provider Relief Fund and other assistance	1,551	4,828	21,519
Gain on termination of participation in PEBB	-	28,436	-
Other nonoperating income, net	<u>779</u>	<u>2,974</u>	<u>4,623</u>
Nonoperating income, net	2,330	36,238	26,142
Capital contributions	311	188	-
Gain on transfer of assets	<u>1,143</u>	<u>1,237</u>	<u>1,269</u>
Change in net position	(22,272)	30,135	16,768
Net position, beginning of year	<u>213,772</u>	<u>183,637</u>	<u>166,869</u>
Net position, end of year	<u>\$ 191,500</u>	<u>\$ 213,772</u>	<u>\$ 183,637</u>

⁽¹⁾ The 2021 amounts have been adjusted for adoption of GASB 87.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Health Care Outlook

2022 was one of the most financially challenging years ever for the healthcare industry due to COVID-19 and its aftermath. The repercussions of the pandemic leave the industry, and SRH, in a precarious position with labor shortages across most health care roles and the need to rely on agency labor to maintain operations. In addition, supply chain shortages and inflation have driven up the cost of drugs, patient supplies, and almost every other category of services needed to run a Health System. Many of those issues are systemic in nature and impossible to control or understand how they may play out in the future. Despite the uncertainty, SRH has developed a comprehensive \$35 million Financial Improvement Plan to help offset these costs over which we have little control. This plan was rolled out in the fall of 2022 and performance against same continues to be a focus of every level of SRH leadership, including the publicly elected board. The improvement plan is growth focused but also looks to eliminate waste, inefficiencies, non-essential spend and to leverage technology when appropriate.

Reimbursement increases for patient services from both governmental and commercial payers have not kept up when compared to inflation. We expect these reimbursement challenges to continue as eventually the consumer must be able to bear the increased premium costs. In addition, Washington State has instituted a Health Care Cost Transparency Board (HCCTB) with the intention of reducing the state's overall growth of health care cost. It is uncertain how the HCCTB will address the real inflationary pressures experienced by providers. SRH continues to focus on leveraging technology and process to reduce denials in an effort to appropriately optimize reimbursements for services provided.

SRH's service area includes North Snohomish, Skagit, and Island Counties. The population in this geography is growing rapidly and demand for services are high. SRH continues to successfully recruit both primary and specialty care providers to meet the healthcare needs of the community which supports the growth strategy of the financial improvement plan. In addition, continued focus on providing Value Based Care that provides the right service to the right patient in the appropriate setting is front of mind and we continue to make progress in this space for commercial, state and Medicare accountable care organization products.

While there remains much uncertainty in the Health Care environment, management is confident in its ability to adapt and execute upon strategies that will result in improved financial performance so that we are able to meet our mission of providing the highest quality services to the members of our communities.

Operating Revenue (in thousands)

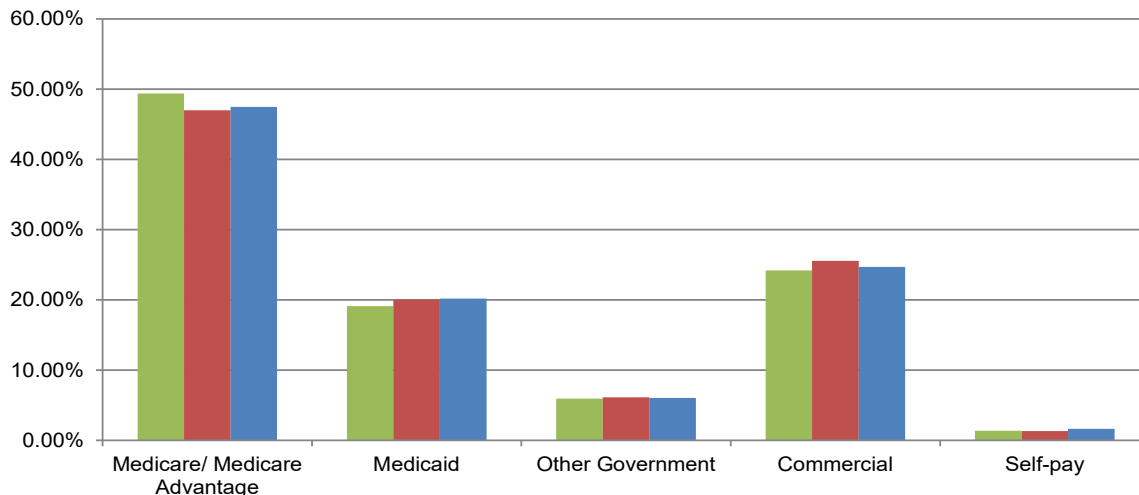
Net Patient Revenue

Net patient revenue consists of gross patient charges less contractual adjustments, financial assistance, and a provision for bad debt. Contractual adjustments represent the difference between gross patient charges at established rates and expected contracted payments from third-party payors with which the District has entered into agreements. In addition, the District provides care to patients, at no charge or reduced rates, who meet certain criteria under its financial assistance policies. The District also estimates the collectability of accounts receivable and records a provision for bad debt. The resulting net patient revenue is highly dependent on the District's payor mix and patient utilization patterns.

Public Hospital District No. 1 of Skagit County, Washington
Management’s Discussion and Analysis
Years Ended December 31, 2022 and 2021

The table and graph below illustrate the three-year trend in SRH’s payor mix, based on gross patient charges, for the years ended December 31, 2020 through 2022.

Payor Mix	Years Ended December 31,		
	2022	2021	2020
Medicare / Medicare Advantage	49.39%	46.99%	47.46%
Medicaid	19.12%	20.03%	20.18%
Other Government	5.93%	6.12%	6.03%
Commercial	24.19%	25.55%	24.69%
Self Pay	1.37%	1.31%	1.64%
	100.00%	100.00%	100.00%



In 2022, SRH net patient service revenue increased by \$28,905 (6.2%) compared to 2021. Increases in inpatient and outpatient hospital volumes and clinic visits is the primary driver of this increase. In 2021, net patient service revenue increased by \$66,166 (16.7%) compared to 2020, this increase is primarily due to volume increases in 2021 related to the return of procedures that were delayed as a result of the pandemic from March to May of 2022 and an increase in commercial payor mix.

Other Operating Revenue

Other operating revenue increased by \$694 (2.3%) from \$30,792 in 2021 to \$31,486 in 2022. In 2021, other operating revenue decreased by \$397 (1.3%) over \$31,189 in 2020. Increased revenues in the contracted pharmacy program were partially offset by unfavorable market value adjustments on restricted funds are the main drivers for this variance in 2022. In 2021, decrease revenues in the contracted pharmacy program and unfavorable market value adjustments on restricted funds are the main drivers for this variance.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Operating Expenses (in thousands)

Total operating expenses in 2022 increased by \$48,127 (9.6%), from \$501,498 in 2021 to \$549,625 in 2022. Total operating expenses increased by \$62,654 (14.3%) in 2021, from \$438,844 in 2020.

Excluding providers, the District employed 1,960 full time equivalents (FTEs) for the year ending December 31, 2022, which was a decrease of 1 FTE from the 1,961 FTEs employed in the same period in 2021, and a two-year increase of 65 FTEs from the 1,895 FTEs employed in the same period in 2020. FTE growth was hampered in 2022 due to employee turnover as well as difficulty in recruiting new candidates for employment, particularly for Registered Nurses.

At year-end 2022, SRH employed 249 providers, comprised of 142 doctors, 34 residents, and 73 mid-level providers. This is a decrease of 9 employed providers from year-end 2021, comprised of 5 doctors and 4 mid-level providers. This decrease was due to normal attrition and relocation of providers seeking employment elsewhere. Graduate medical education resident numbers remained unchanged year over year.

Salaries and benefits increased by \$10,852 (3.8%), from \$283,366 in 2021 to \$294,218 in 2022. Growth in salaries is related to union and non-union staff and provider wage increases, including one-off market adjustments, as well as additional spending for shift incentive pay and signing bonuses. In 2021, salaries and benefits increased by \$35,514 (14.3%) from \$247,852, in 2020. Wage growth due to Collective Bargaining Agreements and volume related FTE growth were the primary drivers of this increase.

Professional fees increased by \$19,346 (86.7%) from \$22,326 in 2021 to \$41,672 in 2022. Increased utilization of contract labor along with associated market driven increases in rates accounted for the majority of this increase. In 2021, professional fees increased by \$2,578 (13.1%), from \$19,748 in 2020. Increased contract labor use and higher hourly wage rates across several areas including the District's laboratories, Health Information Management, surgical and emergency services and COVID-19 screeners accounted for the majority of this variance.

The District's supply expense increased by \$11,877 (14.3%) from \$83,177 in 2021 to \$95,054 in 2022. Inflationary pressures on the supply chain along with the continued recovery in 2022 of surgical and endoscopy services volumes that were lost or deferred in 2021 and 2020 were the primary drives of this increase.

The previous year showed a larger increase in supply expense of \$12,326 (17.4%), from \$70,851 for 2020 to \$83,177 for 2021. The recovery in 2021 of surgical and endoscopy services volumes that were lost or deferred in 2020, paired with an increase in the number of providers led to an overall increase in patient volumes. Additionally, growth in high supply spend departments such as cardiac catheterization and robotic surgery also contributed to the increase in supply expenses. This rebound was not as evident in the oncology service line; however consistent growth in both high-costs drugs and patient volumes still contributed to the overall increase in supply expense for 2021 when compared to 2020.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Purchased services and other expenses increased in 2022 by \$7,062 (8.8%) to \$87,189, from \$80,127 in 2021. This increase was primarily related to an increase in usage of subscription based information technology arrangements including the new ERP system. Additional variances include increases insurance premiums and increased third party recruitment services. Purchased services and other expenses increased \$3,464 (4.5%), from \$76,663 in 2020 to \$80,127 in 2021. This increase was primarily related to an increase in usage of information technology purchased services and software license fees. Additional variances include increases in rents and leases, insurance premiums, and taxes.

Depreciation and amortization expense of \$25,440 in 2022 was \$232 (0.9%) higher than the 2021 depreciation and amortization expense of \$25,208. In 2021, depreciation expense increased \$7,147 (39.6%) over the 2020 expense of \$18,061. The implementation of the GASB 87 lease standard was retroactively applied to 2021 and accounts for the variance between 2020 and 2021. Due to financial challenges, the District modified its capital spend to focus on patient quality and safety-related capital needs. Major capital purchases in 2022 included the furnishing of the new Station Square medical office building, implementation costs related to the new Infor CloudSuite ERP System, and remodeling of the Cardiac Catheterization Lab and Linear Accelerator vault.

Interest and amortization expense decreased by \$1,242 (17.0%) to \$6,052 in 2022, from \$7,294 in 2021. In 2021, interest and amortization expense increased by \$1,625 (28.7%), from \$5,669 in 2020. Interest rate savings related to the refinancing of the 2013 Revenue Bonds is the primary driver for the variance in 2022. The interest portion of the GASB 87 lease standard was the driver of the increase from 2020 to 2021.

Net Nonoperating Income and Other Changes in Net Position (in thousands)

Net nonoperating income and other changes in net position decreased by \$33,908 (93.6%) from \$36,238 in 2021 to \$2,330 in 2022 and increased in 2021 by \$10,096 (38.6%) from \$26,142 in 2020. The \$33,908 decrease in 2022 was primarily driven by a \$28,436 gain on termination of participation in the Public Employees Benefits Board (PEBB) Program for post-employment benefits reported in 2021, along with unfavorable investment market value adjustments, and reduced funding from the CARES Act Provider Relief Fund and other federal and State Assistance.

Gain on transfers of assets relates to the affiliation agreement with Snohomish County PHD 3 decreased by \$94 in 2022 to \$1,143 from \$1,237 in 2021 and \$1,269 in 2020. Additional information about this transfer can be found in the "Affiliation Agreement with Snohomish County PHD No. 3" section below.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Statements of Net Position (in thousands)

The following is a presentation of certain financial information derived from the District's statement of net position (in thousands):

	2022	2021 ⁽¹⁾	2020
	<u> </u>	<u> </u>	<u> </u>
Current assets			
Cash and short-term investments	\$ 19,256	\$ 37,972	\$ 104,157
Accounts receivable, net	63,039	55,371	51,444
Other current assets	<u>16,155</u>	<u>16,141</u>	<u>14,517</u>
Total current assets	98,450	109,484	170,118
Investments	40,828	36,384	-
Other noncurrent cash and investments, net of current portion	129,802	136,478	137,213
Long term lease receivable	4,562	4,846	-
Capital assets, net	129,500	133,705	140,806
Right to use assets, net	88,957	67,272	-
Investments in joint ventures	<u>13,376</u>	<u>13,362</u>	<u>13,572</u>
Total assets	<u>505,475</u>	<u>501,531</u>	<u>461,709</u>
Deferred outflows of resources	<u>4,408</u>	<u>5,194</u>	<u>14,063</u>
Total assets and deferred outflows of resources	<u>\$ 509,883</u>	<u>\$ 506,725</u>	<u>\$ 475,772</u>
Current liabilities	\$ 86,827	\$ 73,354	\$ 99,127
Lease liability, net of current portion	84,054	62,102	-
Long-term debt, net of current portion	129,572	140,244	150,445
OPEB liability	5,723	5,372	30,731
Estimated professional liability	<u>7,436</u>	<u>6,783</u>	<u>6,421</u>
Total liabilities	<u>313,612</u>	<u>287,855</u>	<u>286,724</u>
Deferred inflows of resources	<u>4,771</u>	<u>5,098</u>	<u>5,411</u>
Net position			
Net investment in capital assets	21,006	17,642	17,197
Restricted for debt service	10,421	10,725	10,663
Unrestricted	<u>160,073</u>	<u>185,405</u>	<u>155,777</u>
Total net position	<u>191,500</u>	<u>213,772</u>	<u>183,637</u>
Total liabilities, deferred inflows of resources, and net position	<u>\$ 509,883</u>	<u>\$ 506,725</u>	<u>\$ 475,772</u>

⁽¹⁾ The 2021 amounts have been adjusted for adoption of GASB 87.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Assets and Deferred Outflows of Resources

Total current assets of \$98,450 at December 31, 2022, were \$11,034 (10.1%) lower than at year-end 2021. This decrease is comprised of a \$18,716 (49.3%) decrease in cash and short-term investments, an increase of \$7,668 (13.8%) in net accounts receivable and an increase of \$14 (0.1%) in other current assets. The decrease in cash and short-term investments in 2022 is related to the losses from operations, debt payments, and transfers to investment with long-term maturities.

Total current assets of \$109,484 at December 31, 2021, were \$60,634 (35.6%) lower than at year-end 2020. This increase is comprised of a \$66,185 (63.5%) decrease in cash and short-term investments, an increase of \$3,927 (7.6%) in net accounts receivable, and an increase of \$1,344 (11.2%) in other current assets. The decrease in cash and current assets in 2021 was related to the repayment of the federal liquidity support and a change in investment portfolio allocation to long-term investments.

Investments increased \$4,444 (12.2%) in 2022 from \$36,384 in 2021. This increase is a combination reallocation of invested funds from short-term to longer term maturities offset by unfavorable market value adjustments. In 2021, the District changed its investment portfolio allocation to include long term investment resulting in an increase of \$36,384 from \$0 in 2020.

The lease receivable assets is the result of the implementation of the GASB 87 lease standard. This standard was applied retroactively to 2021 resulting in the initial asset value of \$4,846 in that year. In 2022 the lease receivable reduced by \$284 (5.9%) to \$4,562 related to scheduled payments received on leased property.

Other noncurrent cash and investments, net of current portion decreased from \$136,478 in 2021 to \$129,802 in 2022, a decrease of \$6,676 (4.9%), after falling by \$735 (0.5%) from \$137,213 in 2020. The decrease in 2022 is related to unfavorable market value adjustment on invested funds and reduced debt service reserves. The decrease in 2021 is also related to unfavorable market value adjustments on investment in addition to reduced debt service reserves.

Net right to use assets, is a new asset on the Statements of Net Positions resulting from the adoption of the GASB 87 lease standard. This standard was applied retroactively to 2021 resulting in the initial balance of \$67,272 in that year. In 2022, net right to use assets increased by \$21,685 (32.2%) to \$88,957, related to new leases entered into in that year. The largest of which is the Station Square Medical Office Building lease.

Net capital assets decreased in 2022 by \$4,205 (3.1%), from \$133,705 to \$129,500. This decrease is comprised of \$13,915 of new capital assets, offset by \$15,124 in retirements and a \$18,119 increase in accumulated depreciation. Net capital assets decreased in 2021 by \$7,101 (5.0%), from \$140,806 to \$133,705. This decrease is comprised of \$10,877 of new capital assets, offset by \$5,104 in retirements and a \$2,995 increase in accumulated depreciation. In response to COVID-19 SRH reduced and deferred approximately 50% of the capital budget in 2021 and 2022, focusing on quality and safety related capital needs.

Investments in joint ventures increased from \$13,362 in 2021 to \$13,376 in 2022, an increase of \$14. Distributions from joint ventures accounted for the change in 2021. Investments in joint ventures decreased from \$13,572 in 2020 to \$13,362 in 2021, a decrease of \$210, due to distributions.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Deferred outflows of resources decreased from \$14,063 in 2020 to \$5,194 in 2021 and then further decreased to \$4,408 in 2022. The decrease in 2021 was related to SRH's exit from the state's PEBB program of \$7,706 and a \$1,163 decrease in deferred losses on refundings.

Liabilities and Deferred Inflows of Resources

Current liabilities increased \$13,473 (18.4%) from \$73,354 in 2021 to \$86,827 in 2022. This increase is comprised of an increase of \$9,953 in accounts payable, an increase of \$1,390 in accrued salaries, wages and employee benefits, a decrease of \$39 in accrued interest, a \$928 increase in estimated payments due to third-party payors, and increases of \$736 and \$504 in the current portion of lease liability and long-term debt respectively. Current liabilities decreased \$25,773 (26.0%) from \$99,127 in 2020 to \$73,354 in 2021, primarily related to the repayment of Medicare Advance Payment Program funds.

Lease liabilities, net of current portion is a new liability on the Statements of Net Position resulting from the adoption of the GASB 87 lease standard. This standard was applied retroactively to 2021 resulting in the initial balance of \$62,102 in that year. In 2022, lease liabilities, net of current portion increased by \$21,952 (35.3%) to \$84,054, related to new leases entered into in that year. The largest of which is the Station Square Medical Office Building lease.

Long-term debt, net of current portion, decreased by \$10,672 (7.6%) in 2022 to \$129,572 from \$140,244 in 2021. In 2021, long-term debt, net of current portion decreased by \$10,201 (6.8%) from \$150,445 in 2020. Annual debt service payments account for the decreases in both years.

The District recognizes other post-employment benefit (OPEB) liabilities in accordance with GASB 74 and GASB 75. GASB 75, requires a liability to be recognized for OPEB plans that are not pre-funded. Changes in the OPEB liability are recognized as expense in the Statements of Revenue, Expenses, and Changes in Net position or reported as deferred inflows/outflows of resources on the Statements of Net Position, depending on the nature of those changes. The District's OPEB liability increased \$351 (6.5%) in 2022 from \$5,372 in 2021 to \$5,723 in 2022. From 2020 to 2021, the District's OPEB liability decreased \$25,359 (82.5%) from \$30,731 to \$5,372. This decrease is related to the District's decision to no longer participate in the PEBB beginning in 2021. Further detail of the District's OPEB liability can be found in Note 11 to the financial statements.

Professional malpractice estimate liability reserve increased by \$653 (9.6%) in 2022, from \$6,783 in 2021 to \$7,436. This increase in estimate is based on an actuarial estimate of the professional malpractice liability, using historic claims and changes in volume. In 2021, Professional malpractice liability reserve increased by \$362 from \$6,421 in 2020 to \$6,783.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

As part of the bond resolutions authorizing the issuance of the 2021 direct placement revenue refunding bond, the 2019 direct placement revenue bond, and the 2016 revenue and refunding bonds, the District agreed to certain covenants regarding liquidity (minimum of 60 days cash on hand (the Liquidity Requirement)) and debt service coverage (minimum of 1.25 debt service coverage ratio (the Coverage Requirement)). The covenants provide that if the District's audited financial statements for any year disclose that the Liquidity Requirement or the Coverage Requirement is not being met, the District is required to retain a hospital consultant for the purpose of making recommendations to the District with a view to restoring compliance with the Liquidity Requirement or the Coverage Requirement, as applicable. If and so long as the District complies in all material respects with the recommendations of such hospital consultant, and so long as the Liquidity Requirement is met and the District's net income available for debt service is at least equal to the annual debt service on the District's outstanding revenue bonds in any year for which the hospital consultant's recommendations are made and any subsequent year for which such recommendations are renewed, the Liquidity Requirement and the Coverage Requirement, as applicable, are deemed satisfied, and the failure of the District to comply with the covenant will not be deemed to be an event of default.

For the year ended December 31, 2022, the District will not meet the Coverage Requirement. In compliance with the covenants, the District will retain a healthcare consultant to provide recommendations to restore compliance with the Coverage Requirement. In addition to the covenants described above, the 2021 direct placement revenue refunding bond contains provisions that allow the bond holder to impose a default interest rate that is 4% higher than the interest rate otherwise payable under the bond for the period during which the Coverage Requirement is not met. The 2021 bond holder also has the option to elect to not convert the taxable rate currently payable on the 2021 bond to a tax-exempt rate on at the conversion date (September 5, 2023) if the Coverage Requirement is not met. The District has requested the 2021 bond holder to consent to a waiver of both provisions.

Affiliation Agreement with Snohomish County PHD No. 3

In accordance with the Affiliation Agreement, which was dated December 4, 2015, the District began operating Cascade Valley Hospital on June 1, 2016. The Affiliation Agreement is structured as a long-term lease (the Lease) between Snohomish PHD No. 3 d/b/a Cascade Valley Hospital and Clinics and the District. Pursuant to the Affiliation Agreement, Snohomish PHD No. 3 leased substantially all of its assets, including Cascade Valley Hospital, certain other clinic facilities, Snohomish PHD No. 3's interest as lessor in certain land leases, and intangible assets, to the District for a term of 30 years. The District will pay Snohomish PHD No. 3 an annual base rent of \$10.00 and is responsible for all costs and expenses associated with the leased assets, including maintenance and capital improvements.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

Financial Arrangement

Pursuant to the Affiliation Agreement, Snohomish PHD No. 3 will transfer all of its cash and cash equivalents in excess of a retained amount to the District by June 2017. The retained amount is equal to Snohomish PHD No. 3's known and contingent liabilities and debts plus a minimum cash balance of \$1,000,000. Thereafter, Snohomish PHD No. 3 will continue to levy and collect excess and regular property tax levies, as well as collect revenues from a lease of a medical office building owned by Smokey Point LLC. Smokey Point LLC is owned 50% by the District and 50% by Snohomish PHD No. 3. The Smokey Point LLC building is a two-story, 40,000-square-foot ambulatory center. The building is leased to UW Medicine, which operates a maternal fetal medicine clinic and the District, which operates an outpatient chemotherapy unit, an urgent care clinic, primary and specialty care clinics, and laboratory and imaging services. Snohomish PHD No. 3's excess property tax levy funds will be used solely for the purpose of paying the debt service on Snohomish PHD No. 3's outstanding unlimited tax general obligation bonds. The proceeds from the Snohomish PHD No. 3 regular property tax levy and the Smokey Point LLC lease will be used to pay Snohomish PHD No. 3's expenses, including the annual debt service on Snohomish PHD No. 3's outstanding limited tax general obligation bonds, and to fund the minimum cash balance of \$1,000,000. To the extent the amount collected by Snohomish PHD No. 3 from its regular property tax levy and the Smokey Point LLC lease exceeds Snohomish PHD No. 3's existing obligations in any year, and the Snohomish PHD No. 3 cash balance is equal to \$1,000,000, the excess funds will be transferred to the District.

In accordance with the Affiliation Agreement, the transferred funds will be deposited in Pool A of the "PHD No. 3 Support Fund." The funds in Pool A will be used by the District to: (1) support the provision of health care services rendered in Snohomish County; (2) pay for capital improvements and equipment located in Snohomish County; (3) pay for health information technology and other capital investments that may be located outside of Snohomish County if it serves both the District facilities and the Cascade Valley Hospital facilities, provided that only that portion of the costs of such improvement and equipment that reasonably relate to Snohomish PHD No. 3's usage of the capital investment shall be allocated to Snohomish PHD No. 3; and (4) to cover any losses incurred by the District in the operation of Cascade Valley Hospital services.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

At the end of each year, the District will deposit into a special fund designated as Pool B of the "PHD No. 3 Support Fund" a portion of the District's net cash flow generated from the District's operations, calculated according to a formula set forth in the Affiliation Agreement but in no case less than 1.5% of the annual net revenue generated by the District's operation of the Cascade Valley Hospital services still in operation, which will be calculated based on a three-year rolling average. The funds in Pool B may generally be used and expended by the District in the following order of priority: (1) to cover any Cascade Valley Hospital operating losses, as defined in the Affiliation Agreement, to the extent the loss is not covered by any remaining funds in Pool A; (2) to reimburse the District for expenses incurred in prior years to cover such operating losses that were not reimbursed in prior years because there were insufficient funds in Pool A or Pool B; (3) to reimburse the District for expenses incurred by the District in prior years to fund capital improvements or equipment located at the Cascade Valley Hospital facilities or for health information technology or other capital investments located elsewhere to the extent it serves both the District and Cascade Valley Hospital facilities, but only for such portion that reasonably relate to Snohomish PHD No. 3's usage of the health information technology or other capital investment, to the extent that such expenses were not reimbursed in prior years because there were insufficient funds available in Pool A or Pool B; (4) to reimburse the District for expenses incurred by the District in the current year to fund Cascade Valley Hospital capital improvements, as defined by the Affiliation Agreement; and (5) subject to certain limitations, for other expenditures that support the provision of health care services in Snohomish County.

Required Services

The Affiliation Agreement obligates the District to provide certain required services in North Snohomish County (identified by zip codes 98223, 98241, 98292, 98271, 98270, 98258, and 98252) for 5, 10, and 30-year periods. The District has the right to determine the appropriate level of required services to meet the needs of the residents of North Snohomish County, such as the number of medical/surgical beds, ICU beds, observation beds, emergency department bays, operating rooms, procedure rooms, examination and treatment rooms, and staffing levels, provided it does so reasonably after appropriate evaluation and analysis of any impact a reduction in level of service may have on the residents of North Snohomish County.

During the five-year period following affiliation (the Five-Year Period), the District must provide OB/GYN, pediatric physician, and related Cascade Valley Hospital facilities services at any location within North Snohomish County, which the District reasonably believes will appropriately serve the needs of the residents of North Snohomish County. The District must, however, continue to provide or cause to be provided, primary care services at the Darrington and Granite Falls clinics during the Five-Year Period.

Public Hospital District No. 1 of Skagit County, Washington
Management's Discussion and Analysis
Years Ended December 31, 2022 and 2021

During the ten-year period following the affiliation (the Ten-Year Period), the District must provide inpatient and outpatient surgery, general inpatient acute services, and orthopedic general surgeons in North Snohomish County. In order to satisfy the Ten-Year Period commitment, the District is required to continuously maintain and operate Cascade Valley Hospital as a general acute care hospital duly licensed by the state of Washington and certified under the Medicare and Medicaid programs, with at least the following services: general inpatient acute services, inpatient surgery, a 24-hour emergency department, observation unit, ancillary medical services to the extent required to maintain state acute care hospital licensure, and an organized medical staff consisting, at a minimum, of primary care physicians, orthopedic surgeons, and general surgeons. The District is granted the right during the Ten-Year Period to modify or reduce the level of service provided at Cascade Valley Hospital provided: (1) it continues to provide an appropriate level of such services in North Snohomish County to meet the needs of residents; and (2) it has given notice to Snohomish PHD No. 3 and allowed Snohomish PHD No. 3 to provide input before said service is eliminated, relocated, modified, or reduced. Nonetheless, if the District elects to discontinue outpatient surgery services at Cascade Valley Hospital during the Ten-Year Period, the District must provide such services during remainder of the Ten-Year Period at an alternative location within North Snohomish County at appropriate levels to meet the needs of residents.

During the Thirty-Year Period following the affiliation, the District must provide a 24-hour emergency department, observation unit, ancillary medical services, and primary care physicians in North Snohomish County. After the Ten-Year Period, the District is entitled to relocate the required services that were subject to the Ten-Year Period commitment and that continue to be subject to the Thirty-Year Period commitment to any location within North Snohomish County that it reasonably believes will appropriately meet the needs of the residents of North Snohomish County.

In the event that the District intends to eliminate, reduce, relocate, or change any required service in a manner not described above, it must give Snohomish PHD No. 3 90 days' advance written notice of such intent (the Change Notice). The Change Notice must include a detailed statement of the reasons for the intended action and must be accompanied by an analysis prepared by a qualified independent health care consultant analyzing the potential impact on the accessibility and availability of health care services for residents of North Snohomish County. Snohomish PHD No. 3 is granted the right to determine, in its sole and absolute discretion, whether it will permit the District to proceed with the requested change. Snohomish PHD No. 3 must notify the District within 90 days of receipt of the Change Notice whether it will permit or deny the requested change. If Snohomish PHD No. 3 fails to respond in writing within 90 days of receipt of the Change Notice, Snohomish PHD No. 3 will be deemed to have approved the proposed service change.

Dispute Resolution

Subject to the parties' right to equitable relief, all controversies, claims, and disputes arising in connection with the Affiliation Agreement must be settled by mutual consultation between the parties, but failing amicable settlement must be settled finally by arbitration, conducted in Seattle, Washington, in accordance with the rules and procedures promulgated by Judicial Dispute Resolution before one arbitrator. The decision of the arbitrator is final and binding on the parties.

Public Hospital District No. 1 of Skagit County, Washington

Management's Discussion and Analysis

Years Ended December 31, 2022 and 2021

Termination and Unwinding

The Affiliation Agreement permits termination of the Affiliation Agreement and an unwinding of the affiliation upon the happening of certain conditions. The Affiliation Agreement may be terminated: (1) by mutual written consent of the District and Snohomish PHD No. 3; (2) by either the District or Snohomish PHD No. 3 in the event of an uncured breach of the Affiliation Agreement or the Lease by the other party; (3) by the District in the event that a catastrophic event occurs that was not caused by the District and makes it no longer viable to continue operating Cascade Valley Hospital services as originally contemplated; (4) by either the District or Snohomish PHD No. 3 if Snohomish PHD No. 3 requires the District to purchase the leased facilities and assets as set forth in a certain provision of the Affiliation Agreement governing damages to the facilities related to the District's negligence; and (5) after six years, by the District if the District has incurred sustained operating losses, as defined in the Affiliation Agreement, in the operation of Cascade Valley Hospital services.

To affect an unwind, the District will transfer all of the facilities and assets owned by Snohomish PHD No. 3 back to Snohomish PHD No. 3 following a process consistent with how they were originally transferred. In addition, the District will transfer to Snohomish PHD No. 3 any remaining cash balance in Pool A or Pool B and will assign in part or grant sublicenses under any electronic health records software license, maintenance, and support services agreements in effect at Cascade Valley Hospital facilities immediately prior to termination.

All of the commitments by Snohomish PHD No. 3 to provide any cash or similar support to the District will terminate after the date the District provides written notice of termination of the Affiliation Agreement or concurrent with the termination of the definitive agreements for any other reason, provided that Snohomish PHD No. 3 will remain obligated to provide any cash or similar support on a pro rata basis for the applicable period of time prior to the notice of termination. The Affiliation Agreement provides provisions for certain operating commitments and specific provisions in event the agreement is discontinued.

Contacting the District's Financial Management

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of Skagit Regional Health's finances and to show the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's financial management at Skagit Regional Health Business Center, 1415 East Kincaid Street, Mount Vernon, Washington 98273.

Report of Independent Auditors

The Board of Commissioners
Public Hospital District No. 1 of Skagit County, Washington

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Public Hospital District No. 1 of Skagit County, Washington, which comprise the statements of net position as of and for the years ended December 31, 2022 and 2021, 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.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the financial position of Public Hospital District No. 1 of Skagit County, Washington as of December 31, 2022 and 2021, and the changes in its net position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards (Government Auditing Standards)*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the District and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Emphasis of Matter – Change in Accounting Principle

As discussed in Note 2 of the financial statements, in 2022, Public Hospital District No. 1 of Skagit County, Washington, adopted the provisions of Government Accounting Standards Board Statement No. 87, *Leases*. Our opinion is not modified with respect to this matter.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the District's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the District's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the accompanying Management's Discussion and Analysis on pages 1 through 21 and the Schedule of Changes in Total Other Post-Employment Benefits and Related Ratios on pages 62 and 63 be presented to supplement the basic financial statements. Such information is the responsibility of management and, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 21, 2023, on our consideration of Public Hospital District No. 1 of Skagit County, Washington's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Public Hospital District No. 1 of Skagit County, Washington's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Public Hospital District No. 1 of Skagit County, Washington's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Moss Adams LLP".

Everett, Washington
April 21, 2023

Financial Statements

Public Hospital District No. 1 of Skagit County, Washington
Statements of Net Position
December 31, 2022 and 2021

	2022	2021
		(As Restated)
ASSETS AND DEFERRED OUTFLOWS OF RESOURCES		
CURRENT ASSETS		
Cash	\$ 16,831,407	\$ 23,967,923
Short-term investments	2,424,640	14,004,164
Patient accounts receivable, less allowance for uncollectible accounts of \$7,506,019 and \$6,344,336	58,084,335	51,750,646
Other receivables	4,954,801	3,620,020
Supplies inventory	8,110,311	7,794,301
Prepaid expenses and other assets	6,283,144	6,541,821
Interest receivable	85,557	15,688
Current portion of restricted cash and investments required for current liabilities	1,391,989	1,517,480
Current portion of lease receivable	284,188	273,061
	98,450,372	109,485,104
	40,827,991	36,383,565
INVESTMENTS		
OTHER NONCURRENT CASH AND INVESTMENTS		
Board-designated for capital improvements	108,218,286	110,802,541
Board-designated for professional liability	1,617,093	1,646,655
Restricted for CVH project funds A & B	10,937,115	14,821,187
Restricted bond reserve funds held by trustee	9,028,830	9,207,660
Restricted for bond redemption fund	1,391,989	1,517,480
	131,193,313	137,995,523
Less amounts required for current liabilities	(1,391,989)	(1,517,480)
	129,801,324	136,478,043
LONG TERM LEASE RECEIVABLE		
	4,561,785	4,846,027
CAPITAL ASSETS		
Land	11,712,330	11,712,330
Construction in progress	3,978,805	750,333
Depreciable capital assets, net of accumulated depreciation	113,809,276	121,242,261
	129,500,411	133,704,924
RIGHT TO USE ASSETS, net		
	88,957,071	67,272,054
INVESTMENTS IN JOINT VENTURES		
	13,376,347	13,361,605
Total assets	505,475,301	501,531,322
DEFERRED OUTFLOWS OF RESOURCES		
Deferred OPEB outflows	27,930	-
Deferred losses on refundings	4,380,214	5,193,818
	4,408,144	5,193,818
Total deferred outflows of resources	4,408,144	5,193,818
Total assets and deferred outflows of resources	\$ 509,883,445	\$ 506,725,140

See accompanying notes.

Public Hospital District No. 1 of Skagit County, Washington
Statements of Net Position
December 31, 2022 and 2021

	2022	2021
		(As Restated)
LIABILITIES, DEFERRED INFLOWS OF RESOURCES, AND NET POSITION		
CURRENT LIABILITIES		
Accounts payable	\$ 27,647,484	\$ 17,694,587
Accrued salaries, wages, and employee benefits	30,290,195	28,899,995
Estimated third-party payor settlements	11,297,696	10,370,116
Accrued interest payable	503,027	513,515
Current portion of lease liability	7,051,669	6,343,980
Current portion of long-term debt	10,037,234	9,533,008
Total current liabilities	86,827,305	73,355,201
LEASE LIABILITY, net of current portion	84,053,419	62,101,023
LONG-TERM DEBT, net of current portion	129,571,575	140,243,792
OPEB LIABILITY	5,724,482	5,371,600
ESTIMATED PROFESSIONAL LIABILITY	7,435,531	6,783,026
Total liabilities	313,612,312	287,854,642
DEFERRED INFLOWS OF RESOURCES		
Deferred lease inflows	4,739,557	5,064,441
Deferred gain on refunding	31,668	33,791
Total deferred inflows of resources	4,771,225	5,098,232
NET POSITION		
Net investment in capital assets	21,005,930	17,641,924
Restricted for debt service	10,420,819	10,725,140
Unrestricted	160,073,159	185,405,202
Total net position	191,499,908	213,772,266
Total liabilities, deferred inflows of resources, and net position	\$ 509,883,445	\$ 506,725,140

See accompanying notes.

Public Hospital District No. 1 of Skagit County, Washington
Statements of Revenues, Expenses, and Changes in Net Position
Years Ended December 31, 2022 and 2021

	2022	2021
		(As Restated)
OPERATING REVENUES		
Net patient service revenue (net of provision for bad debts of \$13,776,770 and \$12,559,313)	\$ 492,082,789	\$ 463,177,578
Other operating revenues	31,486,350	30,793,467
Total operating revenues	523,569,139	493,971,045
OPERATING EXPENSES		
Salaries and wages	240,993,095	227,549,268
Employee benefits	53,224,979	55,817,045
Professional fees	41,671,697	22,326,682
Supplies	95,054,221	83,177,050
Purchased services	60,055,921	57,452,618
Other	27,133,394	22,674,418
Depreciation and amortization	25,439,641	25,208,114
Interest and amortization	6,051,664	7,293,633
Total operating expenses	549,624,612	501,498,828
Operating loss	(26,055,473)	(7,527,783)
NONOPERATING INCOME, net		
CARES Act Provider Relief Fund and other assistance	1,551,209	4,827,957
Investment loss	(2,785,568)	(31,571)
Gain on termination of participation in PEBB	-	28,435,601
Revenues from tax levies for general obligation bonds	5,036,450	4,772,632
Interest and amortization expense	(1,366,837)	(1,746,656)
Other expense	(106,920)	(19,649)
Nonoperating income, net	2,328,334	36,238,314
Change in net position before capital contributions and transfers	(23,727,139)	28,710,531
CAPITAL CONTRIBUTIONS	311,343	188,065
GAIN ON TRANSFER OF ASSETS	1,143,438	1,236,706
CHANGE IN NET POSITION	(22,272,358)	30,135,302
NET POSITION, beginning of year	213,772,266	183,636,964
NET POSITION, end of year	\$ 191,499,908	\$ 213,772,266

See accompanying notes.

Public Hospital District No. 1 of Skagit County, Washington
Statements of Cash Flows
Years Ended December 31, 2022 and 2021

	2022	2021
		(As Restated)
Increase (Decrease) in Cash and Cash Equivalents		
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from and on behalf of patients	\$ 486,676,680	\$ 458,001,903
Cash paid to suppliers	(212,968,756)	(184,436,701)
Cash paid to employees	(292,502,922)	(278,244,306)
Cash paid to Medicare Advance Payment Program	-	(35,247,911)
Other cash receipts	28,880,568	31,351,658
Net cash from operating activities	10,085,570	(8,575,357)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Cash received from CARES Act Provider Relief Fund and other assistance	1,551,209	4,827,957
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase of capital assets	(14,313,275)	(11,225,429)
Principal payments on long-term debt	(9,532,126)	(8,974,786)
Interest paid on long-term debt	(6,012,988)	(7,017,909)
Proceeds from issuance of long-term debt	-	18,755,000
Cash paid for financing costs	-	(437,502)
Escrow payment for refunding of 2013A revenue and refunding bonds	-	(18,775,603)
Cash received from tax revenues for general obligation bonds	5,031,508	4,739,205
Cash received from transfer of assets	1,143,438	1,236,706
Cash received from capital contributions	311,343	188,065
Cash paid for leases	(7,585,578)	(7,286,126)
Other	(158,689)	(74,296)
Net cash from capital and related financing activities	(31,116,367)	(28,872,675)
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash distributions from joint ventures	2,290,433	2,500,191
Net change in investments and other noncurrent cash and investments	18,997,973	48,652,095
Investment income	305,837	591,904
Net cash from investing activities	21,594,243	51,744,190
NET CHANGE IN CASH AND CASH EQUIVALENTS	2,114,655	19,124,115
CASH AND CASH EQUIVALENTS, beginning of year	25,551,704	6,427,589
CASH AND CASH EQUIVALENTS, end of year	\$ 27,666,359	\$ 25,551,704
RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENTS OF NET POSITION		
Cash	\$ 16,831,407	\$ 23,967,923
Cash and cash equivalents in other noncurrent cash and investments	10,834,952	1,583,781
	\$ 27,666,359	\$ 25,551,704

See accompanying notes.

Public Hospital District No. 1 of Skagit County, Washington
Statements of Cash Flows
Years Ended December 31, 2022 and 2021

	2022	2021 (As Restated)
Increase (Decrease) in Cash and Cash Equivalents		
RECONCILIATION OF OPERATING INCOME TO		
NET CASH FROM OPERATING ACTIVITIES		
Operating loss	\$ (26,055,473)	\$ (7,527,783)
Adjustments to reconcile operating loss to net cash from operating activities		
Net change in OPEB liability	324,952	5,371,600
Investment loss considered an investing activity	1,034,174	373,308
Interest expense considered a capital financing activity	6,051,664	7,269,553
Depreciation and amortization	25,439,641	25,208,114
Income recognized from joint ventures	(2,305,175)	(2,289,704)
Changes in operating assets and liabilities		
Accounts receivable, net	(6,333,689)	(6,463,090)
Other receivables	(1,334,781)	2,536,512
Supplies inventory	(316,010)	453,879
Prepaid expenses and other assets	258,677	(1,736,987)
Accounts payable	10,351,305	2,077,016
Accrued salaries, wages, and employee benefits	1,390,200	(249,593)
Estimated third-party payor settlements	927,580	1,287,415
Reserve for professional liability costs	652,505	362,314
Advances under Medicare Advance Payment Program	-	(35,247,911)
Net cash from operating activities	\$ 10,085,570	\$ (8,575,357)
DISCLOSURE OF NONCASH FINANCING ACTIVITIES		
Capital assets financed through accounts payable	\$ 398,408	\$ 603,425

See accompanying notes.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Note 1 – Organization

Organization – Public Hospital District No. 1 of Skagit County, Washington (the District), is organized as a municipal corporation pursuant to the laws of the state of Washington. The District is governed by an elected seven-member board. The District, doing business as Skagit Valley Hospital (SVH), added the clinic division on July 1, 2010. The clinic division is known as Skagit Regional Clinics (SRC). On January 1, 2011, the District created the system name Skagit Regional Health (SRH). This name encompasses both SVH's and SRC's operations. SVH is a licensed 137-bed acute care hospital in Mount Vernon, Washington. The District also operates Camano Rural Health Clinic on Camano Island, Washington.

The District and PHD No. 3 also entered into an Affiliation Agreement Regarding the Lease and Operation of CVH (the Affiliation Agreement). CVH is a 48-bed facility that is approximately 20 miles southeast of SVH's main campus. In accordance with Affiliation Agreement, the District began operating CVH on June 1, 2016. The Affiliation Agreement is structured as a long-term lease (the Lease) between PHD No. 3 and the District. PHD No. 3 leased substantially all of its assets, certain other clinic facilities, PHD No. 3's interest as lessor in certain leases, and intangible assets to the District for a term of 30 years. The District will pay PHD No. 3 an annual base rent of \$10 and is responsible for all costs and expenses associated with the leased assets, including maintenance and capital improvements.

Pursuant to the Affiliation Agreement, PHD No. 3 transferred all of its cash and cash equivalents of a retained amount to the District in 2017. The retained amount is equal to PHD No. 3's known and contingent liabilities and debts plus a minimum cash balance of \$1,000,000. Thereafter, PHD No. 3 will continue to levy and collect excess and regular property tax levies, as well collect revenues from a lease of a medical office building owned by Smokey Point LLC. Smokey Point LLC is owned 50% by the District and 50% by PHD No. 3. The proceeds from PHD No. 3's regular property tax levy and the Smokey Point LLC lease will be used to pay PHD No. 3's expenses, including the annual debt service on outstanding limited tax general obligations, and to fund the minimum cash balance of \$1,000,000. To the extent the amount collected by PHD No. 3 from its regular property tax levy and the Smokey Point LLC lease exceeds PHD No. 3's existing obligations in any year, and the PHD No. 3 cash balance is equal to \$1,000,000, the excess funds will be transferred to the District. Cash transferred by PHD No. 3 to the District resulted in a gain on transfer of assets of \$1,143,438 and \$1,236,706 for the years ended December 31, 2022 and 2021, respectively.

The Affiliation Agreement provides provisions for certain operating commitments and specific provisions in event the agreement is discontinued.

Note 2 – Summary of Significant Accounting Policies

Blended component unit – For financial reporting purposes, component units are entities that are legally separate organizations for which the District is financially accountable, and other organizations for which the nature and significance of their relationship with the District are such that exclusion would cause the District's financial statements to be misleading or incomplete. Based on these criteria, the following is considered a component unit of the District's reporting entity.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

The Cascadia Care Network (CCN) is a blended component unit of the District and is included within the accompanying financial statements. The CCN is a Medicare accountable care organization with limited powers and is governed by a board of managers, who are appointed by the District's board of commissioners. The District's management has operational responsibility for the CCN. The District has recorded the revenue, obligations, and the related assets, in the accompanying financial statements of the District.

Accounting standards – The District reports its financial information in a form that complies with the pronouncements of the Governmental Accounting Standards Board (GASB).

Basis of presentation – The accompanying financial statements have been prepared on the accrual basis of accounting using the economic resources measurement focus. Under this method of accounting, revenues are recognized when earned and expenses are recorded when liabilities are incurred without regard to receipt or disbursement of cash.

Use of estimates – The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported 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 demand and interest-bearing deposits with an original maturity of three months or less.

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

Supplies inventory – Supplies inventory, consisting of medicine and medical supplies, is valued at the lower of cost (computed on the first-in, first-out basis), or net realizable value.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Lease receivable – Lease receivable is a new asset on the Statements of Net Position from the adoption of the GASB 87 accounting standard on leases. As a lessor for building leases, the District recorded lease receivables of \$4,845,973 and \$5,119,088 at December 31, 2022 and 2021, respectively.

Right to use assets – Right to use assets is a new asset on the Statements of Net Position from the adoption of the GASB 87 accounting standard on leases. Right to use assets are recognized by lessees, as all applicable leases are treated as finance leases and an asset is recorded for the discounted value of the payments required under the lease term. More details are disclosed in the notes to the financial statements. The District recorded right to use assets, net, of \$88,957,071 and \$67,272,054 for the years ended December 31, 2022 and 2021, respectively.

Capital assets – Land, buildings, and equipment acquisitions are recorded at cost. Improvements and replacements of land, buildings, and equipment are capitalized. The District's capitalization threshold is \$1,000 per item and a useful life of at least three years. Maintenance and repairs are expensed. The cost of land, buildings, and equipment sold or retired and the related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recorded.

Depreciation is recorded over the estimated useful life of each class of depreciable asset using the American Hospital Association's guidelines and is computed using the straight-line method over the shorter period of the lease term or the estimated useful life of the equipment. The estimated useful lives used by the District are as follows:

Land improvements	3 – 40 years
Buildings	15 – 40 years
Fixed equipment	3 – 25 years
Major movable and minor equipment	3 – 20 years

Interest on borrowed funds less any interest earned on temporarily invested funds is capitalized on construction projects as a cost of the related project from the date of borrowing until the construction period ends and the related asset is placed in service. Capitalized interest is depreciated over the estimated useful life of the related asset. Effective in 2022, the District will no longer capitalize interest cost incurred on construction projects as a result of adopting a new accounting standard.

Federal income taxes – The District, as a political subdivision of the state of Washington, is not subject to federal income taxes under Section 115 of the Internal Revenue Code.

Other noncurrent cash and investments – Periodically, the Board of Commissioners sets aside cash resources for the funding of future capital improvements and self-insurance reserves. In addition, certain funds are restricted by bond indentures to be used solely for debt service or for the funding of future capital projects. Pool A and Pool B funds are restricted for capital improvements and operations of CVH as defined in the Affiliation Agreement. These funds are invested in bankers' acceptances, obligations of the United States Government, the State Treasurer's Investment Pool, and certificates of deposit with financial institutions in accordance with state guidelines.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

All District investments are carried at market value. Investment income earned on self-insurance funds and the revenue bond indenture agreements are reported as other operating revenue. Realized and unrealized investment income or losses on other investments are reported as nonoperating gains and losses.

Investments in joint ventures – The District has investments in several different joint ventures providing health care services and accounts for these investments using the equity method, under which the District's share of net income is reported in other operating revenues.

Lease liability – Lease liability is a new liability recorded in the Statements of Net Position due to the adoption of the GASB 87 lease accounting standard. The District recorded lease liabilities of \$91,105,088 and \$68,445,003 at December 31, 2022 and 2021, respectively.

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 illness; natural disasters; medical malpractice; and employee 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. The District pays certain workers' compensation claims on a self-insured basis. The District has purchased stop-loss insurance to cover workers' compensation claims that exceed stated limits and has recorded an estimated reserve for incurred but not reported claims based on an actuarial estimate, which was \$4,045,142 and \$4,327,762 at December 31, 2022 and 2021, respectively. These amounts are recorded in accrued salaries, wages, and employee benefits on the statements of net position. The District also pays certain professional liability claims on a self-insured basis (Note 12).

Postemployment Benefits Other Than Pensions (OPEB) – The net OPEB liability is measured at the actuarial present value of projected benefit payments for the District's covered members. Deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense are recognized as they occur and are based on the changes in the net OPEB liability between measurement dates (Note 11).

Net position – Net position of the District is classified into three components. The net investment in capital assets component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of related debt that is attributable to the acquisition, construction, or improvement of those assets. The restricted component of net position represents noncapital assets that must be used for a specific purpose. The unrestricted component of net position is the remaining net amount of the assets and liabilities that are not included in the determination of net investment in capital assets or the restricted components of net position.

Operating revenues and expenses – The District's statements of revenues, expenses, and changes in net position distinguish between operating and nonoperating revenues and expenses. Operating revenues, such as patient service revenue, result from exchange transactions associated with providing health care services—the District's primary business. Nonexchange revenues, such as revenues for tax levies and contributions for other than capital asset acquisition, are reported as nonoperating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs related to general obligation bonds. Tax levy income and debt service related to general obligation bonds and peripheral or incidental transactions are reported as nonoperating gains and losses.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Net patient service revenue – Patient service revenue is recorded at established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered. Preliminary settlements under reimbursement agreements with Medicare and Medicaid are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

Reimbursements received from certain third-party payors are subject to audit and retroactive adjustment. Provision for possible adjustment as a result of audits is recorded in the financial statements. When reimbursement settlements are received, or when information becomes available with respect to reimbursement changes, any variations from amounts previously accrued are accounted for in the period in which the settlements are received or the change in information becomes available.

CARES Act Provider Relief Fund – The District has received funds from the Provider Relief Fund under the Coronavirus Aid, Relief, and Economic Security (CARES) Act. Per United States Department of Health and Human Services (HHS) guidance, these funds are to be used towards COVID-19 specific expenditures and to assist with lost revenues associated with lower volumes and cancellations of procedures and services. The District recognizes revenue upon meeting the eligibility requirements associated with the funding. The CARES Act guidelines stipulate certain conditions that are required to be met, such as the incurrence of eligible expenditures or loss of revenue. Those conditions are identified, for accounting and financial reporting purposes, as eligibility requirements.

Financial assistance – The District provides care to patients who meet certain criteria under its financial assistance policies. Because the District does not pursue collection of amounts determined to qualify as financial assistance, they are not reported as net patient service revenue. Forgone revenue for financial assistance provided during the years ended December 31, 2022 and 2021, measured by the District's standard charges was \$16,707,622 and \$13,374,453, respectively.

Recently adopted accounting pronouncements – In June 2017, the GASB issued Statement No. 87, *Leases* (Statement 87). Statement 87 establishes a single model for lease accounting based on the foundational principle that leases are financings of a contractual right to use another entity's nonfinancial assets (the underlying asset) for a term exceeding 12 months in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Under Statement 87, a lessor is required to recognize a lease receivable and a deferred inflow of resources, except for certain regulated leases, and a lessee is required to recognize a lease liability and an intangible right to use lease asset, thereby enhancing the relevance and consistency of information about the government's leasing activities. Statement 87 is effective for the year ending December 31, 2022. The District has adopted this new standard retroactively by restating the financial statements for all periods presented. The beginning balance of the net position was restated as of January 1, 2021. The required disclosures for leases can be found in Note 5 in the accompanying notes to the financial statements.

In June 2018, the GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period* (Statement 89). Statement 89 is effective for the year ending December 31, 2022. Statement 89 requires that interest cost incurred before the end of a construction period be recognized as expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, these costs are not included in the capitalized cost of capital assets reported by the District. Statement 89 is applied on a prospective basis and interest costs capitalized prior to implementation will continue to be recognized as those assets are depreciated.

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

The following table shows the balances within the financial statements being restated:

	As Previously Reported	Effect of	As Restated
Current assets			
Interest receivable	\$ 8,416	\$ 7,272	\$ 15,688
Current portion of lease receivable	-	273,061	273,061
Long-term lease receivable	-	4,846,027	4,846,027
Right to use assets	-	67,272,054	67,272,054
Current liabilities			
Accrued interest payable	\$ 419,040	\$ 94,475	\$ 513,515
Current portion of lease liability	-	6,343,980	6,343,980
Lease liability, net of current	-	62,101,023	62,101,023
Deferred lease inflows	-	5,064,441	5,064,441
Net position			
Unrestricted	\$ 186,610,707	\$ (1,205,505)	\$ 185,405,202
	As Previously Reported	Effect of	As Restated
Operating revenue			
Other operating revenue	\$ 30,731,542	\$ 61,925	\$ 30,793,467
Operating expenses			
Other	\$ 29,866,063	\$ (7,191,645)	\$ 22,674,418
Depreciation and amortization	17,978,624	7,229,490	25,208,114
Interest and amortization	6,064,048	1,229,585	7,293,633
Change in net position	\$ 31,340,807	\$ (1,205,505)	\$ 30,135,302

Reclassifications – The District reclassified certain amounts relating to its prior period results to conform to its current period presentation within the financial statements. These reclassifications have not changed the results of operations of prior periods.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Note 3 – Net Patient Service Revenue

The District has agreements with third-party payors that provide for payments to the District at amounts different from its established rates. A summary of the payment arrangements with major third-party payors follows:

Medicare – Inpatient acute care services rendered to Medicare program beneficiaries are paid at predetermined, specific rates for each hospital discharge. Discharges are classified according to a list of Medicare severity diagnosis-related groups (MS-DRGs). Each MS-DRG has a payment weight assigned to it, based on the average resources used to treat Medicare patients in that MS-DRG. The District's classification of MS-DRGs and the appropriateness of their admission are subject to an independent review by a peer review organization. Most outpatient services to Medicare beneficiaries are paid prospectively based on ambulatory payment classifications. The District's cost reports have been reviewed and/or audited by the Medicare fiscal intermediary through 2018 for CVH and 2017 for SVH. Net revenue billed under Medicare totaled \$213,781,850 and \$183,098,583 for the years ended December 31, 2022 and 2021, respectively. Unsecured net patient accounts receivable due from Medicare at December 31, 2022 and 2021, were \$21,045,861 and \$17,662,612, respectively.

Medicaid – The District is reimbursed for Medicaid services under the Certified Public Expenditures (CPE) reimbursement methodology applicable to all noncritical access Washington State governmental hospitals. Under this program, the District is paid for inpatient Medicaid services based on certain costs as determined by Medicaid. The estimated costs for inpatient care are calculated as a ratio of cost to charges from a base year (two years before the service year). Under this program, the District will be reimbursed the higher of the cost of service or "baseline" reimbursement that would have been received based on the pre-July 1 inpatient payment system. Outpatient services are paid on a fee schedule or a percentage of allowed charges based on a ratio of the District's allowable operating expenses to total allowable revenue. The District has finalized the Medicaid CPE cost reports through state fiscal year ending June 30, 2018. Net revenue billed under the Medicaid program totaled \$65,444,778 and \$63,585,925 for the years ended December 31, 2022 and 2021, respectively. Unsecured net patient accounts receivable due from Medicaid at December 31, 2022 and 2021, were \$5,913,532 and \$4,548,170, respectively.

The District's estimates of final settlements to or from Medicare and Medicaid through 2022 have been recorded in the accompanying statements of net position. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in the near term. Differences between the net amounts accrued and subsequent settlements are recorded in operations at the time of settlement and were not significant for the years ended December 31, 2022 and 2021.

Other third-party payors – The District has also entered into various payment arrangements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations, which provide for payment or reimbursement at amounts different from published rates. Contractual adjustments represent the difference between published rates for services and amounts paid or reimbursed by these third-party payors.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

The following are the components of net patient service revenue for the District for the years ended December 31, 2022 and 2021:

	2022	2021
Gross patient service revenue	\$ 1,777,606,012	\$ 1,635,464,882
Less adjustments to gross patient service revenue		
Contractual adjustments	1,255,038,831	1,146,353,538
Provision for bad debts	13,776,770	12,559,313
Financial assistance	16,707,622	13,374,453
Total adjustments to gross patient service charges	1,285,523,223	1,172,287,304
Net patient service revenue	\$ 492,082,789	\$ 463,177,578

Note 4 – Deposits, Investments, and Other Noncurrent Cash and Investments

The District makes investments in accordance with Washington State law. Eligible investments include obligations secured by the U.S. Treasury, other obligations of the United States or its agencies, certificates of deposit with approved institutions, insured money market funds, commercial paper, registered warrants of local municipalities, the Washington State Local Government Investment Pool (LGIP), eligible bankers' acceptances, repurchase agreements, and bonds.

As a political subdivision of the state, the District categorizes deposits and investments to give an indication of the risk assumed at year-end. Category 1 includes deposits and investments that are insured, registered, or held by the District's agent in the District's name. Category 2 includes uninsured and unregistered investments that are held by the broker's or dealer's trust department or agent in the District's name. Category 3 includes uninsured and unregistered deposits and investments for which the securities are held by the broker or dealer, or its trust department or agent, but not in the District's name.

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

At December 31, 2022 and 2021, all deposits and investments of the District are categorized as Category 1 and consist of the following:

	2022	2021
Cash	\$ 16,831,407	\$ 23,967,923
Investments		
Commercial paper	1,387,672	10,106,510
Investment in State Treasurer's Investment Pool	19,814,813	-
U.S. Treasury securities	17,093,114	31,825,139
U.S. government agency obligations	-	1,720,467
Domestic corporate bonds	2,827,728	2,060,553
Foreign bonds	2,011,021	4,085,190
Other assets	118,283	589,870
	43,252,631	50,387,729
Other noncurrent cash and investments		
Cash and cash equivalents	10,834,952	1,583,781
Commercial paper	6,433,737	24,876,440
U.S. Treasury securities	79,249,707	78,335,266
U.S. government agency obligations	10,877,647	17,251,095
Domestic corporate bonds	13,110,343	5,071,901
Foreign bonds	9,323,805	10,055,398
Other assets	1,363,122	821,642
	131,193,313	137,995,523
Total deposits and investments	\$ 191,277,351	\$ 212,351,175

The composition of investments, reported at fair value by investment type at December 31, 2022, and excluding unrestricted cash and cash included in other noncurrent cash and investments of \$47,481,172, is as follows:

Investment Type	Quoted prices in Active Markets for Identical assets (Level 1)	Inputs Other than Quoted Prices that are Directly or Indirectly Observable (Level 2)	Total	Percentage of Totals
Commercial paper	\$ -	\$ 34,982,950	\$ 34,982,950	19%
U.S. Treasury securities	110,160,405	-	110,160,405	59%
U.S. government agency obligations	-	18,971,562	18,971,562	10%
Domestic corporate bonds	-	7,132,454	7,132,454	4%
Foreign bonds	-	14,140,588	14,140,588	8%
Other	-	1,411,512	1,411,512	1%
	\$ 110,160,405	\$ 76,639,066	\$ 186,799,471	100%

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

The composition of investments, reported at fair value by investment type at December 31, 2021, and unrestricted cash and cash and LGIP in other noncurrent cash and investments as to use balances of \$26,141,575, is as follows:

Investment Type	Quoted prices in Active Markets for Identical assets (Level 1)	Inputs Other than Quoted Prices that are Directly or Indirectly Observable (Level 2)	Total	Percentage of Totals
Commercial paper	\$ -	\$ 7,821,409	\$ 7,821,409	5%
U.S. Treasury securities	96,342,821	-	96,342,821	67%
U.S. government agency obligations	-	10,877,647	10,877,647	8%
Domestic corporate bonds	-	15,938,071	15,938,071	11%
Foreign bonds	-	11,334,826	11,334,826	8%
Other	-	1,481,405	1,481,405	1%
	<u>\$ 96,342,821</u>	<u>\$ 47,453,358</u>	<u>\$ 143,796,179</u>	<u>100%</u>

The District's deposits and investments had the following maturities at December 31, 2022:

Investment Type	Fair Value	Investment Maturities (in Years)	
		Less Than 1	1-5
Commercial paper	\$ 7,821,409	\$ 7,821,409	\$ -
U.S. Treasury securities	96,342,821	4,985,550	91,357,271
U.S. government agency obligations	10,877,647	10,877,647	-
Domestic corporate bonds	15,938,071	239,898	15,698,173
Foreign bonds	11,334,826	1,932,080	9,402,746
Other assets	1,481,405	1,481,405	-
Total investments	<u>\$ 143,796,179</u>	<u>\$ 27,337,989</u>	<u>\$ 116,458,190</u>

The District participates in the LGIP. The Office of the State Treasurer of Washington (OST) manages and operates the LGIP. Participation by local governments is voluntary. The investment policies of the LGIP are the responsibility of the OST and any proposed changes are reviewed by the LGIP Advisory Committee. The LGIP is comparable to a Rule 2a-7 money market fund recognized by the Securities and Exchange Commission (17 CFR 270.2a-7). Rule 2a-7 funds are limited to high-quality obligations with limited maximum and average maturities, the effect of which is to minimize both market and credit risk. The objectives of the State Treasurer's investment practices for the LGIP, in priority order, will be safety, liquidity, and return on investment. Separate financial statements for the LGIP are available from the OST. The LGIP is not subject to risk evaluation.

Credit risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The District's investment policy limits the types of securities to those authorized by statute; therefore, credit risk is very limited. The investments held are all investment grade securities that are rated A- and higher by Standard and Poor's. Obligations of the U.S. government and obligations explicitly guaranteed by the U.S. government are not considered to have credit risk.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Deposits – All of the District's deposits are either insured or collateralized. The District's insured deposits are covered by the Federal Deposit Insurance Corporation. Collateral protection is provided by the Washington Public Deposit Protection Commission.

Custodial credit risk – Custodial credit risk is the risk that in the event of a failure of the counterparty, the District will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. All U.S. government securities are held by the District's safekeeping custodian acting as an independent third party and carry no custodial credit risk.

Concentration of credit risk – Concentration of credit risk is the risk of loss attributed to the magnitude of the District's investment in a single issuer. The District mitigates credit risk by limiting the percentage of the portfolio invested with any one issuer.

Interest rate risk – Interest rate risk is the risk that changes in interest rates of debt instruments will adversely affect the fair value of an investment. The District manages interest rate risk by having policy limitations on the maximum maturity of any one security to less than 60 months from settlement date to maturity date unless matched to a specific cash flow requirement.

In addition to interest and investment income included in nonoperating income, interest income included in other operating revenues totaled \$1,034,174 and \$373,308 for the years ended December 31, 2022 and 2021, respectively.

Note 5 – Leases

Lessee – The District enters into noncancellable leases primarily for buildings and equipment. For leases with a maximum possible term of 12 months or less at commencement, the District recognizes expense based on the terms of the lease contract. For all other leases, the District recognizes a lease liability, which is recorded within current portion of lease liabilities and long-term lease liabilities in the statements of net position and an intangible right to use asset, net of accumulated amortization at the present value of payments expected to be made throughout the lease term. When a readily determinable discount rate is not available, the discount rate is determined using the District's incremental borrowing rate based on information available at the commencement date of the lease in determining the present value of lease payments.

Subsequently, the lease liability is reduced by the principal portion of lease payments made. Interest expense is recognized ratably over the contract term. The right to use asset is initially measured as the initial amount of the lease liability, less lease payments made at or before the lease commencement date, plus any initial direct costs ancillary to placing the underlying asset into service, less any lease incentives received at or before the lease commencement date. Subsequently, the asset is amortized on a straight-line basis over the shorter of the lease term or the useful life of the underlying asset which is recorded within depreciation and amortization in the statements of revenues, expenses and changes in net position.

Some leases include one or more renewal options which generally extend the lease at the then market rate of rental payments. All such options are at the District's discretion and if it is reasonably certain that the renewal option(s) will be exercised by the District, the renewal option payments and term are included in the District's measurement of the lease liability and right to use asset.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Certain leases require the District to make variable lease payments that relate to common area maintenance, insurance, taxes, or other payments based on performance or usage. Variable lease payments, other than those payments that depend on an index or rate or are fixed in substance, are excluded from the measurement of the lease liability. Variable lease payments are recognized within other or supplies expense in the statements of revenues, expenses and change in net position when the event, activity or circumstance in the lease agreement on which those payments are assessed occurs. The amounts recognized as expense for variable lease payments not included in the measurement of the lease liability were \$2,951,681 and \$2,720,602 during the years ended December 31, 2022 and 2021, respectively.

Right to use assets – The activity in the District’s right to use assets and related accumulated amortization accounts as of and for the years ended December 31, 2022 and 2021, is set forth below:

	Beginning Balance January 1, 2022	Additions	Modifications/ Renewals	Deductions	Ending Balance December 31, 2022
RIGHT TO USE ASSETS					
Building	\$ 70,919,061	\$ 26,751,821	\$ -	\$ (210,370)	\$ 97,460,512
Equipment	3,582,483	2,340,467	-	(115,458)	5,807,492
Total right to use assets	<u>74,501,544</u>	<u>29,092,288</u>	<u>-</u>	<u>(325,828)</u>	<u>103,268,004</u>
LESS ACCUMULATED AMORTIZATION FOR					
Building	(6,522,483)	(6,572,030)	-	160,538	(12,933,975)
Equipment	(707,007)	(748,231)	-	78,280	(1,376,958)
Total accumulated amortization	<u>(7,229,490)</u>	<u>(7,320,261)</u>	<u>-</u>	<u>238,818</u>	<u>(14,310,933)</u>
Total right to use assets, net	<u>\$ 67,272,054</u>	<u>\$ 21,772,027</u>	<u>\$ -</u>	<u>\$ (87,010)</u>	<u>\$ 88,957,071</u>
	Beginning Balance January 1, 2021	Additions	Modifications/ Renewals	Deductions	Ending Balance December 31, 2021
RIGHT TO USE ASSETS					
Building	\$ 70,919,061	\$ -	\$ -	\$ -	\$ 70,919,061
Equipment	3,582,483	-	-	-	3,582,483
Total right to use assets	<u>74,501,544</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>74,501,544</u>
LESS ACCUMULATED AMORTIZATION FOR					
Building	-	(6,522,483)	-	-	(6,522,483)
Equipment	-	(707,007)	-	-	(707,007)
Total accumulated amortization	<u>-</u>	<u>(7,229,490)</u>	<u>-</u>	<u>-</u>	<u>(7,229,490)</u>
Total right to use assets, net	<u>\$ 74,501,544</u>	<u>\$ (7,229,490)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 67,272,054</u>

Amortization expense of right to use assets for the years ended December 31, 2022 and 2021, was \$7,320,261 and \$7,229,490, respectively.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Lease liabilities – Changes in lease liabilities during the years ended December 31, 2022 and 2021, are summarized below:

Year Ending December 31,	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
2022	\$ 68,445,003	\$ 29,092,288	\$ (6,432,203)	\$ 91,105,088	\$ 7,051,669
2021	\$ 74,501,544	\$ -	\$ (6,056,541)	\$ 68,445,003	\$ 6,343,980

The following schedule shows future annual lease payments, and in five year increments thereafter, as of December 31, 2022, for both principal and interest:

Year Ending December 31,	Lease Liabilities		
	Principal	Interest	Total
2023	\$ 7,051,669	\$ 2,549,241	\$ 9,600,910
2024	33,278,706	1,487,026	34,765,732
2025	6,831,043	890,006	7,721,049
2026	6,752,440	757,016	7,509,456
2027	6,463,548	624,419	7,087,967
2028–2032	24,311,674	1,378,492	25,690,166
2033–2037	5,939,015	258,211	6,197,226
2038	476,993	3,442	480,435
Total payments	<u>\$ 91,105,088</u>	<u>\$ 7,947,853</u>	<u>\$ 99,052,941</u>

Lessor – The District leases building space and land to physician groups and others for medical practices and medical offices. For leases with terms greater than 12 months, the District recognizes a lease receivable and deferred inflows of resources at the present value of payments expected to be received during the lease term using the District’s incremental borrowing rate.

Subsequently, the lease receivable is reduced by the lease payments received and the discount on the lease receivable is amortized through recognition of interest income, which is recorded in other, net in the statements of revenues, expenses and changes in net position. Amounts expected to be received within one year are classified as current assets in the statements of net position. The deferred inflow of resources are recognized over the lease term in subsequent periods as lease revenue, which is recorded in other operating revenue in the statements of revenues, expenses and changes in net position.

Certain leases require the lessee to make variable lease payments that relate to common area maintenance, insurance, taxes, payments based on performance or usage. Variable lease payments, other than those payments that depend on an index or rate or are fixed in substance, are excluded from the measurement of the lease receivable. Variable lease payments are recognized as other revenue in the statements of revenues, expenses and changes in net position when the event, activity or circumstance in the lease agreement on which those payments are assessed occurs.

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

Revenue from leases for the years ended December 31, 2022 and 2021, is as follows:

	2022	2021
Lease revenue	\$ 324,884	\$ 324,825
Interest revenue	86,187	90,396
Total	\$ 411,071	\$ 415,221

The following schedule shows future annual lease receipts, and in five year increments thereafter, at December 31, 2022, for both principal and interest:

Year Ending December 31,	Lease Receivable		
	Principal	Interest	Total
2023	\$ 284,188	\$ 81,589	\$ 365,777
2024	295,454	76,798	372,252
2025	307,514	71,376	378,890
2026	319,734	65,959	385,693
2027	332,339	60,328	392,667
2028-2032	574,781	252,018	826,799
2033-2037	310,295	223,435	533,730
2038-2042	338,321	195,409	533,730
2043-2047	368,880	164,850	533,730
2048-2052	402,132	131,598	533,730
2053-2057	438,543	95,187	533,730
2058-2062	478,156	55,574	533,730
2063-2066	395,636	13,558	409,194
Total payments	\$ 4,845,973	\$ 1,487,679	\$ 6,333,652

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

Note 6 – Capital Assets

Capital asset additions, retirements, and balances as of and for the years ended December 31, 2022 and 2021, were as follows:

	Beginning Balance January 1, 2022	Additions	Retirements	Account Transfers	Ending Balance December 31, 2022
NONDEPRECIABLE CAPITAL ASSETS					
Land	\$ 11,712,330	\$ -	\$ -	\$ -	\$ 11,712,330
Construction in progress	750,333	4,826,465	-	(1,597,993)	3,978,805
Total nondepreciable capital assets	<u>12,462,663</u>	<u>4,826,465</u>	<u>-</u>	<u>(1,597,993)</u>	<u>15,691,135</u>
DEPRECIABLE CAPITAL ASSETS					
Land improvements	7,354,239	-	(59,322)	-	7,294,917
Buildings and leasehold improvements	148,434,767	1,232,341	(3,016,360)	1,455,076	148,105,824
Fixed equipment	23,635,372	253,963	(1,902,312)	106,723	22,093,746
Movable equipment	142,741,849	7,602,098	(10,146,459)	36,194	140,233,682
LESS ACCUMULATED DEPRECIATION AND AMORTIZATION					
Land improvements	(4,509,025)	(258,823)	59,322	-	(4,708,526)
Buildings and leasehold improvements	(83,888,302)	(5,880,491)	3,016,360	-	(86,752,433)
Fixed equipment	(20,242,030)	(450,560)	1,902,312	-	(18,790,278)
Movable equipment	(92,284,609)	(11,529,506)	10,146,459	-	(93,667,656)
Depreciable capital assets, net	<u>121,242,261</u>	<u>(9,030,978)</u>	<u>-</u>	<u>1,597,993</u>	<u>113,809,276</u>
	<u>\$ 133,704,924</u>	<u>\$ (4,204,513)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 129,500,411</u>
NONDEPRECIABLE CAPITAL ASSETS					
Land	\$ 11,712,330	\$ -	\$ -	\$ -	\$ 11,712,330
Construction in progress	852,394	1,811,383	-	(1,913,444)	750,333
Total nondepreciable capital assets	<u>12,564,724</u>	<u>1,811,383</u>	<u>-</u>	<u>(1,913,444)</u>	<u>12,462,663</u>
DEPRECIABLE CAPITAL ASSETS					
Land improvements	7,354,239	-	-	-	7,354,239
Buildings and leasehold improvements	145,824,029	722,052	-	1,888,686	148,434,767
Fixed equipment	23,615,735	50,799	(31,162)	-	23,635,372
Movable equipment	139,497,269	8,293,039	(5,073,217)	24,758	142,741,849
LESS ACCUMULATED DEPRECIATION AND AMORTIZATION					
Land improvements	(4,244,009)	(265,016)	-	-	(4,509,025)
Buildings and leasehold improvements	(78,063,696)	(5,724,269)	-	(100,337)	(83,888,302)
Fixed equipment	(19,712,104)	(561,088)	31,162	-	(20,242,030)
Movable equipment	(86,029,912)	(11,428,251)	5,073,217	100,337	(92,284,609)
Depreciable capital assets, net	<u>128,241,551</u>	<u>(8,912,734)</u>	<u>-</u>	<u>1,913,444</u>	<u>121,242,261</u>
	<u>\$ 140,806,275</u>	<u>\$ (7,101,351)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 133,704,924</u>

Depreciation and amortization expense of operating assets for the years ended December 31, 2022 and 2021, was \$18,119,380 and \$17,978,624, respectively.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Note 7 – Investments in Joint Ventures

Cascade Imaging Associates, LLC – Together with a local radiology group, the District formed Cascade Imaging Associates, LLC (CIA), a limited liability company, to provide magnetic resonance imaging and computer-assisted tomography services to the residents of the community. The District has a 50% interest in CIA at December 31, 2022 and 2021. During the years ended December 31, 2022 and 2021, the District recognized operating income of \$1,359,586 and \$2,576,494, respectively, for its share of the net income realized by CIA. The District's recorded investment in CIA was \$1,474,490 and \$1,149,904 at December 31, 2022 and 2021, respectively.

Skagit Digital Imaging, LLC – Together with a local radiology group, the District formed Skagit Digital Imaging, LLC (SDI), a limited liability company, to provide mammography and stereotactic biopsy services to the residents of the community. The District has a 50% interest in SDI at December 31, 2022 and 2021. During the years ended December 31, 2022 and 2021, the District recognized operating loss of \$155,637 and operating income of \$10,010, respectively, for its share of the net income realized by SDI. The District's recorded investment in SDI was \$1,381,617 and \$1,637,254 at December 31, 2022 and 2021, respectively.

Skagit Hospice Services, LLC – Together with Public Hospital District No. 304 of Skagit County, Washington, the District formed Skagit Hospice Services, LLC, dba Hospice of the Northwest (Hospice), a limited liability company, to provide hospice services to the residents of the community. The District has a 50% interest in Hospice at December 31, 2022 and 2021. During the years ended December 31, 2022 and 2021, the District recognized operating income of \$234,295 and \$350,991, respectively, for its share of the net income realized by Hospice. The District's recorded investment in Hospice was \$1,892,832 and \$1,658,536 at December 31, 2022 and 2021, respectively.

Skagit Valley Real Estate Partnership – As part of the closing of the integration with SRC in 2013, the District purchased a membership interest in Skagit Valley Real Estate Partnership (SVREP), a partnership that invests in and develops real property located mainly in Skagit and Snohomish Counties, Washington. The District has a 30% interest in SVREP at December 31, 2022 and 2021. During the years ended December 31, 2022 and 2021, the District recognized operating income of \$382,126, for its share of the net income realized by SVREP. The District's recorded investment in SVREP was \$4,434,955 and \$4,560,204 at December 31, 2022 and 2021, respectively.

Smokey Point Medical Center, LLC – Together with PHD No. 3, the District formed Smokey Point Medical Center, LLC (SPMC), a limited liability company, which owns the building, land, and equipment leased to the District and PHD no. 3 to operate the Smokey Point clinics. The District has a 50% interest in SPMC at December 31, 2022 and 2021. During the years ended December 31, 2022 and 2021, the District recognized operating income of \$511,745 and \$794,200, respectively, for its share of the net income realized by SPMC. The District's recorded investment in SPMC was \$4,192,453 and \$4,355,707 at December 31, 2022 and 2021, respectively.

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

Aggregated financial information for all of the District's joint ventures is summarized below:

	<u>2022</u>	<u>2021</u>
Current assets	\$ 22,836,658	\$ 9,232,991
Noncurrent assets, net	<u>26,271,616</u>	<u>25,855,943</u>
	<u>\$ 49,108,274</u>	<u>\$ 35,088,934</u>
Current liabilities	\$ 3,489,460	\$ 2,688,738
Long-term liabilities	23,200,741	10,675,468
Equity	<u>22,418,073</u>	<u>21,724,728</u>
	<u>\$ 49,108,274</u>	<u>\$ 35,088,934</u>
Revenue	\$ 34,927,812	\$ 28,847,903
Expenses	<u>29,121,752</u>	<u>23,427,417</u>
Net income	<u>\$ 5,806,060</u>	<u>\$ 5,420,486</u>

For more information on these joint ventures, including financial statements for the individual joint ventures, please contact the Business Services office of the District.

Note 8 – Long-Term Debt and Other Noncurrent Liabilities

Interest rates and maturities of long-term debt at December 31, 2022 and 2021, for the District consisted of the following:

	<u>2022</u>	<u>2021</u>
Direct placement revenue refunding bond, 2021, 2.10% to 2.57%, due annually on December 1, in amounts from \$110,000 in 2024 to \$8,000,000 in 2036, maturing in 2037.	\$ 16,695,000	\$ 18,755,000
Direct placement revenue refunding bond, 2019, 3.08%, due annually on December 1, in amounts from \$855,000 in 2023 to \$7,105,000 in 2035, maturing in 2035.	30,500,000	31,330,000
Direct placement unlimited tax general obligation refunding bond, 2019, 1.85% to 2.27%, due annually on December 1, in amounts from \$435,000 in 2023 to \$6,130,000 in 2028, maturing in 2028.	28,135,000	28,445,000
Revenue and refunding bonds, 2016, 4.00% to 5.00%, due serially on December 1, in amounts from \$1,915,000 in 2023 to \$5,875,000 in 2032, maturing in 2037, net of unamortized premium of \$4,682,399 and \$4,998,067 in 2022 and 2021, respectively.	57,317,399	59,473,067

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

	2022	2021
Unlimited tax general obligation refunding bonds, 2012, 5.00%, due serially on December 1, in amounts of \$4,155,000 in 2023, maturing in 2023, net of unamortized premium of \$1,894,499 and \$2,214,696 in 2022 and 2021, respectively.	\$ 6,049,499	\$ 10,164,696
Other notes payable, due in monthly installments of \$58,000, including interest of 4.50%, maturing in 2026.	911,911	1,609,037
	139,608,809	149,776,800
Less current portion	(10,037,234)	(9,533,008)
	\$ 129,571,575	\$ 140,243,792

During 2021, the District issued the 2021 direct placement revenue refunding bond to carry out a taxable refunding of a portion of the 2013A revenue and refunding bonds. The refunding resulted in the recognition of an accounting gain of \$33,968, which will be deferred and amortized over the life of the 2013A bond, which was set to mature in 2037 and is classified as a deferred inflow of resources on the statement of net position. The refunding decreased the District's aggregate debt service payments by \$4,347,000 over the next 16 years and resulted in an economic gain (difference between the present values of the old and new debt service payments) of \$3,385,000. If certain conditions are met, on September 5, 2023, the taxable bond will convert to a tax-exempt bond with an interest rate of 2.10%. If conditions are not met, the taxable bond remains outstanding, with an interest rate of 2.57% until such time that the conversion occurs or until maturity thereof.

During 2019, the District issued the 2019 direct placement revenue bonds to carry out a taxable refunding of the 2010 revenue bonds. The refunding resulted in the recognition of an accounting loss of \$1,593,000, which will be deferred and amortized over the life of the 2010 bond, which was set to mature in 2035 and is classified as a deferred outflow of resources on the statement of net position. The refunding decreased the District's aggregate debt service payments by \$8,426,000 over the next 16 years and resulted in an economic gain (difference between the present values of the old and new debt service payments) of \$6,612,000.

During 2019, the District issued the 2019 direct placement unlimited tax general obligation (UTGO) refunding bond to carry out a taxable refunding of a portion of the 2012 unlimited tax general obligation and refunding bonds. The refunding resulted in the recognition of an accounting loss of \$3,731,700, which will be deferred and amortized over the life of the 2012 bond, which was set to mature in 2028 and is classified as a deferred outflow of resources on the statement of net position. The refunding decreased the District's aggregate debt service payments by \$3,127,000 over the next 9 years and resulted in an economic gain (difference between the present values of the old and new debt service payments) of \$2,886,000. If certain conditions are met, on December 1, 2022, the taxable bond will convert to a tax-exempt bond with an interest rate of 1.85%. If conditions are not met, the taxable bond remains outstanding, with an interest rate of 2.27% until such time that the conversion occurs or until maturity thereof.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

As part of the bond resolutions authorizing the issuance of the 2021 direct placement revenue refunding bond, the 2019 direct placement revenue bond, and the 2016 revenue and refunding bonds, the District agreed to certain covenants regarding liquidity (minimum of 60 days cash on hand (the Liquidity Requirement)) and debt service coverage (minimum of 1.25 debt service coverage ratio (the Coverage Requirement)). The covenants provide that if the District's audited financial statements for any year disclose that the Liquidity Requirement or the Coverage Requirement is not being met, the District is required to retain a hospital consultant for the purpose of making recommendations to the District with a view to restoring compliance with the Liquidity Requirement or the Coverage Requirement, as applicable. If and so long as the District complies in all material respects with the recommendations of such hospital consultant, and so long as the Liquidity Requirement is met and the District's net income available for debt service is at least equal to the annual debt service on the District's outstanding revenue bonds in any year for which the hospital consultant's recommendations are made and any subsequent year for which such recommendations are renewed, the Liquidity Requirement and the Coverage Requirement, as applicable, are deemed satisfied, and the failure of the District to comply with the covenant will not be deemed to be an event of default.

For the year ended December 31, 2022, the District will not meet the Coverage Requirement. In compliance with the covenants, the District will retain a healthcare consultant to provide recommendations to restore compliance with the Coverage Requirement. In addition to the covenants described above, the 2021 direct placement revenue refunding bond contains provisions that allow the bond holder to impose a default interest rate that is 4% higher than the interest rate otherwise payable under the bond for the period during which the Coverage Requirement is not met. The 2021 bond holder also has the option to elect to not convert the taxable rate currently payable on the 2021 bond to a tax-exempt rate on at the conversion date (September 5, 2023) if the Coverage Requirement is not met. The District has requested the 2021 bond holder to consent to a waiver of both provisions.

Changes in the District's noncurrent liabilities during the years ended December 31, 2022 and 2021, are summarized below:

	Beginning Balance January 1, 2022	Additions	Reductions	Ending Balance December 31, 2022	Amounts Due Within One Year
LONG-TERM DEBT					
2021 Direct placement revenue refunding bond	\$ 18,755,000	\$ -	\$ 2,060,000	\$ 16,695,000	\$ 2,110,000
2019 Direct placement revenue refunding bond	31,330,000	-	830,000	30,500,000	855,000
2019 Direct placement UTGO refunding bond	28,445,000	-	310,000	28,135,000	435,000
2012 UTGO refunding bonds	10,164,696	-	4,115,197	6,049,499	4,155,000
2016 Revenue and refunding bonds	59,473,067	-	2,155,668	57,317,399	1,915,000
Other notes payable	1,609,037	-	697,126	911,911	567,234
	<u>149,776,800</u>	<u>-</u>	<u>10,167,991</u>	<u>139,608,809</u>	<u>10,037,234</u>
ESTIMATED PROFESSIONAL LIABILITY	<u>6,783,026</u>	<u>-</u>	<u>-</u>	<u>6,783,026</u>	<u>-</u>
Total noncurrent liabilities	<u>\$ 156,559,826</u>	<u>\$ -</u>	<u>\$ 10,167,991</u>	<u>\$ 146,391,835</u>	<u>\$ 10,037,234</u>

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

	Beginning Balance January 1, 2021	Additions	Reductions	Ending Balance December 31, 2021	Amounts Due Within One Year
LONG-TERM DEBT					
2021 Direct placement revenue refunding bond	\$ -	\$ 18,755,000	\$ -	\$ 18,755,000	\$ 2,060,000
2019 Direct placement revenue refunding bond	32,130,000	-	800,000	31,330,000	830,000
2019 Direct placement UTGO refunding bond	28,745,000	-	300,000	28,445,000	310,000
2012 UTGO refunding bonds	13,939,893	-	3,775,197	10,164,696	3,795,000
2013 Revenue and refunding bonds - series A	20,846,039	-	20,846,039	-	-
2016 Revenue and refunding bonds	61,563,734	-	2,090,667	59,473,067	1,840,000
Other notes payable	2,163,554	255,269	809,786	1,609,037	698,008
Total long-term debt	159,388,220	19,010,269	28,621,689	149,776,800	9,533,008
ESTIMATED PROFESSIONAL LIABILITY	6,420,712	362,314	-	6,783,026	-
Total noncurrent liabilities	\$ 165,808,932	\$ 19,372,583	\$ 28,621,689	\$ 156,559,826	\$ 9,533,008

Annual debt service requirements to maturity for long-term debt are as follows:

Year Ending December 31,	Bonds and Notes Payable			Direct Placement Bonds		
	Principal	Interest	Total	Principal	Interest	Total
2023	\$ 6,637,234	\$ 2,722,015	\$ 9,359,249	\$ 3,400,000	\$ 1,870,214	\$ 5,270,214
2024	4,365,400	2,415,950	6,781,350	5,960,000	1,731,801	7,691,801
2025	4,310,000	2,246,400	6,556,400	6,270,000	1,610,442	7,880,442
2026	4,450,911	2,074,500	6,525,411	6,585,000	1,483,028	8,068,028
2027	4,605,000	1,897,000	6,502,000	6,905,000	1,349,454	8,254,454
2028–2032	26,700,000	5,794,250	32,494,250	12,055,000	5,252,532	17,307,532
2033–2037	6,633,366	1,325,500	7,958,866	34,155,000	2,506,224	36,661,224
Total	57,701,911	\$ 18,475,615	\$ 76,177,526	\$ 75,330,000	\$ 15,803,695	\$ 91,133,695
Net unamortized premiums and discounts	6,576,898					
	<u>\$ 64,278,809</u>					

Annual debt service is calculated assuming conversion of the 2019 direct placement UTGO refunding bond and the 2021 direct placement revenue refunding bond to tax-exempt bonds.

Note 9 – Deferred Compensation and Pension Plans

The District has a deferred compensation plan and pension plans created in accordance with Internal Revenue Code §457(b), §401(a), and §414(h). The plans are available to eligible employees and collectively provide for District matching contributions of a maximum of 9% of the employee's gross compensation earned in the prior year. Current District policy is to fund contributions. Plan provisions and contribution requirements are established by the District and may be amended by the District's Board of Commissioners.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Under the §401(a) plan, the District makes contributions on behalf of eligible employees based upon funding levels ranging from 4% to 9% of an employee's gross earnings plus an additional 1/10 of 1% for each year of the first 10 years of credited service. The District contributes up to 9% not to exceed the maximum federal amount for the year. Employees are not allowed to contribute to the §401(a) plan. All employee contributions are made to the §457(b) plan.

The §457(b) plan is available to eligible employees and permits them to defer a portion of their salary until withdrawn in future years. The deferred compensation is not available to employees until termination, retirement, death, or an unforeseeable emergency.

The §414(h) plan allows a limited group of employees to make an irrevocable election prior to the beginning of the plan year. The maximum contribution is the §415 limit minus any employer §401(a) contributions. These pick-up contributions are completely voluntary and are in addition to any District contributions made to the §401(a) plan and any contributions that are made to the §457(b) deferred compensation plan. Generally, the benefits may only be distributed at termination of employment or death.

The District has limited administrative involvement and does not perform the investing function for the plans. The District does not hold the assets of the plans in a trustee capacity and does not perform fiduciary accountability for the plans. Therefore, the District employees' deferred compensation plans are not reported on the financial statements of the District.

The District's contributions to the employee benefit plans totaled \$10,569,657 and \$10,155,533 during the years ended December 31, 2022 and 2021, respectively. Contributions made by employees to the benefit plans totaled \$13,776,568 and \$12,951,981 during the years ended December 31, 2022 and 2021, respectively. For more information on the retirement plans, contact the District's director of human resources.

Note 10 – Property Taxes

The county treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities. Taxes are levied annually on January 1 on property values listed as of the prior May 31. Assessed values are established by the county assessor at 100% of fair market value. A revaluation of all property is required every four years.

Taxes are due in two equal installments on April 30 and October 31. Collections are distributed monthly to the District by the county treasurer.

The District is permitted by law to levy up to \$0.75 per \$1,000 of assessed valuation for general district purposes. As the District has never established a regular tax levy, any future regular levy would require voter approval. The Washington State Constitution and Washington State law, RCW 84.55.010, limit the rate. The District may also levy taxes at a lower rate. Further amounts of tax need to be authorized by the vote of the people.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

For 2022 and 2021, the District did not have a regular tax levy. There is a voter-approved tax levy for service of the unlimited tax general obligation bonds. For the years ended December 31, 2022 and 2021, the tax levy for bond service was \$0.72 and \$0.77 per \$1,000 on a total assessed valuation of \$6,935,091,770 and \$6,128,101,353, for a total levy of \$4,992,567 and \$4,713,997, respectively. The District also receives revenue from timber taxes. Timber tax revenue during the years ended December 31, 2022 and 2021, was \$43,883 and \$58,635, respectively.

Property taxes are recorded as receivables when levied. Because state law allows for sale of property for failure to pay taxes, no estimate of uncollectible taxes is made.

Note 11 – Postemployment Benefits Other Than Pensions (OPEB)

General information about the OPEB Plan

Termination of participation in PEBB – Beginning January 1, 2021, the District no longer participates in the Public Employees Benefits Board (PEBB) Program for post-employment benefits. This resulted in a \$28,435,601 gain on termination of participation in PEBB due to a \$30,730,533 decrease in the OPEB liability, \$7,706,233 decrease in deferred outflows of resources, and a \$5,411,301 decrease in deferred inflows of resources in January 2021.

Plan description – Effective January 1, 2021, there is the early retirement medical benefit program. The District will pay the full premium for retirees with 20 or more years of service between the ages of 62 and 65. The fully insured plans offered are from Premera. Retiree's spouses may enroll until they are age 65 and have to pay the spouse portion of the premium. No assets are accumulated in a trust that meets the criteria in paragraph 4 of GASB 75.

Eligibility – Employees are eligible for retiree health benefits if they retire between ages 62 and 65 and have 20 or more years of service. Employees in “pay-in-lieu of benefits, <0.50 FTE, Per Diem and/or temporary” FTE status are not entitled to retirement benefits.

Benefits provided – The benefits provided by the District and valued in this report include premium reimbursement. Eligible employees receive full reimbursement for the retiree portion of medical premiums. There is no reimbursement for dental premiums or the dependent portion of medical premiums, nor spousal or dependent premiums. Medical premiums of retirees and spouses over the age of 65 are not reimbursed.

GASB 75 requires the projection of the total cost of benefit payments to be based on claims costs or age adjusted premiums approximating claims costs. Because claims costs are expected to vary by age and sex, we have used claims costs that vary by age and sex. The projection of retiree premiums is based on current amounts for the retirees' premium, projected with the medical trend assumption.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Membership data – At December 31, 2022 and 2021, the following membership census was used:

	2022	2021
Membership census		
Retirees	17	17
Actives	1,978	1,978
	1,995	1,995

Individuals covered by benefit terms – At December 31, 2022 and 2021, the following retirees and spouses were covered by the benefit terms:

	2022	2021
Retirees and spouses currently receiving benefits		
Members	17	17
Surviving Spouses	-	-
Spouses	2	2

Total OPEB liability

The District's total OPEB liability was \$5,724,482 and \$5,371,600 as of the reporting date of December 31, 2022 and 2021, respectively. The corresponding measurement date was December 31, 2021 and 2020, respectively, and the actuarial valuation date was July 1, 2020. GASB 75 allows a lag of up to one year between the measurement date and the reporting date. No adjustment is required between the measurement date and the reporting date.

Actuarial assumptions and other inputs – The total OPEB liability in the December 31, 2022, actuarial valuation was determined using the following actuarial assumptions and other inputs, applied to all periods included in the measurement, unless otherwise specified:

Inflation	2.75%
Salary increases	3.50% and promotion and longevity increases ranging from 6% at 0 years of service to 0% at 21+ years of service

Even though the benefits are not based upon pay, salary assumptions are necessary for the actuarial cost method. These assumptions are for promotion and longevity and reflect the assumptions used in the 2020 actuarial valuation for Washington State Public Employees Retirement System (PERS).

Healthcare cost trend rates	Ranging from 8.90% beginning 7/1/2021 to 4.20% beginning 7/1/2087 and plus
-----------------------------	--

There is substantial uncertainty regarding the impact of the COVID-19 pandemic on projected plan costs. Therefore, for purposes of this valuation, no adjustments were made to these costs. The COVID-19 pandemic could have a material cost impact in future valuations.

Discount Rate (Liabilities)	2.06%
-----------------------------	-------

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

The discount rate was based on the Bond Buyer General Obligation 20-bond municipal bond index for bonds that mature in 20 years. GASB 75 requires that the discount rate be based on a 20-year high quality (AA/Aa or higher) municipal bond rate.

Demographic assumptions regarding retirement, mortality, disability mortality, turnover, and marriage are based on assumptions used in the 2020 actuarial valuation for the Washington State retirement systems and modified for the District.

- The assumed rates of disability under PERS plan 2 from the 2020 actuarial valuation are less than 0.1% for ages 50 and below and continue to be low after that. An assumption of a 0% disability rate for all ages was used.
- For service retirement, the PERS plan 2, with less than 30 years of service assumptions, from the 2020 actuarial valuation for Washington State retirement systems was used. The service requirements for these plans vary based on hire date and years of service. An assumption of 100% retirement at age 65 was used so that the attribution period under the actuarial cost method ends when the benefits end, as stated in A 4.383 of the implementation guide for GASB 75.
- For mortality, the assumptions from the 2020 actuarial valuation for Washington State retirement systems, adjusted for the District was used. For all healthy members, the PubG.H-2010 base mortality table with generational mortality adjustments using the long-term MP-2017 generational improvement scale was used.
- For other termination of employment, the assumptions by plan from the 2020 actuarial valuation for Washington State retirement systems were used, but no less than 2% per year.

The actuarial assumptions used for the December 31, 2022 reporting were based on a census date of July 1, 2020.

Changes in the total OPEB liability

Balance at December 31, 2020	\$ 30,730,533
Changes of benefit terms (termination of participation in PEBB)	<u>(25,358,933)</u>
Balance at December 31, 2021	<u>5,371,600</u>
Service cost	501,919
Interest	121,340
Effect of assumption changes or inputs	31,104
Benefit payments	<u>(301,481)</u>
Net Changes	<u>352,882</u>
Balance at December 31, 2022	<u><u>\$ 5,724,482</u></u>

Changes of assumptions and other inputs reflect a change in the discount rate from 2.74% in 2020 to 2.12% in 2021 and 2.06% in 2022.

Public Hospital District No. 1 of Skagit County, Washington
Notes to Financial Statements

Sensitivity of the total OPEB liability to changes in the discount rate – The following presents the total OPEB liability of the District, as well as what the District's total OPEB liability would be if it were calculated using a discount rate that is one percentage point lower or one percentage point higher than the current discount rate:

	<u>1% Decrease (1.06%)</u>	<u>Discount Rate (2.06%)</u>	<u>1% Increase (3.06%)</u>
2022			
Total OPEB liability	<u>\$ 6,215,741</u>	<u>\$ 5,724,482</u>	<u>\$ 5,260,919</u>
2021			
Total OPEB liability	<u>\$ 5,817,257</u>	<u>\$ 5,371,600</u>	<u>\$ 4,950,669</u>

Sensitivity of the total OPEB liability to changes in the healthcare cost trend rates – The following presents the total OPEB liability of the District, as well as what the District's total OPEB liability would be if it were calculated using healthcare cost trend rates that are one percentage point lower or one percentage point higher than the current healthcare cost trend rates:

	<u>1% Decrease</u>	<u>Healthcare Cost Trend Rates</u>	<u>1% Increase</u>
2022			
Total OPEB liability	<u>\$ 4,918,245</u>	<u>\$ 5,724,482</u>	<u>\$ 6,715,444</u>
2021			
Total OPEB liability	<u>\$ 4,684,885</u>	<u>\$ 5,371,600</u>	<u>\$ 6,209,782</u>

OPEB expense and deferred outflows of resources and deferred inflows of resources related to OPEB

For the years ended December 31, 2022 and 2021, the District recognized OPEB expense of \$5,724,482 and \$5,371,600, respectively, which was included in Employee Benefits in the Statements of Revenues, Expenses, and Changes in Net Position.

The District reported deferred outflows of resources related to OPEB from the following sources as of December 31:

	<u>Deferred Outflows of Resources</u>
2022	
Changes of assumptions or other inputs	\$ 27,930

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Note 12 – Professional Liability Insurance

The District has purchased professional liability insurance from Physicians Insurance (PI) on a claims-made basis in the amount of \$1,000,000 per occurrence, with a \$5,000,000 annual aggregate limit. The District has a retention of \$100,000 per claim with an aggregate retention of \$300,000. PI, together with MedPro and AIG, also provides excess coverage on a claims-made basis in the amount of \$45,000,000 per occurrence, with a \$49,000,000 annual aggregate limit. The District accrues an actuarial estimate of the expected value of losses and related expenses for unreported incidents and claims on an occurrence basis which was \$7,435,531 and \$6,783,026 at December 31, 2022 and 2021, respectively.

Note 13 – Joint Venture Transactions

The District provides services, including accounting, management, and ancillary services, to the joint ventures (Note 7). The District was reimbursed approximately \$23,559,000 and \$21,778,000 in expenses related to these services for the years ended December 31, 2022 and 2021, respectively.

As of December 31, 2022 and 2021, the District had a total of approximately \$2,487,000 and \$1,611,000, respectively, in accounts receivable from joint ventures.

The joint ventures provide various services to the District (Note 7). The District paid approximately \$16,466,000 and \$15,562,000 to the joint ventures for providing these services for the years ended December 31, 2022 and 2021, respectively.

As of December 31, 2022 and 2021, the District had a total of approximately \$1,149,000 and \$1,014,000, respectively, in accounts payable to joint ventures.

Note 14 – Concentrations of Credit Risk

The District grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of net receivables from patients and third-party payors at December 31, 2022 and 2021, was as follows:

	2022	2021
Medicare	36%	34%
Medicaid	11%	10%
Group Health	5%	6%
Patient and self-pay	0%	0%
Commercial	34%	35%
Other third-party payors	14%	15%
	100%	100%

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Note 15 – Commitments and Contingencies

Litigation – This District is a defendant in a putative class-action lawsuit filed by a former employee of the District, who alleges that the District's electronic timekeeping system rounds certain time increments in a way that results in hourly employees at the District's hospital facilities being underpaid in certain circumstances for regular wages and overtime pay. The District contests plaintiff's claims and is defending the lawsuit, which is in the pre-class certification procedural phase. No trial date has been set. Lawsuits alleging similar claims have been filed against other healthcare employers, with most resulting in court-approved settlements. Based on the ranges of other court-approved settlements involving similar claims, and the potential for this case to go to trial on plaintiff's alleged claims if no settlement could be reached, the District has established a reserve based on an estimate of plaintiff's claim for damages and fees against the District.

The District is also involved in litigation and regulatory investigations arising in the course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material adverse effect on the District's future financial position or results from operations.

Compliance with laws and regulations – The health care industry is subject to numerous laws and regulations from 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 Medicaid fraud and abuse. Government activity with respect to investigations and allegations regarding possible violations of these laws and regulations by health care providers, including those related to medical necessity, coding, and billing for services, has increased substantially. Violations of these laws and regulations could result in expulsion from government health care programs, together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the District is in compliance with the fraud and abuse regulations, as well as other applicable government laws and regulations. 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 16 – Collective Bargaining Agreements

At December 31, 2022, the District had a total of approximately 2,469 employees. Of this total, 1,718 employees are covered by collective bargaining agreements. There are no collective bargaining agreements that expire during 2023. The District does not anticipate any significant interruptions as a result of negotiations surrounding the collective bargaining agreement.

Public Hospital District No. 1 of Skagit County, Washington

Notes to Financial Statements

Note 17 – COVID-19 Pandemic

The global crisis resulting from the spread of COVID-19 had a substantial impact on the District's operations during the years ended December 31, 2022 and 2021. Management cannot currently estimate the duration of the impact of the COVID-19 pandemic on the organization; neither are they able to predict how the pandemic will evolve nor how various government entities will respond to its evolution. Should the District's business be subject to reduced capacity or should closures occur, operations would be adversely affected. Even without government orders, patients may choose to postpone or decline elective care. Ongoing material adverse impacts from the COVID-19 pandemic could result in reduced revenue and cash flow.

In April 2020, the District applied for and received advances from the Medicare under the Medicare Accelerated and Advance Payment Program, administered by Centers for Medicare & Medicaid Services, of \$44,059,888. This amount was treated as an advance liability bearing no interest, with a recoupment period that was originally scheduled to begin 120 days following receipt of the accelerated payments. On September 30, 2020, a new funding bill was enacted which delayed recoupment of such funds. The finalized funding bill gave hospitals one year before Medicare could claim payments to repay the advance payments. Additionally, the measure lowered the interest rate on outstanding payments after the 29-month period from 10.25% to 4%. The District repaid the remaining advance due in September 2021.

The District applied for expedited funding from the Federal Emergency Management Agency (FEMA) Public Assistance Program. The FEMA Public Assistance Program provides partial funding for costs related to emergency protective measures conducted as a result of the COVID-19 pandemic. This grant is meant to offset incremental expenses incurred as a result of the COVID-19 pandemic. This funding channel allows for an organization to receive 50% of estimated expenses prior to project close (after removing a 25% state cost share requirement). The District recognized \$1,551,209 and \$270,493 during the years ended December 31, 2022 and 2021, respectively, as non-operating revenue on the Statements of Revenues, Expenses, and Changes in Net Position.

During the years ended December 31, 2022 and 2021, the District received funds under the CARES Act Provider Relief Fund, administered by the U.S. Department of Health & Human Services (HHS), of \$0 and \$4,352,645, respectively. The District has recognized the amounts received as nonoperating revenue on the Statements of Revenues, Expenses, and Changes in Net Position during the year ended December 31, 2021. The District was required to agree to the terms and conditions associated with the funds. Those terms and conditions include measures to prevent fraud and misuse. Documentation is required to ensure that these funds are to be used for expenses or lost revenue attributable to COVID-19. Also, anti-fraud monitoring and auditing will be done by HHS and the Office of the Inspector General. HHS may issue more specific guidance in the future on how the lost revenue and expenses should be calculated, which may result in modification to management's estimates in future periods.

Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Commissioners
Public Hospital District No. 1 of Skagit County, Washington

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Public Hospital District No. 1 of Skagit County, Washington as of and for the year ended December 31, 2022, and the related notes to the financial statements, which collectively comprise Public Hospital District No. 1 of Skagit County, Washington's basic financial statements, and have issued our report thereon dated April 21, 2023.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Public Hospital District No. 1 of Skagit County, Washington's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Public Hospital District No. 1 of Skagit County, Washington's internal control. Accordingly, we do not express an opinion on the effectiveness of Public Hospital District No. 1 of Skagit County, Washington's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that were not identified.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether Public Hospital District No. 1 of Skagit County, Washington's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

A handwritten signature in cursive script that reads "Moss Adams LLP".

Everett, Washington
April 21, 2023

Required Supplementary Information

Public Hospital District No. 1 of Skagit County, Washington
Schedule of Changes in Total Other Post-Employment Benefits
and Related Ratios
December 31, 2022

	<u>2022</u>	<u>2021</u>	<u>2020</u>	<u>2019</u>	<u>2018</u>
Total OPEB liability					
Service cost	\$ 501,919	\$ -	\$ 1,992,258	\$ 2,656,838	\$ 2,322,431
Interest	121,340	-	1,013,604	893,888	800,469
Changes of benefit terms (termination of participation in PEBB)	-	(25,358,933)	-	-	-
Effect of economic/demographic gains/(losses)	-	-	-	2,176,604	-
Effect of assumption changes or inputs	31,104	-	5,229,798	(5,956,536)	1,628,431
Benefit payments	(301,481)	-	(465,133)	(275,776)	(278,124)
Net change in total OPEB liability	352,882	(25,358,933)	7,770,527	(504,982)	4,473,207
Total OPEB liability - beginning	5,371,600	30,730,533	22,960,006	23,464,988	18,991,781
Total OPEB liability - ending	<u>\$ 5,724,482</u>	<u>\$ 5,371,600</u>	<u>\$ 30,730,533</u>	<u>\$ 22,960,006</u>	<u>\$ 23,464,988</u>
Covered-employee payroll	<u>\$ 171,581,416</u>	<u>\$ 155,906,296</u>	<u>\$ 158,595,040</u>	<u>\$ 154,175,746</u>	<u>\$ 170,215,023</u>
Total OPEB liability as a percentage of covered-employee payroll	<u>3.34%</u>	<u>3.45%</u>	<u>19.38%</u>	<u>14.89%</u>	<u>13.79%</u>
	<u>2017</u>				
Total OPEB liability					
Service cost	\$ 2,377,362				
Interest	688,677				
Changes of benefit terms	-				
Effect of economic/demographic gains/(losses)	-				
Effect of assumption changes or inputs	(852,947)				
Benefit payments	(266,904)				
Net change in total OPEB liability	1,946,188				
Total OPEB liability - beginning	17,045,593				
Total OPEB liability - ending	<u>\$ 18,991,781</u>				
Covered-employee payroll	<u>\$ 150,792,481</u>				
Total OPEB liability as a percentage of covered-employee payroll	<u>12.59%</u>				

*This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, the District will present information for available years.

See report of independent auditors.

Public Hospital District No. 1 of Skagit County, Washington
Schedule of Changes in Total Other Post-Employment Benefits
and Related Ratios
December 31, 2022

Changes in benefit terms – The District left the PEBB Program on December 31, 2020. Effective January 1, 2021, there is the early retirement medical benefit program. The District will pay the full premium for retirees with 20 or more years of service between the ages of 62 and 65. The fully insured plans offered are from Premera. Retiree's spouses may enroll until they are age 65 and have to pay the spouse portion of the premium.

Changes of assumptions – Changes of assumptions and other inputs reflect the effects of changes in the discount rate, election, demographic and health assumptions each period.

